



# **STUDY OF THE NATIONAL ECONOMY 2005**

**Guatemala, June 2006**



## INDEX

	<b>No.</b>
<b>I. GENERAL ASPECTS</b>	<b>1</b>
A. THE INTERNATIONAL ECONOMIC SCENARIO	1
1. Advanced economies	2
2. Other economies with emerging markets and developing countries	2
B. THE NATIONAL ECONOMY	5
1. The real sector	5
2. The foreign sector	7
3. The fiscal sector	8
4. The monetary sector	9
<b>II. THE INTERNATIONAL ECONOMY</b>	<b>12</b>
A. GENERAL SCENE	12
B. ADVANCED ECONOMIES	13
C. OTHER ECONOMIES WITH EMERGING MARKETS AND DEVELOPING COUNTRIES	23
<b>III. THE NATIONAL ECONOMIC ACTIVITY</b>	<b>35</b>
A. GENERAL STATEMENTS	35
B. GROSS DOMESTIC PRODUCT PER EXPENDITURE	36
C. GROSS DOMESTIC PRODUCT PER ECONOMIC BRANCHES	38
D. BEHAVIOR OF DOMESTIC PRICES	44
1. Consumer Price Index -CPI-	44
2. Hidden inflation	49
3. Imported inflation	50
<b>IV. BALANCE OF INTERNATIONAL PAYMENTS</b>	<b>53</b>



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A. GENERAL STATEMENTS	53
B. PAYMENT BALANCE	54
1. Current Operations	54
a) Exports	54
b) Imports	58
c) Commercial balance	59
d) Services and transfers	60
2. Operations of capital	61
3. International Monetary Reserves	62
C. NOMINAL EXCHANGE RATE	63
D. REAL EXCHANGE RATE	65
E. FOREIGN PUBLIC DEBT	66
F. SUSTAINABILITY OF THE PUBLIC FOREIGN DEBT	68
<b>V. MONETARY AND FINANCIAL SITUATION</b>	<b>70</b>
A. GENERAL STATEMENTS OF THE MONETARY POLICY	70
B. EVOLUTION OF THE MAIN MONETARY AGGREGATES	72
C. CREDIT ACTIVITY OF THE <i>BANCO DE GUATEMALA</i>	77
D. CREDIT OF THE BANKS AND FINANCIAL STOCK COMPANIES TO THE PRIVATE SECTOR	79
E. BANKING CASH	80
F. INTEREST RATES	81
1. In national currency	81
2. In foreign currency	84
G. OPERATIONS OF MONETARY STABILIZATION	85
1. In national currency	85
2. In foreign currency	87
H. BALANCE ACCOUNTS OF THE BANKS OF THE SYSTEM	88
I. LEGAL AND IMMEDIATE CAPACITY OF CREDIT EXPANSION OF THE BANKS OF THE SYSTEM	88
J. BANKING INSTITUTIONS	90
K. BALANCE ACCOUNTS OF THE FINANCIAL STOCK COMPANIES	90



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L. FINANCIAL GROUPS	91
M. OFF-SHORE ENTITIES	94
N. ADVANCES IN THE STRENGTHENING PROCESS OF THE NATIONAL FINANCIAL SYSTEM	97
1. Financial groups	97
2. Banking system	97
3. Strengthening of the banking security network	99
O. DUE AND DEFAULT PORTFOLIO	99
P. IMPRODUCTIVE ASSETS	101
<b>VI. PUBLIC FINANCES</b>	<b>104</b>
A. GENERAL BUDGET STATEMENTS	104
B. BUDGET EXECUTION	104
C. INCOME	107
D. EXPENDITURES	110
1. Expenses according to the type of program and specific objective	111
2. Expenses per institutional destination	112
3. Expenses according to nature	112
a) Operation Expenses	112
b) Capital Expenses	113
E. FISCAL CASH	114
F. DEBT OF THE PUBLIC SECTOR	115
1. Domestic public debt	115
a) Movement of the domestic public debt	115
b) Balance and distribution per domestic public debtor	116
c) Interest rate	117
2. Foreign public debt	118
G. MAIN DECISIONS REGARDING PUBLIC FINANCES IN 2005	122
<b>STATISTICAL TABLES</b>	



## I. GENERAL ASPECTS

### A. THE INTERNATIONAL ECONOMIC SCENARIO

According to the International Monetary Fund -IMF<sup>1</sup>, in 2005 the world GDP increased by 4.8% (5.3% in 2004); this growth was due to favorable conditions of the financial markets, as well as to adaptable macroeconomic policies. The growth of the global economy in 2005 continued exceeding the expectations, due, among others, to the following factors: increase in the industrial production; dynamism of the services sector; world trade growth; improvement of consumer confidence; stability of the working market; and, increase of investors' confidence.

Regarding inflation in 2005, the inflationary pressures remained under control, as a result of the implementation of disciplined monetary policies, even though high oil prices were observed and that new natural disasters occurred. On the other hand, in 2005, the inflation in the advanced economies registered rates higher than the ones in the previous year, while being of 2.3% (2.0% in 2004). It is important to mention that Japan was the only country that registered deflation, varying the inflationary rate in -0.3%, lower than the inflation rate observed in 2004, close to zero.

Regarding the group of countries with emerging and developing economies, the inflation was of 5.4%; lower than the rate registered the previous year (5.7%). It is important to mention that in the People's Republic of China a reduction of 2.1 percentage points was observed in the inflation rate, from 3.9% in 2004 to 1.8% in 2005. In the European countries with emerging economies, the inflation was reduced to 4.9% (6.2% in 2004), while the Community of Independent States registered an inflation rate of 12.3%, percentage higher than the observed in 2004 (10.3%).

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<sup>1</sup> Perspectives of the World Economy, April, 2006, IMF.



## **1. Advanced Economies**

In 2005 the advanced economies reached a growth rate of real production of 2.7%, lower than the one of the previous year (3.3%).

In the United States of America, the GDP registered a growth rate of 3.5%, lower by 0.7 percentage points than the observed in 2004 (4.2%). The reduction in the growth of this economy was influenced, among other factors, by the deceleration in private consumption, caused, on one hand, by the fall in the sale of automobiles and, on the other hand, by the high prices of gas caused by the damage caused by hurricane Katrina to the oil infrastructure of the Gulf of Mexico. Regarding the current account of the payment balance in the United States of America, the deficit continued increasing being placed at 6.4% of the GDP in 2005 (5.7% en 2004), which contrasts with the surplus registered in the oil exporting countries, People's Republic of China, Japan and other economies with emerging markets in Asia. It is important to indicate that the referred deficit was financed through the income of foreign capitals induced by the positive differentials between the domestic and foreign interest rates, as well as by the high rates of net savings of the North American corporations.

The economy of Japan grew 2.7% in 2005 (2.3% in 2004). Said growth was associated, on one hand, with the strong demand of Japanese products from the United States of America and the People's Republic of China, associated with the depreciation of the *yen* and, on the other hand, with the increasing influence of domestic demand, which was due to the increase of employment, to the utilities generated by the corporation and to the expansion of the growth of the banking credit to the private sector.

## **2. Other economies with emerging markets and developing countries**

The countries of the group of other economies with emerging markets and developing countries, reached an economic growth rate of 7.2% in 2005, percentage slightly higher than the one of the previous year (7.6%). It is important to indicate that the growth rate within said group of countries, as in the previous year, was unequal. In effect, the emerging economies of Asia registered an



average economic growth of 8.6%, the People's Republic of China and India standing out; with growth rates higher than the referred average. The People's Republic of China, for the fifth consecutive year continued showing a strong economic growth (9.9% in 2005), which is mainly associated with its net exports, as a result of its higher investment rates. While in India, the growth of the real production of 8.3% in 2005 is explained by the dynamism shown by the manufacturer and services sectors. In contrast, the developing countries of Africa, jointly, reached a growth of 5.2%, lower than the percentage registered in 2004 (5.5%). In Latin America and the Caribbean the economic growth rate was of 4.3% in 2005, lower than the one of 2004 (5.9%)<sup>2</sup>.

Said increase is based on the dynamism shown by investment as well as by exports. On the other hand, public finances were impelled by the increase of the economic activity rates and by the high prices of some basic export products. Said situation contributed in generating better relations of the public debt rate regarding the gross domestic product and the international monetary reserves regarding the export of goods and services, which generated a lower foreign vulnerability for the region. It is important to mention that the economic growth of the region in 2005 highlights the evolution of South-America's economies, particularly, from Venezuela, which registered a growth rate of 9.0%; Argentina 8.6%; Peru 6.0%; and Chile 6%; and, in a lower proportion, the economies of the Caribbean that showed an average growth rate of 4.1%, due to the increase in investment and exports, in the world growth environment, impelled by the economies of the United States of America and the People's Republic of China. On the other hand, Mexico and Central America grew but at a lower rhythm, of 3.0% and 3.6%, respectively

Regarding the domestic prices at a Latin American rate, the inflation remained relatively controlled in most of the countries; notwithstanding, the increase in international oil prices. In effect, the average inflationary rate in 2005 was of 6.3% (7.4% in 2004). However, in some countries, the prices' growth continued being high, as in Haiti (16.8%), Jamaica (16.5%), Venezuela (15.9%) and Costa Rica (13.6%), while in other countries the inflation was of only one digit.

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<sup>2</sup> Preliminary balance of the Latin American and Caribbean Economies. *Comisión Económica para América Latina y el Caribe -CEPAL-* 2005.



In 2005, the countries of Central and Eastern Europe showed, as an average, an economic growth rate of 5.3%, lower than the one observed in 2004 (6.5%). Said result is associated with the impulse of the domestic demand and with the dynamic observed in exportation.

The countries of the Community of Independent States in 2005 showed an economic growth of 6.5% (8.4% in 2004). This behavior is explained by the lower impulse of the energetic sector in Russia and Kazakhstan, as well as by the political uncertainty in Ukraine, and Republic of Kirgizstan and Russia. The Middle East region grew 5.9% in 2005 (5.4% in 2004), behavior mainly associated with the economic growth in the oil exporter countries, due to the high oil prices and, in the countries that do not produce oil, due to the positive impact of the economic reforms implemented in certain countries.

Finally, in the countries of the African continent, the economic activity grew, as an average, 5.2% in 2005 (5.5% in 2004). Said increase was due to the strengthening of the economy of the Southern Sahara's countries, which showed an economic growth rate of 5.5%. Other factors that positively influenced in the economic development of the region were the increase in the prices of metals, which favored South Africa and, the positive effects of the economic reforms implemented in Ethiopia, Mozambique and Sierra Leone.

## **B. THE NATIONAL ECONOMY**

### **1. The real sector**

The deceleration that the growth rate of the national economic activity showed since 1999 was reverted in 2004, trend that continued in 2005. In effect, the economic growth, measured by the Real Term Gross Domestic Product –GDP- registered a growth of 3.2%, higher by 0.5 percentage points than the rate registered in 2004 (2.7%). The performance of the national economy was influenced by foreign and domestic factors. Among the foreign factors are, first, the positive effect on the national economy by the favorable developing registered by the economy of the United States of America, which in 2005 grew above the average growth rate observed by the advanced economies (2.7%); second, the



economies growth of the rest of the main countries that are commercial associates of Guatemala<sup>3</sup>; and, third, the recovery in the international prices of some export products (coffee and sugar)<sup>4</sup>. It is important to mention that though the international oil price, for the second consecutive year, has been an adverse factor for the national productive activity, the impulse that the world economy continued showing, mainly due to the economic growth of the United States of America and the People's Republic of China, supported the growth of the Guatemalan economy. In that sense, it was observed that the impact of the international oil price increase was transferred to the general level of prices and did not affect the national economic activity.

The domestic factors that favored the positive evolution of the national economy is the maintenance of macroeconomic stability and the lower incidence of adverse extra-economic factors, especially, the invaluable effect that tropical storm Stan had in the country's production flow.

In the described context, it is important to mention that in 2005 most of the productive sectors registered a positive behavior, except exploitation of mines and quarries sector and public administration and defense.

On the other hand, the sectors that showed more dynamic growth rates were: manufacturing industry; construction; and, banking, insurance and real estate. Regarding the GDP variables per expenditure, in real terms, in 2005, acceleration was seen in the observed growth in most of the components of global demand. In effect, private consumption, variable with the highest weighting in the GDP structure (81.9%), registered a growth of 4.3%, higher by 0.5 percentage points than the one observed in 2004 (3.8%); this behavior is associated with the macroeconomic stability, with the higher dynamism of the productive activity and with the reception of a higher amount of family remittances. Regarding public consumption, that includes remuneration and purchase of goods and services of the general government, this registered a fall of 1.4% (-10.1% in 2004). This result

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<sup>3</sup> According to estimations of the International Monetary Fund –IMF- in 2005 the economy of the United States of America grew 3.5%; Mexico's 3.0%; El Salvador's 2.0%; Honduras' 4.2%; Costa Rica's 3.2%; and Nicaragua's 3.5%.

<sup>4</sup> In the case of coffee, the average export price per quintal increased from US\$72.54 in 2004 to US\$105.83 in 2005; while the average export price per quintal of sugar increased from US\$7.49 in 2004 to US\$8.45 in 2005.



is associated with the higher execution rate of the central government's operating expenditure observed during 2005.

Regarding the gross geographical formation of fixed capital, it showed an increase of 12.5%, as a result of a positive variation of 11.7% in the private gross geographical formation and of an increase of 16.4% in the public gross geographical formation. In the result of the private gross geographical formation that represented 82.8% of the total gross geographical formation mainly influenced the growth of private construction, as well as the increase of imported capital goods. The public gross geographical formation was influenced by the increase in the purchase of machinery and equipment and by the increase in the construction of roads and public works.

Regarding foreign demand, the export of goods and services registered a fall in 2005, in real terms, of 1.0% (growth of 6.5% in 2004), behavior mainly associated with a reduction in the exported volume of coffee, as well as in the value of services, in real terms. Regarding foreign offer, the import of goods and services showed a growth of 1.4% in real terms, lower than the observed the previous year (7.2%). It is important to indicate that this behavior is mainly associated with the lower dynamism of imports, in North American dollars, consumption goods; basic goods and intermediate products, and capital goods, which grew in 7.2% (13.2% in 2004), 4.4% (18.2% in 2004) and 11.6% (16.5% in 2004), respectively.

## **2. The foreign sector**

In the context of the referred international economic scenario, in 2005 the payment balance registered an increase of international net monetary reserves of US\$254.4 million; this result was determined by a surplus of US\$1,641.7 million in the capital account, which allow financing the deficit in the current account of US\$1,387.3 million which caused the relation current account/GDP to remain at 4.4%, equal to the observed in 2004.

The balance of the current account is explained by the deficit of the commercial balance of US\$5,433.8 million and by the surplus, not only of the



balance of services of US\$489.0 million, but also of the net current transfers of US\$3,557.5 million.

On the other hand, the surplus in the capital account was determined by the continuous income of capital abroad, associated with the positive expectations derived from macroeconomic stability, as well with the relatively low rates that the interest rates showed in the international financial market.

As a result of the current operations and capital of the payment balance, the international net monetary reserves were of US\$3,782.4 million, higher by US\$254.4 million than the observed to December 31<sup>st</sup>, 2004 (US\$3,528.0 million).

The rate of the net international monetary reserves that was reached is equivalent to 4.3 months of import of goods and non-factorial services (4.4 months in 2004), which indicates that the foreign position of the country in 2005 continued being favorable. Regarding the exchange rate of the *quetzal* regarding the US dollar registered a nominal appreciation of 1.8%, from Q7.75 per US\$1.00 on December 31<sup>st</sup>, 2004 to Q7.61 per US\$1.00 on December 31<sup>st</sup>, 2005. Said appreciation was mainly associated with the international phenomenon of the depreciation of the US dollar, which provided a higher income of capital to emerging economies, like Guatemala.

### **3. The fiscal sector**

Regarding public finances, the fiscal deficit to December 31<sup>st</sup>, 2005 was of Q3,593.8 million, amount higher by Q1,513.7 million than the one observed in 2004. The behavior of the referred variable was mainly due to a higher dynamism in public expenditure, which registered a relative variation of 11.6%, while the total income registered an increase of 6.2%. Consequently, the fiscal deficit/GDP relation increased from 1.0% in 2004 to 1.5% in 2005.

On the other hand, the tax collection rate during 2005 caused the tax burden to be of 9.6%.

The expenses of the central government, in 2005, were of Q28,500.5 million, higher by Q2,958.3 million (11.6%) than the registered in 2004. Said result



caused the total expenditure of the central government, as a proportion of the gross domestic product, to be of 11.8%, equal to the observed in 2004.

Regarding the funding sources of the fiscal deficit, the net domestic funding was positive in Q2,621.3 million. On the other hand, the foreign net funding was negative at Q336.8 million. It is important to indicate that the funds derived from the funding allowed the financial deficit to be of Q1,309.3 million, which reduced the availability of fiscal cash for the same amount.

Finally, regarding public debt, at the end of 2005 the balance of domestic debt of the non-financial public sector was of Q16,425.7 million equivalent to 6.8% of the GDP, higher by Q3,584.9 million than the one registered in 2004. On the other hand, the balance of the foreign public debt was of US\$3,722.9 million, equivalent to 11.8% of the GDP.

#### **4. The monetary sector**

The implementation of the monetary policy in 2005 was consistent with the efforts of advancing in the adoption of a complete scheme of explicit inflation goals, which is based on the selection of the inflation goals as a nominal anchor of the referred policy and is consolidated with the implementation of a regimen of flexible exchange rate, with the use of instruments of indirect monetary control (monetary stabilization operations, giving privilege to market decisions), as well as with the higher transparency of the operations of the Central Bank, which allowed continuing consolidating the stability and confidence in the main macroeconomic and financial variables.

It is important to indicate that in 2005 the Monetary Board determined as a monetary policy goal to place the inflation within a range of 4% and 6%. The range established as a goal for the monetary policy search to strengthen the credibility of the Central Bank and to positively influence in the expectations of the economic agents, in order to propitiate a stable scenario, so that the same can make adequate decisions regarding production, consumption, saving and investment. In the mentioned context, to December 2005 the inflationary rate was of 8.57%, lower than the one of December 2004 (9.23%). Though in 2005 the deflation process



foreseen for 2004 could be materialized consistently, the inflation rate did not increase, though the adverse incidence of exogenous factors, as well as the constant increase of the international oil price and the effect on the inflationary expectations of tropical storm Stan. In effect, during 2005 the increase in the international oil price continued being one of the main factors that explained the behavior of the inflationary rate, as in 2004. On the other hand, in the internal order, the support provided by the fiscal policy to the monetary policy was important, due to the higher deposits rate that the Central Government maintained in the *Banco de Guatemala*; the demonetizing behavior of the rest of the public sector reflected in a higher demand of CDPs of the *Banco de Guatemala*; and, the formation of positive economic growth expectations by the economic agents.

In that context, during 2005 the management of the monetary policy was oriented to take measures that allow helping in the deceleration of the inflationary rate. In that sense, the Execution Committee of the *Banco de Guatemala*, in order to moderate the inflationary expectations of the economic agents and to send a certain message regarding the compromise of the Central Bank to continue watching for the stability in the general rate of prices, increased the leading interest rate of the monetary policy during seven occasions<sup>5</sup>. Besides, in order to increase the effectiveness of the monetary policy, and according to the lineaments of the Monetary Board, actions were adopted to improve some operative procedures, oriented to advance in the complete adoption process of a monetary scheme of explicit inflation goals (Inflation Targeting).

In that sense, regarding the monetary stabilization operations, the following measures, among others, were adopted in 2005: i) establishment of a single leading interest rate for the short-term operations of monetary stabilization (LTDs up to 7 days); ii) scheduling of the Execution Committee's decisions regarding

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<sup>5</sup> The leading interest rate is the interest rate that the Central Bank recognizes for the fund-raising of CDPs to 7 day-terms. The increases in said rate were registered on February 18th (from 2.55% to 2.75%); on May 20th (from 2.75% to 3.00%); on July 22nd (from 3.00% to 3.25%); on August 19th (from 3.25% to 3.50%); on September 16<sup>th</sup> (from 3.50% to 3.75%); on November 18<sup>th</sup> (from 3.75% to 4.00%); and, on December 16<sup>th</sup> (from 4.00% to 4.25%).



changes of the leading interest rate in the next date to day 15 of each month; iii) reduction of the number of bids; and, iv) setting of quotas for the LTDs fund-raising placed for the bid mechanism.

Within the indicative or reference variables of the monetary policy, it was estimated by the end of 2004 that the payment means -M2- would increase by 2005, between 10% and 12%, in inter-annual terms; while the banking credit to the private sector should have increased between 11.5% and 13.5%. By the end of 2005, the inter-annual growth rate of M2 was of 14.7%. On the other hand, the banking credit to the private sector had an inter-annual increase of 21.4%.

Finally, the weighted average interest rates in national currency of the banking system showed a stable trend, due to the fact that from December 2004 to December 2005 the asset interest rate decreased from 13.50% to 12.67%, while the liability slightly increased from 4.54% to 4.62%.

## **II. THE INTERNATIONAL ECONOMY**

### **A. GENERAL SCENARIO**

According to the International Monetary Fund –IMF-<sup>6</sup>, in 2005 the world GDP grew at a rate of 4.8% (5.3% in 2004); this growth is due to favorable conditions of the financial markets, as well as to adaptable macroeconomic policies. The growth of the global economy in 2005 continued exceeding the expectations, due, among others, to the following factors: increase in the industrial production; dynamism of the services sector; growth of the world trade; improvement of the consumers' confidence; stability of the working market; and, increase of the investors' confidence.

The inflationary pressures in 2005 remained under control, due to the implementation of disciplined monetary policies, though the high oil prices and the effects of the natural disasters that occurred.

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<sup>6</sup> Perspectives of the World Economy, April 2006. IMF.



In the advanced economies<sup>7</sup>, in 2005 the inflation showed rates higher than the ones of the previous year, while being of 2.3% (2.0% in 2004). It is important to mention that Japan was the only country that registered deflation, placing the inflationary rate in -0.3%, lower than its inflation rate close to zero observed in 2004. On the other hand, in the Special Administrative Region of Hong Kong of the People's Republic of China, the inflation rate was of 1.1%, reverting the inflationary rate registered in 2004 (-0.4%). In the same way, Israel observed an inflation rate of 1.3%, after registering a deflation of 0.4% in 2004. Regarding the inflation in the group of countries with economies in emerging and developing markets, it was of 5.4%, lower than the registered the previous year (5.7%).

It is important to mention that in the People's Republic of China a reduction of 2.1 percentage points was observed in the inflation rate, from 3.9% in 2004 to 1.8% in 2005. On the other hand, in Indonesia an important increase in the inflationary rate was observed, being of 10.5% in 2005, higher than the observed the previous year (6.1%). In countries of Europe with economies in emerging markets the inflation was reduced, being of 4.9% (6.2% in 2004), while in the Community of Independent States an inflationary rate of 12.3% was registered, percentage higher than the observed in 2004 (10.3%).

## **B. ADVANCED ECONOMIES**

During 2005 the growth rate of the advanced economies was of 2.7%, lower than the rate of 2004 (3.3%). In the particular case of the economy of the United States of America, this grew at rhythm of 3.5%, lower in 0.7 percentage points than the observed in 2004 (4.2%). The reduction in the growth of this economy was influenced, among other factors, by the deceleration in the private consumption caused, on one hand, by the fall in the automobiles sale and, on the other hand, by damage that the hurricane Katrina caused to the petroleum infrastructure of the Gulf of Mexico.

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<sup>7</sup> The classification of countries, used by the IMF regarding groups and regions of the countries, are shown in Annex 1 of this chapter.



Regarding the current account of the payment balance in the United States of America, the deficit continued growing being placed in 6.4% of the GDP in 2005 (5.7% en 2004), which contrasts with the surplus registered in the oil exporting countries, People's Republic of China, Japan and other economies with emerging markets of Asia. It is important to indicate that the referred deficit was financed through the income of foreign capitals induced by the positive differentials between the domestic and foreign interest rates, as well as by the high rates of net savings of the North-American corporations.

In Canada, the growth rate of the GDP was of 2.9%, equal than the one registered in 2004, influenced, among others factors, by the positive effect of the exchange terms, derived from the increase in the price of its exportable products, mainly energetic; by the increase in the private consumption, which at the same time was influenced by the increase in the employment rate and in the price of the financial assets; and by the higher corporative profits that supported the increase of the private investment.

In the Eurozone, the growth rate was of 1.3%, lower than the observed in 2004 (2.1%), influenced by the lower dynamism of the economic activity during the last trimester of 2005, which is mainly explained by a reduction not only of the domestic consumption but also of the net exports. In Germany a deceleration was observed in the economic growth rate, while the GDP grew in 0.9%, percentage lower than the registered in 2004 (1.6%). This behavior was mainly caused by the fall of the private consumption. In the United Kingdom, the GDP grew in 1.8% in 2005, percentage lower than the registered in 2004 (3.1%). Said behavior was influenced by the reduction of the private consumption, associated with the application of a restrictive monetary policy and with the high prices of the energetic products. In Japan, the GDP grew in 2.7% in 2005, higher than the observed in 2004 (2.3%). Said growth was supported by the increase of the domestic demand, which, at the same time, was influenced by the increase of employment, corporative utilities and banking credit, as well as by the growth of the exports of the United States of America and People's Republic of China, stimulated by the depreciation of the *yen* regarding the North-American dollars.



TABLE 1

**ADVANCED ECONOMIES: GROWTH OF THE REAL GDP  
YEARS: 2004-2005  
(In percentages)**

COUNTRY	2004	2005
<b>TOTAL</b>	<b>3.3</b>	<b>2.7</b>
United States of America	4.2	3.5
Canada	2.9	2.9
Eurozone	2.1	1.3
Germany	1.6	0.9
France	2.1	1.4
Italy	0.9	0.1
Spain	3.1	3.4
United Kingdom	3.1	1.8
Japan	2.3	2.7
Other economies <sup>a/</sup>	4.6	3.7

<sup>a/</sup> Korea; Australia; Taiwan; Sweden; Switzerland; Special Administrative Region of Hong Kong of the People's Republic of China; Denmark; Norway; Israel; Singapore; New Zealand; Cyprus; and, Iceland.  
SOURCE: Perspectives of the World Economy April de 2006. IMF.

The advanced economies registered an inflation of 2.3%, higher than the one of 2004 (2.0%). In the United States of America the inflation rate was of 3.4% (2.7% in 2004). In Canada an increase of the inflationary rate was observed, from 1.8% in 2004 to 2.2% in 2005. Japan could not restrain its deflation which was of 0.3% in 2005, while in 2004 its inflationary rate was close to zero. In the Eurozone the inflation increased from 2.1% in 2004 to 2.2% in 2005. The countries that registered the lowest inflation rates in 2005 were: Finland 0.9%; and, Low Countries 1.5% (0.1% and 1.4% in 2004, respectively); while Greece and Spain registered higher inflation rate of 3.5% and 3.4%, respectively (3.0% and 3.1% in 2004, respectively).

TABLE 2



**ADVANCED ECONOMIES: INFLATION**  
**YEARS: 2004-2005**  
**(In percentages)**

COUNTRY	2004	2005
<b>TOTAL</b>	<b>2.0</b>	<b>2.3</b>
United States of America	2.7	3.4
Canada	1.8	2.2
Eurozone	2.1	2.2
Germany	1.8	1.9
France	2.3	1.9
Italy	2.3	2.3
Spain	3.1	3.4
United Kingdom	1.3	2.1
Japan	-- <sup>b/</sup>	-0.3
Other economies <sup>a/</sup>	1.9	2.1

<sup>a/</sup> Korea; Australia; Taiwan; Sweden; Switzerland; Special Administrative Region of Hong Kong of the People's Republic of China; Denmark; Norway; Israel; Singapore; New Zealand; Cyprus; and, Iceland

<sup>b/</sup> Percentage close to zero.

SOURCE: Perspectives of the World Economy, April 2006. IMF.

The advanced economies, for the second consecutive year experienced a decrease in the unemployment rate in 2005, placed in 6.0% (6.3% in 2004). From the main advanced economies, the United States of America, Canada, Japan and the Eurozone registered in 2005 unemployment rates of 5.1%, 6.8%, 4.4% and 8.6%, respectively. On the other hand, the United Kingdom registered an unemployment rate of 4.8%, equal to the one of 2004.



<b>COUNTRY</b>	<b>2004</b>	<b>2005</b>
<b>TOTAL</b>	<b>6.3</b>	<b>6.0</b>
United States of America	5.5	5.1
Canada	7.2	6.8
Eurozone	8.9	8.6
Germany	9.2	9.1
France	9.5	9.6
Italy	8.3	8.1
Spain	11.0	9.2
United Kingdom	4.8	4.8
Japan	4.7	4.4

SOURCE: Perspectives of the World Economy, April 2006. IMF.

In the United States of America, the Federal Reserve continued implementing measures of restrictive monetary policy. In effect, said Central Bank decided to increase the federal funds rate of 2.25% to 4.25%. On the other hand, the Bank of Canada, taking into account the growth rate of the economy and the high prices of the energetic products, decided to increase the objective interest rate from 2.50% to 3.25%. In the Eurozone, the interest rate for the main operations of refunding, through which the liquidity of the banking system is controlled, remained in 2.0% during most of the year. However, the Governmental Council of the European Central Bank, in December 2005 decided to increase said rate to 2.25%, in order to knock down the inflationary pressures. Regarding the United Kingdom, the Bank of England, taking into account the scarce dynamism of the added demand and the low investment, in 2005 reduced in 0.25 percentage points its reference interest rate, which increased from 4.75% to 4.50%.



<b>TABLE 4</b>										
<b>ADVANCES ECONOMIES: INTEREST RATES ANNUAL WEIGHTED AVERAGE PERÍOD: 2001-2005</b>										
<b>COUNTRY</b>	<b>OF SHORT-TERM</b>					<b>OF LONG-TERM</b>				
	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>
<b>AVERAGE</b>	<b>3.2</b>	<b>2.1</b>	<b>1.6</b>	<b>1.7</b>	<b>2.5</b>	<b>4.4</b>	<b>4.1</b>	<b>3.6</b>	<b>3.8</b>	<b>3.7</b>
United States of America	3.5	1.6	1.0	1.4	3.2	5.0	4.6	4.0	4.3	4.3
Canada	3.9	2.6	2.9	2.2	2.7	5.5	5.3	4.8	4.6	4.1
Eurozone	4.3	3.3	2.3	2.1	2.2	5.0	4.9	4.0	3.9	3.7
United Kingdom	5.0	4.0	3.7	4.6	4.7	5.0	4.8	4.5	4.8	4.3
Japan	-	-	-	-	-	1.3	1.3	1.0	1.5	1.4

SOURCE: Perspectives of the World Economy, April 2006. IMF.

In the main international exchange markets, the North-American dollar experimented, in 2005) an appreciation regarding the following currencies: Japanese Yen, 14.2%; pound sterling, 10.6%; and, Euro, 13.1%. However, said currency registered depreciations regarding the Canadian dollar (4.6%), as well as regarding some currencies of the other economies with emerging markets, especially from Latin America and Asia. It is important to indicate that, though the deficit in current account of the payment balance remained within the record and the dollar as indicated experimented depreciation, a higher demand of instruments denominated in North-American dollars was observed, which moderated the trend to the mentioned depreciation.



TABLE 5

**AVERAGE INTEREST RATE OF SOME CURRENCIES  
REGARDING THE NORTH-AMERICAN DOLLAR  
DECEMBER 2004 – DECEMBER 2005  
(Monetary units per North-American dollar)**

<b>MES</b>	<b>JAPANESE YEN</b>	<b>POUND STERLING</b>	<b>CANADIAN DOLLAR</b>	<b>EURO</b>
DECEMBER 2004	103.78435	0.51810	1.21770	0.74542
JANUARY 2005	103.25250	0.53235	1.22478	0.76251
FEBRUARY	104.94325	0.52986	1.23957	0.76821
MARCH	105.14286	0.52449	1.21571	0.75737
APRIL	107.25857	0.52767	1.23640	0.77296
MAY	106.73286	0.53987	1.25655	0.78889
JUNE	108.74773	0.55000	1.24167	0.82296
JULY	111.90700	0.57145	1.22333	0.83031
AUGUST	110.66091	0.55763	1.20474	0.81372
SEPTEMBER	111.05318	0.55269	1.17815	0.81595
OCTOBER	114.87950	0.56686	1.17768	0.83179
NOVEMBER	118.50690	0.57688	1.18235	0.84893
DECEMBER	118.53190	0.57277	1.16217	0.84329

SOURCE: Bloomberg

The volume of the world trade of goods and services showed a deceleration in 2005, registering a growth rate of 7.3%, lower than the observed in 2004 (10.4%), behavior that is mainly explained by the lowest dynamism of the world economy. The group of countries of advanced economies showed a lower dynamism in their exports, which increased by 5.3%, percentage lower than the observed in 2004 (8.5%). Besides, the exports of other economies with emerging markets and developing countries experimented an increase of 11.5%, lower than the growth registered in 2004 (14.6%). On the other hand, the imports of advanced economies grew in 5.8%, percentage lower than the observed in 2004 (8.9%). In the same way, the growth rate of imports of other economies with emerging markets and developing countries was of 12.4%, percentage lower than the registered in 2004 (15.8%).

Regarding the exchange terms, in the advanced economies, these registered a detriment in 2005, while showing a relative variation of -1.3% (-0.1% in



2004), result that is mainly explained by the increase in the prices of some imported goods, especially energetic. In contrast, the other economies with emerging countries and developing countries continued improving their exchange terms, while registering a relative variation of 5.0% (2.2% in 2004), due to an increase of the prices in the international market of the main export products.

<b>TABLE 6</b>		
<b>WORLD TRADE OF GOODS AND SERVICES EXCHANGE VOLUME AND TERMS YEARS: 2004-2005 (Percentage variations)</b>		
<b>CONCEPT</b>	<b>2004</b>	<b>2005</b>
<b>1. TOTAL VOLUME</b>	<b>10.4</b>	<b>7.3</b>
<b>Exports</b>		
Advanced Economies	8.5	5.3
Other economies with emerging markets and developing countries	14.6	11.5
<b>Imports</b>		
Advanced Economies	8.9	5.8
Other economies with emerging markets and developing countries	15.8	12.4
<b>2. EXCHABGE TERMS</b>		
Advanced Economies	-0.1	-1.3
Other economies with emerging markets and Developing countries	2.2	5.0

SOURCE: Perspectivas de la Economía Mundial Abril de 2006. FMI.

The advanced economies, jointly, increased significantly their deficit in current account of the payment balance, which was of US\$510.7 milliard, higher than the observed in 2004 (US\$283.9 milliard). This result was mainly influenced by the behavior of the current account of the payment balance of the United States of America, the deficit of which in 2005 was of US\$805.0 milliard, amount higher than the observed in 2004 (US\$668.1 milliard). In the United Kingdom, Italy and



France, deficits were also registered in their current accounts in 2005, which were of US\$58.1 milliard, US\$26.6 milliard and US\$27.6 milliard, respectively. On the other hand, in Canada, Germany and Japan, surplus results were observed in 2005, placed in US\$25.0 milliard, US\$114.8 milliard and US\$163.9 milliard, respectively.

<b>ADVANCED ECONOMIES: BALANCE IN CURRENT ACCOUNT OF THE PAYMENT BALANCE YEARS: 2004-2005</b>				
<b>COUNTRY</b>	<b>2004</b>		<b>2005</b>	
	<b>In milliard of US\$</b>	<b>As a percentage of the GDP</b>	<b>In milliard of US\$</b>	<b>As percentage of the GDP</b>
<b>TOTAL</b>	<b>-283.9</b>	<b>-0.9</b>	<b>-510.7</b>	<b>-1.5</b>
United States of America	-668.1	-5.7	-805.0	-6.4
Canada	22.2	2.2	25.0	2.2
Eurozone	75.2	0.8	2.5	--
Germany	101.7	3.7	114.8	4.1
France	-8.4	-0.4	-27.6	-1.3
Italy	-15.1	-0.9	-26.6	-1.5
Spain	-55.3	-5.3	-85.9	-7.6
United Kingdom	-43.2	-2.0	-58.1	-2.6
Japan	172.1	3.8	163.9	3.6

SOURCE: Perspectives of the World Economy, April 2006. IMF.

In 2005, the advanced economies, jointly, showed a fiscal deficit of 3.9% of the GDP, percentage lower than the registered in 2004 (4.4%). However, the middle-term fiscal status continued being of particular concern, due to the detriment of the pension and benefits of social prevision systems. Within this group of economies, Japan registered the highest fiscal deficit, which was of 5.8%, lower than the observed in 2004 (6.6%). In the United States of America, the fiscal misbalance was reduced to 4.1% of the GDP (4.7% in 2004), result associated with



an improvement in the fiscal incomes derived from the tax payment on higher corporative profits and to the finalization of an additional deductions program on account of depreciations to motivate the investment. In the Eurozone, though the efforts made in several countries to fulfill the compromises assumed in the framework of the Stability and Growth Pact -PEC- [Acronym in Spanish.], the reduction of the budgetary deficit was slightly significant, due to the lack of corrective measures, most of all on huge economies. In effect, in 2005 Germany and France reduced their fiscal deficit to 3.3% and 2.9%, respectively, compared with 3.7% registered in both countries in 2004. On the other hand, Spain continued showing a strengthening in its fiscal policy, due that after registering a deficit of 0.1% in 2004, ended with 1.1% of surplus in 2005. In contrast, Italy and the United Kingdom increased their fiscal deficit to 4.1% and 3.6%, respectively (3.4% and 3.2% in 2004, respectively). On the other hand, Canada, for the second consecutive year, became the only country of the advanced economies that reach a fiscal surplus of 1.7% of the GDP in 2005 (0.7% In 2004).

<b>ADVANCED ECONOMIES: RESULT OF PUBLIC FINANCES REGARDING THE GDP <sup>a/</sup> YEARS: 2004-2005 (In percentages)</b>		
<b>COUNTRY</b>	<b>2004</b>	<b>2005</b>
<b>TOTAL</b>	<b>-4.4</b>	<b>-3.9</b>
United States of America	-4.7	-4.1
Canada	0.7	1.7
Eurozone	-2.7	-2.3
Germany	-3.7	-3.3
France	-3.7	-2.9
Italy	-3.4	-4.1
Spain	-0.1	1.1
United Kingdom	-3.2	-3.6
Japan	-6.6	-5.8

<sup>a/</sup> It makes references to the deficit or surplus of the general government. Sign (-) = deficit

SOURCE: Perspectives of the World Economy, April 2006. IMF.



### **C. OTHER ECONOMIES WITH EMERGING MARKETS AND DEVELOPING COUNTRIES**

According to the IMF, the economic activity of other economies with emerging markets and developing countries, jointly, continued strengthening; this was reflected in a GDP growth rate of 7.2% in 2005; rate slightly lower than the registered the previous year (7.6%). It is important to mention that, except the Middle East region which reached a growth of 5.9% (5.4% in 2004), the other countries that conform this group experimented a decrease in their economic growth rate.

The developing countries of Africa, jointly, reached a GDP growth of 5.2% in 2005, lower than the percentage observed in 2004 (5.5%). Said growth was due, among others, to the following aspects: a) the dynamism of the Southern Sahara's countries, which showed a strong economic expansion while the GDP increased by 5.5% (5.6% in 2004); b) the improvement of the productive capacity of Angola and the Republic of Congo; c) the increase in the oil production of Mauritania; d) the increase in the prices of metals exported by South Africa and Zambia; e) the success of the economic reforms implemented in Ethiopia, Mozambique and Sierra Leona; and, f) the dynamism of the economic activity of South Africa, supported on the domestic demand and on the increase of its exports.

The Asian developing countries showed a GDP growth rate of 8.6%, which means a slight deceleration regarding the growth of 2004 (8.8%). In this group of countries, highlights, among other factors, the economic expansion of the People's Republic of China, while growing in 9.9% (10.1% in 2004); this growth is due to the strengthening of its exports, as well as to the investment rates; the economic growth of 8.3% of India (8.1% in 2004), supported by a strong domestic demand and by the favorable development of the manufacturer and services sector.

The Middle East region registered a growth of 5.9%, higher than the obtained in 2004 (5.4%). This positive behavior is because, for the third consecutive year, the oil exporting countries obtained higher incomes originated from the increase in the international oil price, as well as from the strengthening of



its domestic demand. On the other hand, the countries that do not produce oil of this region, continued obtaining benefit, on one hand, from the growth of the oil exporting countries, and on the other hand, on the positive effect derived from economic reforms.

In the Western Hemisphere, the GDP showed a growth of 4.3% in 2005 (5.6% in 2004). This economic expansion was caused, on one hand, by a strong demand of export products from Chile and other countries of the Andean region (fuels and metals) and from Argentina and Uruguay (agricultural products); and, on the other hand, by an improvement in the exchange terms, which helped, for the third consecutive year, to obtain a surplus of the region's current account of the payment balance, mainly as a result of an increase in the exports value.

<b>TABLE 9</b>		
<b>OTHER ECONOMIES WITH EMERGING MARKETS AND DEVELOPING COUNTRIES: GROWTH OF THE REAL GDP YEARS: 2004-2005 (In percentages)</b>		
<b>CONCEPT</b>	<b>2004</b>	<b>2005</b>
<b>TOTAL</b>	<b>7.6</b>	<b>7.2</b>
Oil exporting countries	7.1	6.7
Oil non-exporting countries	7.7	7.2
<b>PER REGIONS</b>		
Africa	5.5	5.2
Asian developing countries	8.8	8.6
Middle East	5.4	5.9
Western Hemisphere	5.6	4.3

SOURCE: Perspectives of the World Economy, April 2006. IMF.

According to data from the Economic Commission for Latin America and the Caribbean -CEPAL- [Acronym in Spanish.]<sup>8</sup>, the Latin American and Caribbean region registered a growth of 4.3% (5.9% in 2004). This performance was due,

<sup>8</sup> Preliminary balance of the Latin American and Caribbean Economies, 2005. CEPAL



among other factors, to higher investments rates and family remittances towards the region; to the improvement of the exchange terms, and to an average increase of 7.7% in the export volume, stimulated by a favorable international context. According to CEPAL, the most relevant characteristic of the region in 2005 was that, for the third consecutive year, a surplus was registered in the current account of the payment balance, which, regarding the GDP, registered the following magnitudes: 1.3% in 2005, 0.9% in 2004 and 0.5% in 2003. Besides, it is important to highlight that during the last three years, the region showed a surplus in the current account of the payment balance of about 0.9% of the GDP, result without precedents in the region's recent economic history.

The economic growth of the region was based on the evolution of the South American economies, particularly of Venezuela, Argentina, Peru and Chile, while registering growth rates of 9.0%, 8.6%, 6.0% and 6.0%. On the other hand, the economies of the Caribbean, jointly, showed a growth rate of 4.1% (4.0% in 2004), Central America, 3.6% (3.7% in 2004) and Mexico, 3.0% (4.2% in 2004).

Regarding the monetary policy, the inflation management continued being the main objective of the same in the region's countries, in response to the observed inflationary pressures. In the countries where the inflation goal was fulfilled, the monetary policy contributed in the reactivation of the economic growth. On the other hand, the favorable economic and financial status in which the region is found regarding the rest of the world, has given place to the income of foreign capitals, aspect that has increased the offer of foreign currency in most of the countries, propitiating the appreciation of the real exchange rates.

Regarding the public finances, the region's governments have been able to improve them, as a result of the favorable juncture, in which the fiscal incomes increased, due to the impulse of the economic activity and to the high prices of some export products (energetic, minerals and metals), which are mainly extracted and produced by the public sector. On the other hand, the expenses growth rate has been slower than the incomes, which has originated, on one hand, a positive primary balance and, on the other hand, an improvement in the debt and GDP



relation and, therefore, it has been possible to reduce the foreign vulnerability of the region.

<b>TABLE 10</b>		
<b>LATIN AMERICA AND THE CARIBBEAN: GROWTH OF THE REAL GDP YEARS: 2004-2005 (In percentages, on the base of prices of 2000)</b>		
<b>COUNTRIES</b>	<b>2004</b>	<b>2005 <sup>a/</sup></b>
<b>TOTAL</b>	<b>5.9</b>	<b>4.3</b>
Granada	-2.8	9.2
Venezuela	17.9	9.0
Argentina	9.0	8.6
Saint Lucia	3.6	7.9
Trinidad y Tobago	6.4	7.0
Dominican Republic	2.0	7.0
Uruguay	12.3	6.0
Panama	7.6	6.0
Chile	6.1	6.0
Peru	4.8	6.0
Surinam	7.8	5.2
Saint Kitts and Nevis	6.3	5.1
Colombia	4.0	4.3
Honduras	5.0	4.2
Costa Rica	4.2	4.2
Antigua y Barbuda	5.3	4.0
Nicaragua	5.1	4.0
Bolivia	3.6	3.8
Guatemala	2.7	3.2
Belize	4.6	3.0
Ecuador	6.9	3.0
Mexico	4.2	3.0
Paraguay	4.0	3.0
Saint Vincent and the Grenadines	5.4	2.8
Barbados	4.9	2.8
Dominica	3.6	2.8
Brazil	4.9	2.5
El Salvador	1.5	2.5
Bahamas	1.4	2.1
Haiti	-3.8	1.5
Jamaica	0.9	1.4
Guyana	1.6	-2.9
Cuba	3.0	11.8 <sup>b</sup>



a/ Preliminary data

b/ This growth rate was estimated based on a new methodology that is being analyzed between CEPAL and the Government of Cuba.

SOURCE: Preliminary balance of the Latin American and Caribbean Economies 2005. CEPAL.

<b>TABLE 11</b>		
<b>AMÉRICA LATINA Y EL CARIBE: CRECIMIENTO DEL PIB POR HABITANTE</b>		
<b>AÑOS: 2004-2005</b>		
<b>(En porcentajes)</b>		
<b>PAÍS</b>	<b>2004</b>	<b>2005 <sup>a/</sup></b>
<b>TOTAL</b>	<b>4.3</b>	<b>2.8</b>
Granada	-3.1	8.5
Venezuela	8.0	7.6
Argentina	15.8	7.1
Saint Lucia	2.8	7.0
Trinidad y Tobago	6.1	6.7
Dominican Republic	0.3	5.4
Uruguay	11.5	5.3
Panama	4.9	4.9
Chile	7.1	4.5
Peru	3.3	4.5
Surinam	5.7	4.2
Saint Kitts and Nevis	5.0	3.9
Colombia	2.8	3.5
Honduras	4.0	2.8
Costa Rica	2.3	2.6
Antigua y Barbuda	4.7	2.5
Nicaragua	2.3	2.3
Bolivia	3.3	2.3
Guatemala	4.8	2.2
Belize	1.4	2.1
Ecuador	3.1	1.9
Mexico	2.5	1.7
Paraguay	2.8	1.6
Saint Vincent and the Grenadines	5.4	1.5
Barbados	3.4	1.1
Dominica	0.4	1.0
Brazil	2.4	0.9
El Salvador	0.1	0.7
Bahamas	-0.2	0.7
Haiti	1.5	0.5
Jamaica	-5.5	-0.3
Guyana	1.5	-3.0



Cuba	2.7	...
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<sup>a/</sup> Preliminary datas

SOURCE: Preliminary balance of the Latin American and Caribbean Economies 2005. CEPAL.

According to the IMF, in 2005 the inflation rate of the group of countries of other economies with emerging markets and developing countries was reduced with regard to the previous year, while being of 5.4% (5.7% in 2004). In Africa, the inflation was of 8.5% (8.1% in 2004); nevertheless, in Zimbabwe the inflation remained significantly high, while being of 237.8% (350.0% in 2004), as a result of the inorganic monetization associated with the increase of the **near-fiscal deficit**. In Angola, an inflation rate of 23.0% was registered, lower than the percentage observed the previous year (43.6%); while in the Democratic Republic of Congo an acceleration was observed in the inflationary rate, from 4.0% in 2004 to 21.4% in 2005.

In the developing countries of Asia, the inflation was moderately reduced, from 4.2% in 2004 to 3.6% in 2005. In Indonesia, the inflation was of 10.5% (6.1% in 2004), while in Thailand the inflation was of 4.5% in 2005 (2.8% in 2004).

Regarding the Western Hemisphere, the inflation registered a decreasing behavior, from 6.3% in 2005 (6.5% in 2004). In this region, Haiti, Jamaica, Venezuela and Costa Rica registered the highest inflation rates in 2005, of 16.8%, 16.5%, 15.9% and 13.6%, respectively. On the other hand, the Dominican Republic registered an inflationary rate of 4.2% in 2005 (51.5% in 2004), mainly as a result of the success of the monetary policy oriented to the sterilization of the liquidity surplus derived from the banking crises of the previous year.

The Middle East region registered an inflation of 8.4%, equal than the observed in 2004. Within this group of countries, it is important to highlight the reversion of the deflationary trend shown by Libya, from -2.2% in 2004 to 2.5% in 2005. According to information of CEPAL, the inflation rate in the Latin American and Caribbean countries, jointly, continued showing a decreasing trend, while registering 6.3% in 2005 (7.4% in 2004 and 8.5% in 2003), mainly due to the implementation of measures of restrictive monetary policy.



TABLE 12

**LATIN AMÉRICA AND THE CARIBBEAN: INFLATION  
YEARS: 2003-2005  
(In percentages)**

COUNTRY	2003	2004	2005 <sup>a/</sup>
<b>TOTAL <sup>b/</sup></b>	<b>8.5</b>	<b>7.4</b>	<b>6.3</b>
Argentina	3.7	6.1	12.0
Bahamas	2.3	1.0	2.4 <sup>c/</sup>
Barbados	0.3	4.3	5.5 <sup>d/</sup>
Bolivia	3.9	4.6	5.0
Brazil	9.3	7.6	6.2
Chile	1.1	2.4	3.6
Colombia	6.5	5.5	5.1
Costa Rica	9.9	13.1	14.2
Cuba	-1.0	2.9	4.2
Dominica	2.8	0.8	2.4 <sup>c/</sup>
Ecuador	6.1	1.9	3.8
El Salvador	2.5	5.4	4.6
Guatemala	5.9	9.2	9.2
Guyana	5.0	5.5	7.4 <sup>c/</sup>
Haiti	40.4	20.2	15.2 <sup>e/</sup>
Honduras	6.8	9.2	7.7
Jamaica	14.1	13.7	15.9 <sup>e/</sup>
Mexico	4.0	5.2	2.9
Nicaragua	6.6	8.9	10.5 <sup>e/</sup>
Panama	1.5	1.5	4.0 <sup>e/</sup>
Paraguay	9.3	2.8	12.3
Peru	2.5	3.5	1.1
Dominican Republic	42.7	28.7	4.8
Saint Vincent and the Grenadines	2.7	1.7	3.1 <sup>c/</sup>
Surinam	13.1	9.1	16.6 <sup>e/</sup>
Trinidad and Tobago	3.0	5.6	6.8 <sup>e/</sup>
Uruguay	10.2	7.6	4.8
Venezuela	27.1	19.2	15.3

<sup>a/</sup> Variation in twelve months until November 2005.

<sup>b/</sup> Does not include the Bahamas, Barbados, Granada, Guyana, Saint Vincent and the Grenadines and Saint Lucia. Besides, 2005 does not include Cuba.

<sup>c/</sup> Variation in twelve months until September 2005.

<sup>d/</sup> Variation in twelve months until June 2005.

<sup>e/</sup> Variation in twelve months until October 2005.

SOURCE: Preliminary balance of the Latin American and Caribbean Economies 2005. CEPAL.



Regarding the financial conditions of the economies with emerging markets and developing countries, the net flows of private capital showed a considerable increase, from US\$237.8 milliard in 2004 to US\$269.7 milliard in 2005. According to the IMF, said flows increased by Central and Eastern Europe, in the Western Hemisphere, in Africa and in the Community of Independent States and reduced in the developing countries of Asia and Middle East. In effect, in 2005 the net flows of private capital in the group of countries of Central and Eastern Europe reached \$108.2 milliard (US\$71.0 milliard in 2004); in the Western Hemisphere, US\$25.2 milliard (US\$6.0 milliard in 2004); in Africa and in the Community of Independent States, US\$30.4 milliard and US\$24.9 milliard, respectively (US\$13.0 milliard and US\$8.0 milliard, in 2004, respectively). On the other hand, in the developing countries of Asia, the net flows of private capital were reduced to US\$69.8 milliard in 2005 (US\$123.4 milliard in 2004); while in the Middle East countries were of US\$11.2 milliard, lower than the one registered in 2004 (US\$16.3 milliard).

Regarding the current account of the payment balance of the economies with emerging markets and developing countries, in 2005 it registered a surplus of US\$423.3 milliard, significantly higher than the registered in 2004 (US\$219.8 milliard). This result was influenced by the positive balances in the developing countries of Asia of US\$155.4 milliard; in the Middle East of US\$196.0 milliard; in Africa of US\$15.2 milliard; in the Western Hemisphere of US\$29.6 milliard; and, in the Community of Independent States of US\$90.3 milliard.

According to CEPAL, in 2005 the Latin American exports grew in 19.0% (7.7% in terms of volume and 10.6% in terms of unit price). This growth rate reflected a lower dynamism regarding the previous year, when the exports grew in 22.8% (9.6% in terms of volume and 12.0% in terms of unit price). On the other hand, the region's imports also reflected a lower increased regarding 2004, while registering a rate of 17.5% (11.4% in terms of volume and 5.5% in terms of unit price); while in 2004 grew in 21.7% (14.5% in terms of volume and 6.3% in terms of unit price).

In the described context, though the lower dynamism of the region's foreign trade, the trade opening grade (understood as the sum of exports and imports



regarding the GDP) remained almost unaltered, due that the same was placed in 44.0% of the GDP, not only in 2004, but also in 2005.

The balance of goods observed a positive balance, for the fourth consecutive year, though in 2005 it was of US\$75.7 milliard, which represented 3.2% of the regional GDP. On the other hand, the positive balance in the current account of the payment balance of the region was of US\$29.7 milliard (1.3% of the GDP).

The countries of the Community of Independent States, in 2005 registered a growth of 6.5%, which means a significant deceleration if it is compared with the strong growth of the two previous years (8.4% in 2004 and 7.9% in 2003). This behavior is mainly explained by the lower impulse of the energetic sector in Russia and in Kazakhstan, as well as from the political and economic uncertainty that remained in Ukraine, in the Republic of Kyrgyzstan and Russia, which affected the investment rates in these economies.

On the other hand, the countries of the Central and Eastern Europe, jointly, showed an economic growth of 5.3% in 2005, lower than 6.5% of the previous year. Said growth was mainly caused by a strong domestic demand and a solid behavior of the exports.

<b>COUNTRIES OF CENTRAL AND EASTERN EUROPE AND OF THE COMMUNITY OF INDEPENDENT STATES: GROWTH OF THE REAL GDP YEARS: 2004-2005 (In percentages)</b>		
<b>COUNTRY</b>	<b>2004</b>	<b>2005</b>
<b>Central and Eastern Europe</b>	<b>6.5</b>	<b>5.3</b>
Albania	5.9	5.5
Bosnia and Herzegovina	6.2	5.0
Bulgaria	5.7	5.5
Croatia	3.8	4.1
Slovenia	4.2	3.9
Estonia	7.8	9.8



Hungary	4.6	4.1
Latvia	8.5	10.2
Lithuania	7.0	7.3
Ex Yugoslav Republic of Macedonia	4.1	3.8
Malta	1.0	1.0
Poland	5.3	3.2
Czech Republic	4.7	6.0
Republic of Slovakia	5.5	6.0
Rumania	8.4	4.1
Serbia and Montenegro	8.8	4.7
Turkey	8.9	7.4
<b>Community of Independent States</b>	<b>8.4</b>	<b>6.5</b>
Armenia	10.1	13.9
Azerbaijan	10.2	24.3
Byelorussia	11.4	9.2
Georgia	6.2	7.7
Kazakhstan	9.6	9.4
Moldavia	7.3	7.0
Mongolia	10.7	6.2
Republic of Kyrgyzstan	7.0	-0.6
Russia	7.2	6.4
Tajikistan	10.6	6.7
Turkmenistan	17.2	9.6
Ukraine	12.1	2.6
Uzbekistan	7.4	7.0

SOURCE: Perspectives of the World Economy, April 2006. IMF.



<b>ANNEX 1 CLASSIFICATION OF COUNTRIES</b>				
<b>According to the Report of Perspectives of the World Economy, April 2006 of the International Monetary Fund - IMF-, the countries are classified in two main groups: a) advanced economies; and, b) other economies with emerging markets and developing countries.</b>				
<b>ADVANCED ECONOMIES PER COUNTRIES SUB-GROUPS</b>				
<b>Main advanced economies</b>	<b>Other advanced economies</b>	<b>European Union</b>	<b>Eurozone</b>	<b>Asian Economies Recently Industrialized</b>
Germany Canada United States France Italy Japan United Kingdom	Australia Korea Cyprus Denmark Hong Kong SAR <sup>a/</sup> Iceland Israel New Zealand Norway Singapore Sweden Switzerland Taiwan	Germany Austria Belgium Denmark Spain Finland France Greece Ireland Italy Luxembourg Low countries Portugal Sweden United Kingdom	Germany Austria Belgium Spain Finland France Greece Ireland Italy Luxembourg Low countries	Korea Hong Kong SAR <sup>a/</sup> Singapore Taiwan
<b>OTHER COUNTRIES OF THE EUROPEAN UNION, THE ECONOMIES OF WHICH ARE NOT CONSIDERED ADVANCED</b>				
		Cyprus Slovenia Estonia Hungary Latvia Lithuania Malta Poland Czech Republic Republic of Slovakia		

<sup>a/</sup> On July 1st, 1997, the People's Republic of China recovered the sovereign of Hong Kong, which became the Special Administrative Region of Hong Kong of the People's Republic of China (SAR).

SOURCE: Perspectives of the World Economy, April 2006. IMF.



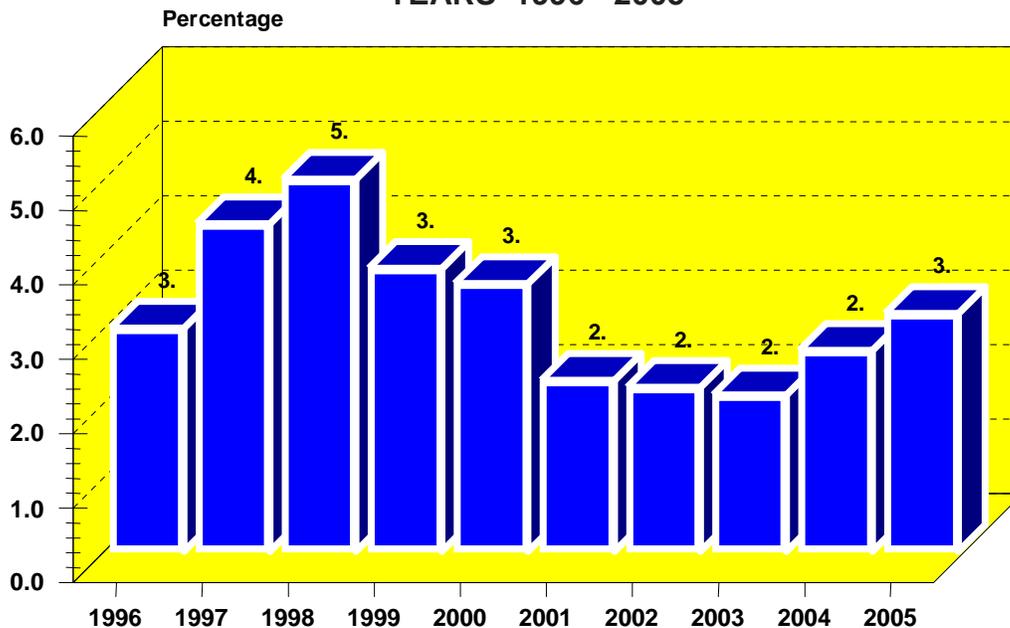


### III. THE NATIONAL ECONOMIC ACTIVITY

#### A. GENERAL STATEMENTS

The deceleration that the growth rate of the national economic activity started showing since 1999 was reverted in 2004; trend that continued in 2005. In effect, the economic growth, measured by the GDP in real terms, registered a rate of 3.2%, higher by 0.5 percentage points than the registered in 2004 (2.7%). It is important to indicate that this economic growth rate continues being lower than the average rate registered in the nineties (4.1%), but higher, for the second consecutive year, than the population's growth rate (2.5%)<sup>9</sup>.

**FIGURE 1**  
**REAL GROSS DOMESTIC PRODUCT**  
**VARIATION RATE**  
**YEARS 1996 - 2005**



<sup>9</sup> Estimation carried out by the *Instituto Nacional de Estadística -INE-*, based on the XI National Population Census 2002.



Said behavior is based, in the external order, on the increase registered not only in the economy of the United States of America, which in 2005 grew in 3.5%, growth rate that surpassed the average rate observed in the advanced economies (2.7%), but also on the rest of the main countries that are commercial associates of Guatemala<sup>10</sup> and, in the internal order, on the maintenance of the macroeconomic stability, based on the application of a prudent monetary policy, strongly supported by a disciplined fiscal policy, as well as on the slightly significant effect that the tropical storm Stan<sup>11</sup> had on the production flow of the country, which was computed according to the calculation methodology of the national accounts.

It is important to indicate that though the increase of the international oil price, for the second year, was constituted in an adverse factor for the national economic activity, the impulse that the world economy continued showing, mainly supported by the economic growth of the United States of America and the People's Republic of China, supported the growth of the Guatemalan economy. In that sense, it was observed that though the international oil price was transferred to the general rate of prices, it did not affect the impulse of the national economic activity.

## **B. GROSS DOMESTIC PRODUCT PER EXPENDITURE**

According to the behavior of the GDP per expenditure, in real terms, the global demand registered a growth of 2.9%, lower than the registered in 2004 (3.5%).

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<sup>10</sup> According to the document "Perspectives of the World Economy", prepared by the IMF in April, 2006, the economy of Mexico grew in 3.0%; El Salvador's in 2.8%; Honduras' in 4.2%; Costa Rica's 4.1%; and, Nicaragua's 4.0%.

<sup>11</sup> According to the document "Effects in Guatemala of the Torrential Rains and the Tropical Storm Stan, October 2005" dated November 24th, 2005, prepared by the Economic Commission for Latin America and the Caribbean - CEPAL-, at the request of the *Secretaría General de Planificación y Programación de la Presidencia -SEGEPLAN-*, the effect of the phenomenon in the country's economy was low, due that the subsistence agricultural production was the most affected and the contribution of which is slightly significant in the country's total production. In effect, according to the mentioned document, the permanent crops did not register significant losses and the production of the rest of the productive sector was not affected.



The domestic demand, constituted by the total consumption and gross geographical investment, registered a growth of 3.4%, higher by 0.4 percentage points than the observed in 2004 (3.0%). Regarding the variables that integrate the domestic demand, the private consumption, which represented 77.9% of the same, registered a growth of 4.3% in real terms, higher by 0.5 percentage points than the one shown in 2004 (3.8%); this behavior is associated with the macroeconomic stability and with the reception of a higher amount of family remittances.

The consumption expenditure of the general government, that includes remunerations and purchase of goods and services, registered a fall in real terms of 1.4%, lower in 8.7 percentage points than the observed in 2004 (-10.1%); this behavior is explained by a higher budgetary execution due to the operational expense of the central government during the year.

The gross geographical formation of fixed capital registered an increase of 12.5% (2.0% in 2004), as a result of a positive variation of 11.7% in the gross geographical formation of the private sector (9.5% in 2004) and an increase of 16.4% in the public investment (-24.0% in 2004). In the result of the gross geographical formation of the private sector that constituted 82.8% of the total gross geographical formation, was mainly influenced by the growth of the private construction, from 11.9% in 2004 to 26.9% in 2005, as well as by the increase of 10.9% in the goods of imported capital (12.3% in 2004). Regarding the increase of the public investment, it was influenced by the increase of 210.1% in the purchase of machinery and equipment sector (-19.6% in 2004) and by the increase of 2.6% in the construction of roads and public works sector (-24.3% in 2004).

Regarding the foreign demand, constituted by the export of goods and services<sup>12</sup>, it showed a fall of 1.0% in real terms (growth of 6.5% in 2004); this behavior was mainly associated with a reduction in the coffee exported volume (-

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<sup>12</sup> The compilation methodology of the international trade statistics of Guatemala was modified in November 2003 and reviewed in retrospect until January 2002 in order to compare. The new methodology classifies the Guatemalan trade in three components: Trade of Custom Territory, Trade of Tax-free area and Trade of Companies supported by Decree number 29-89 of the Congress of the Republic (Foment and Developmental Law for the Exporter Activity and Manufacturers); while the methodology of the 1958 base regarding National Accounts, only includes the Trade of Custom Territory and Trade of Tax-free areas.



3.0%) and in petroleum (-8.8%), as well as in the value of the non-factorial services in real terms (-12.0%). Regarding the foreign offer, the import of goods and services registered, in real terms, a growth of 1.4%, lower than the observed the previous year (7.2%). This behavior is mainly associated with a lower dynamism of the imports, in terms of North American dollars, of consumption goods; of basic goods and intermediate products; and, of capital goods, which grew in 7.2% (13.2% in 2004), 4.4% (18.2% in 2004) and 11.6% (16.5% in 2004).

### **C. GROSS DOMESTIC PRODUCT PER ACTIVITY BRANCH**

Regarding the production that in 2005, with the exception of the *exploitation of mines and public administration and defense* sector, register negative growth rates, though lower than the previous year, a positive behavior was observed for the productive sectors, highlighting the *manufacturer industry, construction and banking, insurance and real estate*, the growth rate of which was more dynamic than the observed in 2004.

The behavior of the added value of the *agriculture, forestry, hunting and fishing* sector, based on the data provided by producers' associations, guilds and public and private entities, registered a growth of 2.2%, lower than the rate observed the previous year (4.0%). This result is mainly explained by the deceleration registered in the production of the agricultural sub-sector, the growth rate of which in 2005 was of 2.9% (5.6% in 2004) and represented 60.2% of the sector. The behavior of this sub-sector was mainly influenced by the lower dynamism in the export agricultural production (mainly of coffee and cardamom), which grew in 2.7% (10.1% in 2004) and in the agricultural production of industrial consumption (mainly of sugar cane), which registered a growth rate of 2.2% (4.2% in 2004).

The domestic consumption products had a positive and more dynamic behavior, except corn which experienced a negative variation in its production as a result of the damages caused by the tropical storm Stan.

It is important to indicate that according to the information of the *Ministerio de Agricultura, Ganadería y Alimentación -MAGA-*, except sesame, the main



agricultural products (coffee, sugar cane and banana) maintained a normal production process during the year, due that the tropical storm Stan mainly affected the subsistence production, as well as the backyard agricultural activities, the contribution of which is slightly significant in the total production of the agricultural sub-sector. Said activities are mainly associated with the production of corn (white and yellow), beans, some vegetables (tomato, onion, potato, pepper), some fruit plantations (watermelon, papaya, pineapple) and, in a lower scale, with the production of cattle and poultry. The production of golden coffee in 2005, according to information provided by the *Asociación Nacional del Café -ANACAFÉ-*, was of 4,800.0 thousands of quintals, higher by 16.2 thousand of quintals (0.3%) than the observed in 2004 (4,783.8 thousand of quintals). The low dynamism in the growth of coffee production, though the average export price per quintal was of US\$72.54 in 2004 to US\$105.83 in 2005, is because, according to ANACAFÉ, the investment in cultural works was not significantly increased and some grain producers of *Escuintla* started to diversify their production, producing sugar cane and rubber, before the expectation that they might obtain a better benefit with the enforcing of the Free Trade Agreement between the United States of America and Central America and the Dominican Republic (DR-CAFTA). Regarding the production of banana in 2005, according to information from *Compañía Bananera Guatemalteca Independiente, S. A., -COBIGUA-* and from *Compañía de Desarrollo Bananero de Guatemala, S. A., -BANDEGUA-*, it was of 24.7 million of quintals, higher by 11.4% than the observed in 2004, which was of 22.2 million of quintals (6.5%), behavior associated with the higher profit of the plantations in the South. The production of cardamom grew in 0.3% (27.5% in 2004). According to the *Asociación de Cardamomeros de Guatemala -CARDEGUA-*, the lower dynamism is explained by the reduction of the international price of this aromatic, which was reflected in the average export price, which decreased from US\$118.84 per quintal in 2004 to US\$102.35 per quintal in 2005, due to the accumulation of inventory of said product in the Middle East countries. The production of sugar cane, according to information from the *Asociación de Azucareros de Guatemala -ASAZGUA-* and from the *Centro Guatemalteco de Investigación y Capacitación de*



*la Caña de Azúcar -CENGICAÑA-*, registered a growth of 0.2% (10.0% in 2004), because the profit per harvested block slightly increased, due to the maintenance of the cultural works and to favorable climatic conditions in the producing zones. In effect, during the 2004/2005 harvest, a production of 392.0 million of quintals of sugar cane was obtained, amount higher by 0.8 million of quintals than the one registered in the previous harvest (391.2 million of quintals).

With regard to basic grains, corn and beans, based on the information provided by the *Coordinadora Nacional de Productores de Granos Básicos-CONAGRAB-*, the production of corn was of 22.5 million of quintals, which meant a fall of 4.1% regarding the previous year (0.2%), as a result of the losses caused by the tropical storm Stan, which are estimated in about 1.9 million of quintals (8.5% of the national production)<sup>13</sup>. On the other hand, the production of beans increased by 3.0% (fall of 5.2% in 2004), from 2.0 million of quintals in 2004 to 2.1 million of quintals in 2005.

Regarding the production of fruit, it registered a more dynamic behavior than the previous year, from 1.5% in 2004 to 6.2% in 2005, which is mainly explained by an increase of 7.8% in the exported volume of melon (-3.8% in 2004) and of 47.6% in banana (-20.6% in 2004). It is important to indicate that both products jointly represent 74.8% of the exported volume of fruits.

The production of vegetables, on one hand, reached 10.4 million of quintals, showing an increase of 8.1% regarding the previous year (3.5%); this behavior is associated with the higher demand of said products in the international market, which was evidenced in an increase of 19.1% in the exported volume in 2005 (4.9% in 2004). It is important to indicate that the sale of vegetables abroad, particularly carrot, cabbage, onion and tomato, were the most significant, which jointly, in 2005, represented about 35.5% of the exported value of this sector.

Regarding the added value of the *exploitation of mines and quarries* sector, in 2005, registered a fall of 2.1% (7.6% of fall in 2004). This behavior was

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<sup>13</sup> According to information of CONAGRAB, the production of corn was affected in *San Marcos, Quetzaltenango, Retalhuleu, Suchitepéquez, Escuintla, Santa Rosa, Totonicapán, Sololá* and *Chimaltenango*, which jointly produce about 35.0% of the country's total production.



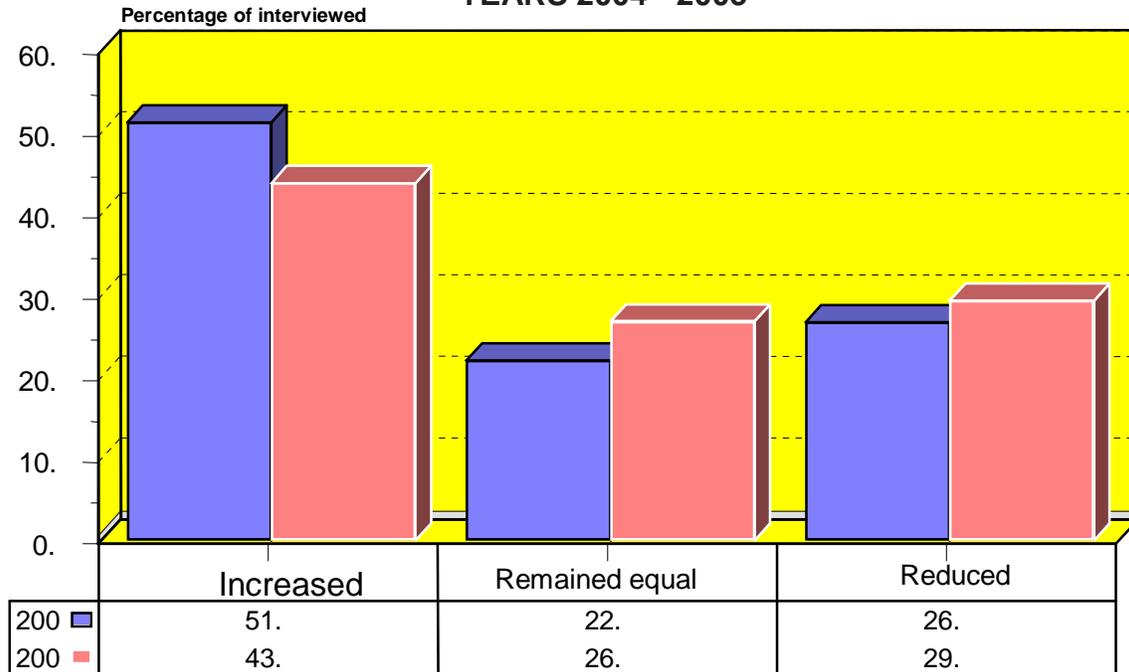
influenced by the reduction observed in the production of crude oil (55.0% of the production of this sector), while registering a total of 6,727.6 thousands of barrels, 8.3% less than in 2004 (7,333.8 thousand of barrels). According to the information of the *Ministerio de Energía y Minas*, said result is associated, on one hand, with the fact that the pumping pressure of some wells continued depressed and, on the other hand, that there were no new wells operating. On the other hand, the *gravel and sand* sub-sector, registered an increase of 26.8% (11.7% in 2004), as a result of a higher dynamism observed in the private construction.

The added value of the *manufacturing industry* sector registered a growth of 2.7% in 2005, percentage higher than the observed in 2004 (2.3%), representing the highest relative variation during the last seven years. This behavior was influenced by the growth of the demand of Guatemalan industrial products in the North-American and Central American markets, derived from the positive performance of their economies. In effect, the value of exports to the United States of America increased by the following way: sugar 43.7% (19.1% in 2004); fruits and **preparations** 17.0% (1.2% in 2004); wood and wood manufactures 12.8% (-1.5% in 2004); and, food products 12.7% (6.7% in 2004). Regarding the sales to Central America, highlight the export of fruits and preparations, 31.3% (17.7% in 2004); plastics, 21.1% (23.4% in 2004); construction materials, 15.1% (31.1% in 2004); food products, 13.5% (4.9% in 2004); and, chemical products, 11.3% (13.3% in 2004).

On the other hand, in 2005 the imports of basic goods and intermediate products destined for the *manufacturing industry* sector, registered, in dollars of the United States of America, a growth of 4.1% (17.2% in 2004); while the import of capital good for the industry registered an increase of 14.8% (18.7% in 2004).



**FIGURE 2**  
**SURVEY OF BUSINESS OPINION**  
**VOLUME OF INDUSTRIAL PRODUCTION**  
**YEARS 2004 - 2005**



It is important to mention that the dynamism observed in the *manufacturing industry* is congruent with the results of the Survey of Business Opinion<sup>14</sup>. In effect, 70.7% of the interviewed expressed that in 2005 the production volume increased or remained the same; while in 2004 said percentage was of 73.3%. The added value of the *construction, public and private*, registered an increase of 16.0% (fall of 18.2% in 2004), as a result of an increase of 27.0% in the *private construction* (12.2% in 2004) and of 4.6% in the *public construction* (36.0% of fall in 2004).

Regarding the *private construction*, the positive behavior is associated, on one hand, with the increase of 58.4% in the surface of authorized construction in

<sup>14</sup> Carried out in February-March 2006 to a sample of 400 industrial entities, from which 60% are big companies (more than 50 employees); 22% middle companies (20 to 49 employees); and, 18% small companies (5 to 9 employees).



the main surveyed municipalities<sup>15</sup> (1.4% in 2004) and, on the other hand, with the increase in the amount of loans granted by the banking system to the private construction which in 2005 increased by Q714.9 million (53.1%) regarding 2004 (12.5%). Regarding the public construction, the result is explained by the fact that the budgetary execution of the central government in 2005 showed an increase in the capital expenditure, as a result of the rehabilitation and maintenance programs of roads during said year, which were intensified due to the damages caused by the tropical storm Stan.

The added value of the *electricity and water* sector registered a growth of 1.7% (6.0% in 2004). According to information of the *Administrador del Mercado Mayorista -AMM-*, a total gross generation of electric energy of 7,222.5 thousand of Megawatts/per (MWH) was registered, which means an increase of 1.8% regarding the previous year (6.0%). The lower dynamism of this sub-sector was influenced by the fall in the sale of electric energy to El Salvador, which showed a fall of 28.0% (126.9 thousand of MWH), growth of 7.7% in 2004, as well as by the reduction of 5.3% in the thermal gross generation. On the other hand, the gross hydraulic generation grew in 14.4% (17.0% en 2004). The added value of the transport, storing and communications sector observed a growth rate of 9.3% (9.5% in 2004), behavior explained, on one hand, by the increase of 7.3% in the transport sub-sector (6.3% en 2004), associated with the increase of 28.8% (fall of 0.4% in 2004) registered in the urban passenger transport and of 7.6% in the aerial international transport (1.9% in 2004) and, on the other hand, by the growth of 12.0% (14.0% in 2004) in the communications sub-sector. Regarding this last sub-sector, according to information from the *Superintendencia de Telecomunicaciones de Guatemala -SIT-*, in 2005 the total of new telephone lines was increased by 9.6% regarding the previous year (20.5%), from 3,588.7 thousand in 2004 to 3,934.4 thousand in

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<sup>15</sup> Survey carried out by the *Banco de Guatemala* in 40 municipalities of the Republic of Guatemala (Guatemala, Mixco, Villa Nueva, Santa Catarina Pinula, San José Pinula, Villa Canales, San Miguel Petapa, Amatitlán, Antigua Guatemala, Chimaltenango, Coatepeque, Cobán, Escuintla, Huehuetenango, Jalapa, Mazatenango, Puerto Barrios, Quetzaltenango, Santa Cruz del Quiché, Jutiapa, Cuilapa, Retalhuleu, San Pedro Carchá, Esquipulas, Tiquisate, La Gomera, San Pedro Sacatepéquez, Sololá, San Marcos, Malacatán, Nueva Santa Rosa, Asunción Mita, Puerto de San José, San Antonio Suchitepéquez, Momostenango, Totonicapán, Guastatoya, Salamá, Flores and Zacapa).



2005. The added value of the wholesale and retail trade sector registered a growth of 2.4% (3.1% in 2004), behavior associated with the lower dynamism observed in the agro-forestry sector and the growth of 12.8% (16.2% in 2004), in terms of dollars of the United States of America, registered in the import of goods.

The added value of the *banking, insurance and real estate* sector registered in 2005 a variation of 3.1%, higher by 0.9 percentage points than the observed the previous year (2.2%), associated not only with the behavior of the banking fund-raising, but also with the credit to the private sector.

Finally, the *housing property and private services* sector showed growth rates of 2.5% and 3.6%, respectively (2.9% and 3.6%, respectively, in 2004) and regarding the *public administration and defense* sector registered a fall of 1.8% with regard to 2004 (-8.4%), behavior associated with the budgetary restriction of the central government's operating expenditure observed during 2005.

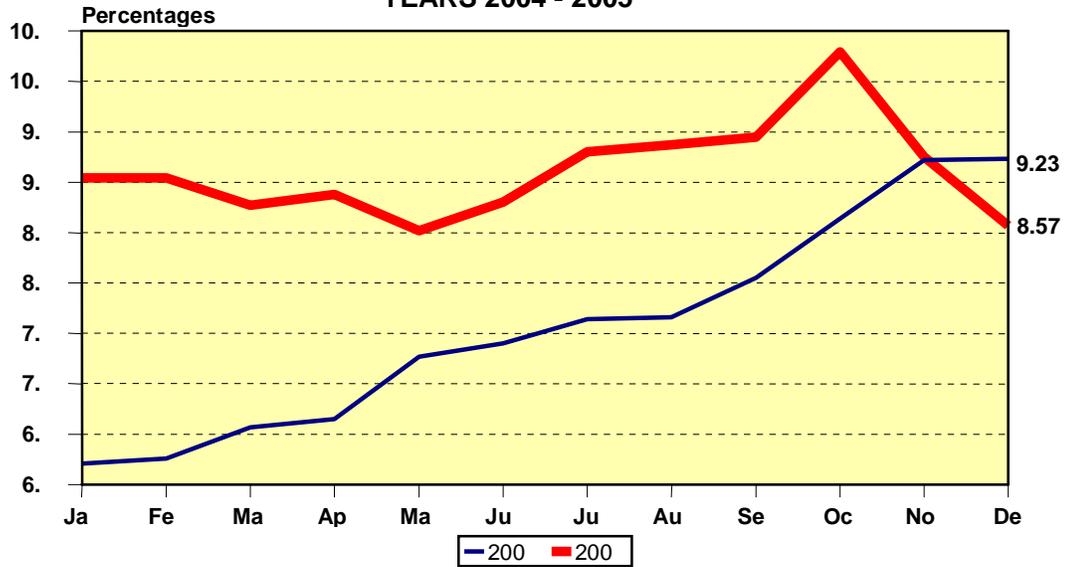
## **D. BEHAVIOR OF THE OD THE DOMESTIC PRICES**

### **1. Consumer Price Index –CPI**

In 2005, according to the Consumer Price Index -CPI-, prepared by the *Instituto Nacional de Estadística -INE-*, at a national rate, an inflation rate of 8.57% was registered, percentage higher than the goal established in the Monetary, Exchange and Credit Policy determined by the Monetary Board for 2005 (4.0% - 6.0%). Said inflationary rate is lower in 0.66 percentage points than the observed in en 2004 (9.23%).



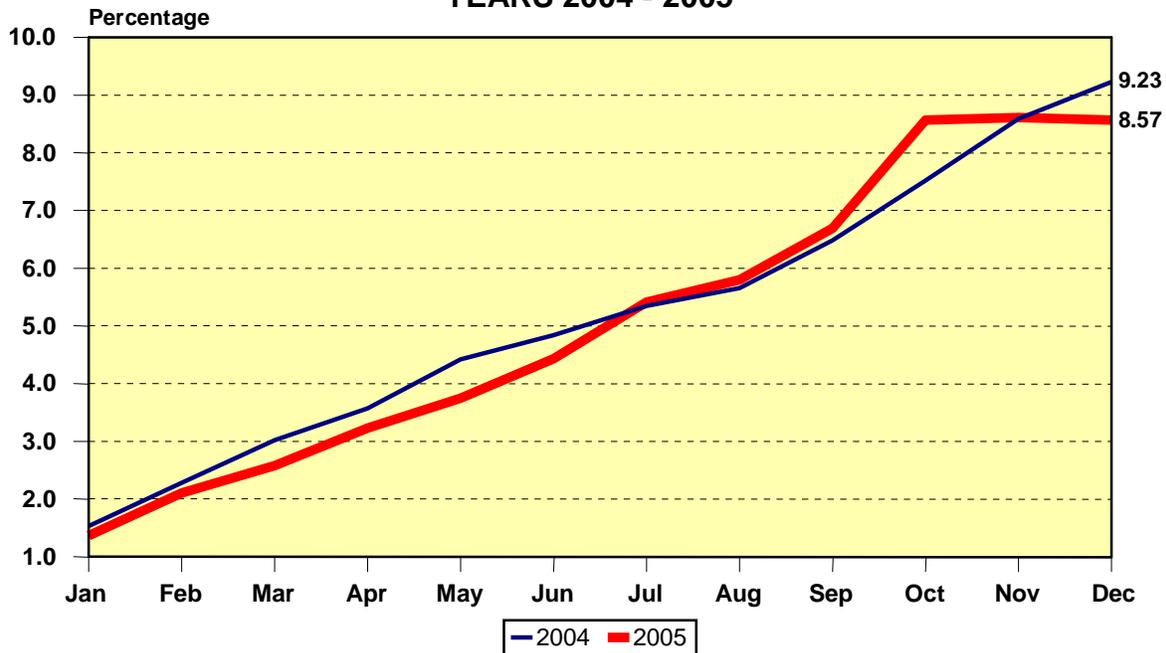
**FIGURE 3**  
**CONSUMER PRICE INDEX**  
**INFLATIONARY RATE**  
**YEARS 2004 - 2005**



Source: Instituto Nacional de Estadística.



**FIGURE 4**  
**CONSUMER PRICE INDEX**  
**ACCUMULATED INFLATION**  
**YEARS 2004 - 2005**



Source: *Instituto Nacional de Estadística*.

As analyzed afterwards, most of the inflation surplus above the referred goal is explained by the effects derived from the increase in the international prices of fuels, which is reflected in the behavior of the imported inflation.

It is important to mention that during 2005, the behavior of the inflationary rate can be divided in three phases. The first one was characterized by a slight trend to the fall, from 9.04% in January to 8.52% in May. In the second phase, which covered from June to October, said trend was reverted, mainly due to an increase in the international oil price, reaching a rate of 10.29% in October<sup>16</sup>, as a result of the lack of agricultural products and damages to the country's roads, caused by the tropical storm Stan. In the third phase, a deceleration of the inflation rate was shown registering 9.25% in November and 8.57% in December, after the

<sup>16</sup> In October the CPI inter-monthly variation was of 1.76%, which is the highest since November 1998, month when the country was affected by the Mitch hurricane.



supply of agricultural products was normalized and after observing a reduction in the price of fuels.

On the other hand, the CPI inter-annual variation to December 2005 shows the growth of the indexes of the nine expenditure divisions that constitute it, particularly, *Food, non-alcoholic beverages and take-out foods* that registered an inter-annual variation of 12.38% and explained 61.14% of the CPI inter-annual increase. Other divisions that explain the behavior of the inflationary rate are *Transport and communications; housing, water, electricity, gas and other fuels;* and, *Education*, which added to the *Food, non-alcoholic beverages and take-out foods*, explained 81.77% of the CPI inter-annual variation to December 2005.

TABLE 14

**INTER-ANNUAL VARIATION OF THE CONSUMER PRICE INDEX  
AT A NATIONAL RATE  
Base: December 2000 = 100.0  
TO DECEMBER OF EVERY YEAR**

EXPENSE DIVISION	WEIGHTING	INDEX		VARIATION	PERCENTAGE PARTICIPATION
		2004	2005		
<b>GENERAL INDEX</b>	<b>100.00</b>	<b>133.89</b>	<b>145.36</b>	<b>8.57</b>	<b>100.00</b>
1. Food, non-alcoholic beverages and take-out foods	38.75	146.07	164.16	12.38	61.14
2. Clothing and footwear	7.94	120.99	125.25	3.52	2.95
3. Housing, water, electricity, gas and others	10.00	125.13	133.46	6.66	7.26
4. Furniture, housing equipment and daily maintenance	7.95	126.96	132.94	4.71	4.15
5. Health	5.48	127.70	135.34	5.98	3.65
6. Transport and communications	10.92	120.12	129.60	7.89	9.02
7. Recreation and culture	6.83	131.47	137.60	4.66	3.65
8. Education	5.60	135.18	144.09	6.59	4.35
9. Diverse goods and services	6.53	128.90	135.64	5.23	3.84

Source: *Instituto Nacional de Estadística -INE-*

In the *Food, non-alcoholic beverages and take-out foods expense division* (weighting 38.75%), the variation of 12.38% was mainly due to the increase in the *bread and cereals; take-out foods and tidbits; vegetables, legumes and tubercles; and, meats* expenditure groups, which jointly explained 83.54% of the inter-annual variation of this division.

The *Transport and Communications* division (weighting 10.92%), registered an inter-annual variation of 7.89%, mainly determined, by the increase in the average price of two main expenditures: *gasoline and extra-urban transport;* these



increases are associated with the increase in the international oil price, and that jointly explained 64.08% of the inter-annual variation of said division.

The *housing, water, electricity, gas and other fuels division* (weighting 10.00%), showed an inter-annual variation of 6.66%, determined by the behavior of the following basic expenditures: *propane gas and real housing rentals*, which jointly explained 68.72% of the variation of this division.

On the other hand, the *Education division* (weighting 5.60%), registered an inter-annual variation of 6.59%, explained by the behavior of the following basic expenditures: *monthly quota in elementary and pre-school education; other educational materials and supplies; and, monthly quota of secondary education*, which jointly explain 60.64% of the variation of this division.

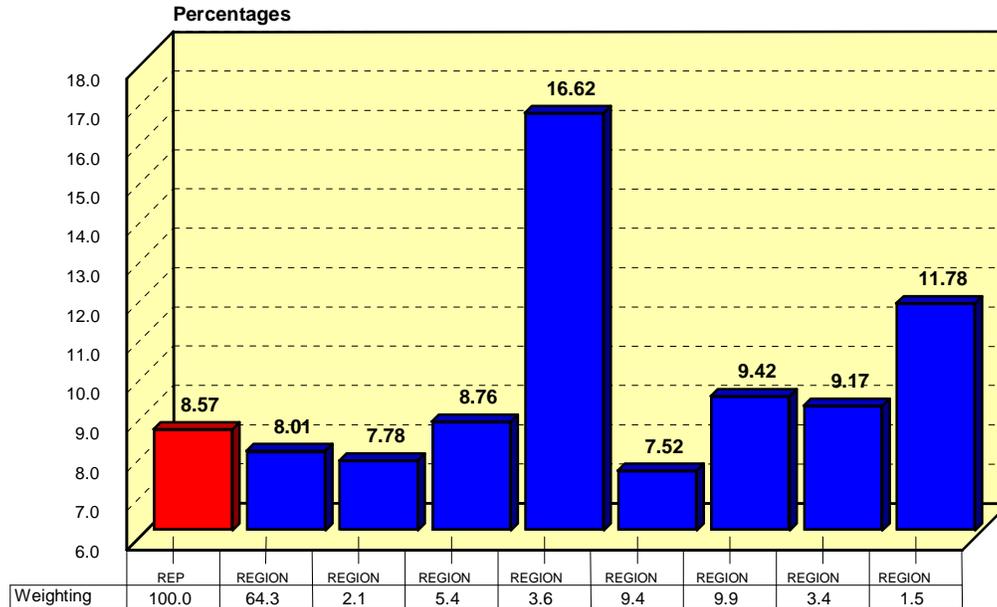
At a regional rate<sup>17</sup>, region IV (South East) reached the highest inflationary rate, with 16.62%, followed by region VIII (*Petén*) and region VI (South West), which registered a rate of 11.78% and 9.42%, respectively. Region I (Metropolitan), which has the highest weighting within the total of regions (64.32%), showed an inter-annual variation of 8.01%, lower in 0.56 percentage points than the inflationary rate at a national rate (8.57%).

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<sup>17</sup> Region I, Metropolitan (Guatemala); region II, North (*Alta Verapaz* and *Baja Verapaz*); región III, North East (*El Progreso, Zacapa, Izabal* and *Chiquimula*); region IV, South East (*Santa Rosa, Jalapa* y *Jutiapa*); region V, Central (*Chimaltenango, Sacatepéquez* and *Escuintla*); region VI, South West (*San Marcos, Quetzaltenango, Totonicapán, Suchitépéquez, Retalhuleu* and *Sololá*); region VII, North West (*Huehuetenango* and *Quiché*); and, region VIII (*Petén*).



**FIGURE 5  
CONSUMER PRICE INDEX  
INFLATIONARY RATE PER REGIONS  
YEAR 2005**



Source: Instituto Nacional de Estadística.

In region IV (South East), with a weighting of 3.60% within the structure per regions, significant increases were registered in the average price of the following products: *tortilla products* (145.30%); *other vegetables* (101.43%); *bread* (15.45%); and, *expenses derived from the service of residential water* (370.59%). It is important to indicate that the mentioned increases jointly represent 62.27% of the inter-annual variation of said region.

In region VIII (*Petén*), with a weighting of 1.59% within the total of regions, the inter-annual variation registered is mainly explained by the increase in the average price of the following products: *bread* (57.62%); *tortilla products* (44.15%); *beans* (40.12%); *other vegetables* (63.46%); and, *tomato* (25.52%), which jointly explain 49.83% of the inter-annual variation of the region.

The increase observed in region VI (South West), with a weighting of 9.92%, is mainly due to the increase registered in the average price of the following products: *tortilla products* (40.58%); *bread* (21.04%); *beans* (37.02%); *fresh,*



*refrigerated and frozen meat* (11.36%); *expenses due to the consumption of domestic oils and oils for lamps, fuels for use* (21.99%); *breakfast or dinner* (12.17%); and, *other vegetables* (40.31%), which jointly represent 46.71% of the region's inter-annual variation.

Regarding region I (Metropolitan), with a weighting of 64.32% within the total of regions, the inter-annual variation registered is mainly explained by the increase in the average price of the following products: *bread* (17.75%); *tortilla products* (24.95%); *lunch* (9.02%); *gasoline* (17.60%); *fresh, refrigerated and frozen meat* (11.53%); *breakfast or dinner* (10.65%); *real housing rentals* (6.27%); and, *beans* (34.12%), products that explain 45.69% of the inter-annual variation of the region.

## 2. Hidden inflation

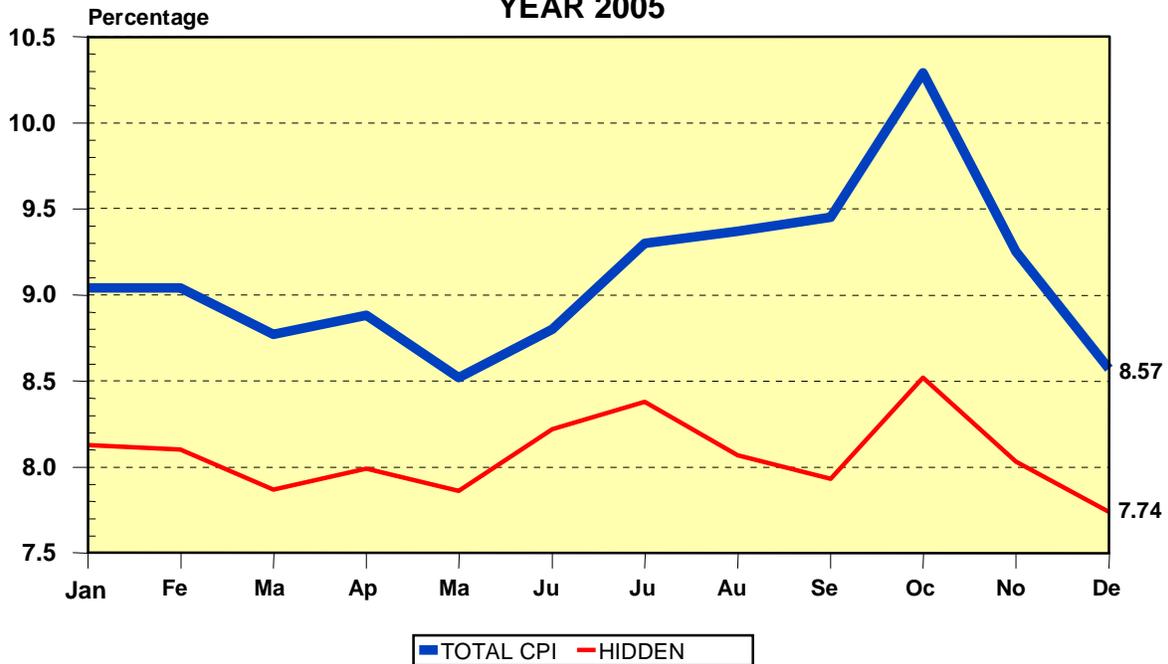
In general terms, the hidden inflation is the growth rate of a price index that, in order to eradicate distortions in its calculation, excludes some goods and services that have very volatile prices or that are subjected to foreign shocks. In the case of Guatemala the price indexes of the following goods are excluded: *Fresh, dry and candied fruit; Vegetables, legumes and tubercles; Manufactured and natural gas and gases melted from petroleum; and, Gasoline*, the weightings of which in the GDP are of 1.28%, 3.77%, 1.09% and 2.04%, respectively. Said indexes jointly represent 8.18% of the CPI.

It is important to indicate that the hidden inflation registered, to December 2005, an inter-annual variation of 7.74%; percentage lower in 0.83 percentage points than the registered by the total CPI (8.57%); this difference is because some sectors that registered significant increases were eradicated from its composition: *Gasoline* (which registered a variation of 17.51%); *Vegetables, legumes and tubercles* (18.43%); *Manufactured and natural gas and gases melted from petroleum* (22.65%); and, *Fresh, dry and candied fruits* (12.01%).

In the behavior of the hidden inflationary rate, the evolution of the prices of the tortilla and bread products were determinant, which jointly explain 30.06% of the hidden inflation in 2005.



**FIGURE 6**  
**CONSUMER PRICE INDEX**  
**INFLATIONARY RATE**  
**TOTAL AND HIDDEN INDEX**  
**YEAR 2005**



Source: Instituto Nacional de Estadística.

### 3. Imported inflation

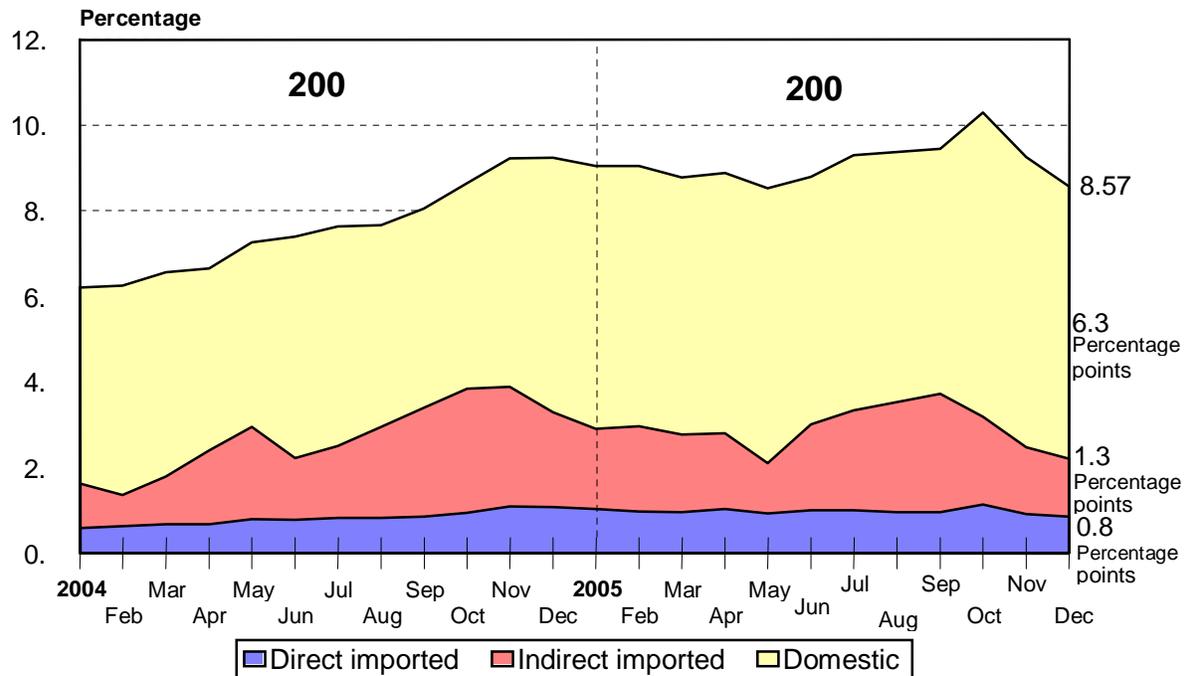
The behavior of the inflationary rate registered during the year, as indicated, was significantly influenced by the imported inflation, which, at the same time, mainly replied to the increase of the international oil price. For analysis purposes, the imported inflation can be divided in direct and indirect. The direct refers to the effect that the international oil price has on the prices of 32 goods and services of the basic food goods, which in their cost structure intensively use oil derivatives. The calculation of the same is possible because the statistical information from the national accounts that were prepared based on the National Accounts System of 1993 -SCN93-[Acronym in Spanish.], allows counting on the structure of the costs production of these goods and services. On the other hand, the indirect imported inflation (second-round effect), refers to the increase of prices of those goods and services that in their costs structure do not incorporate oil derivatives, but that are



indirectly affected by aspects such as the increase in the price of transport, electricity and others.

In that sense, it is important to indicate that, in 2005 the imported inflation explained 2.21 percentage points of the total inflationary rate (8.57%), from which 0.85 percentage points corresponded to the direct imported inflation and 1.36 percentage points to the indirect imported inflation.

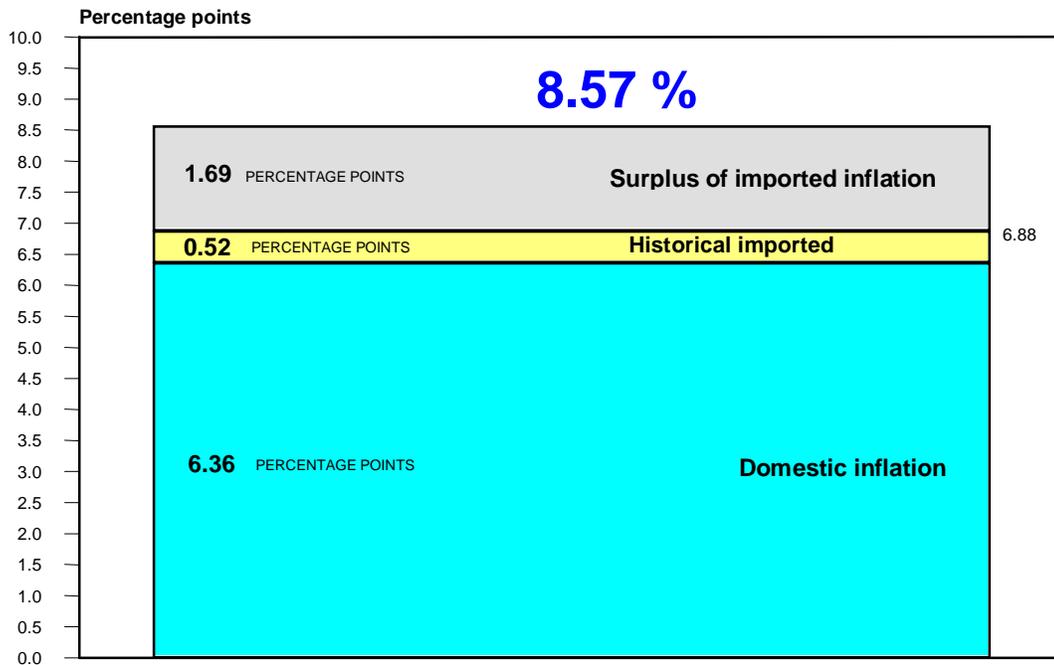
**FIGURE 7**  
**IMPORTED INFLATION**  
**INCIDENCE IN THE INFLATIONARY RATE**  
**CPI BASE DECEMBER 2000 = 100**  
**YEARS 2004 - 2005**





Finally, during the 2001–2003 period, as an average, 0.52 percentage points of the inflation corresponded to the imported inflation, not only direct but also indirect. During those years, the behavior of oil prices was stable; therefore, said average can be considered as a normal historical rate. Therefore, if the reference average is deducted to the imported inflation data to December 2005 (2.21 percentage points), a surplus of imported inflation of 1.69 percentage points<sup>18</sup> is obtained. In that sense, as shown in the following figure, if the imported inflation surplus is deducted to the total inflation (8.57%), the inflationary rate to December should have been of 6.88%.

**FIGURE 8**  
**COMPOSITION OF THE INFLATION'S INCIDENCE**  
**IMPORTED IN THE INFLATIONARY RATE**  
**December 2005**



<sup>18</sup> The increase in the international oil price constitutes a determining factor of the imported inflation surplus. In 2005, said factor continued being one of the main causes that conditioned the inflationary rate as in 2004. During 2005, the international oil price registered a persistent trend to the increase; in the second semester it was placed in record rates several times, reaching on August 30th the highest historical closing price in the New York Merchandise Exchange (US\$69.81 per barrel).



## IV. BALANCE OF INTERNATIONAL PAYMENTS

### A. GENERAL STATEMENTS

At the end of 2005, the payment balance registered an increase of net international monetary reserves of US\$254.4 million, result that was determined by a surplus of US\$1,641.7 million in the capital account, which allowed financing the deficit in the current account of US\$1,387.3 million. The balance of the current account is explained by the deficit of the balance of trade of US\$5,433.8 million and by the surplus not only of the balance of services of US\$489.0 million, but also of the net current transfers of US\$3,557.5 million. On the other hand, the balance of the capital account was determined by the continuous income of capital to the country, associated with positive expectations derived from the macroeconomic stability, as well as with the relatively low levels of interest rates in the international market.

Regarding the exchange rate of the *quetzal* with regard to the dollar of the United States of America, it registered a nominal appreciation of 1.8%, from Q7.75 per US\$1.00 on December 30<sup>th</sup>, 2006 to Q7.61 per US\$1.00 on December 29<sup>th</sup>, 2005. Said appreciation was generated, among other causes, by the international depreciation phenomenon of the dollar of the United States of America (derived from the relaxing of the fiscal and monetary policies that said country applied in the recent past), which propitiated the income of capitals to emerging economies as Guatemala, as well as from the positive differentials between the domestic and foreign interest rates. Regarding the foreign public debt, to December 31<sup>st</sup>, 2005, it was placed in US\$3,723.2 million, lower in US\$120.7 million than the registered on December 31<sup>st</sup>, 2004 (US\$3,843.9 million). This result was due to the amortization of said debt, not only from the public sector of US\$118.7 million, but also from the *Banco de Guatemala* of US\$2.0 million.



## **B. PAYMENT BALANCE**

### **1. Current operations**

The current account of the payment balance, as indicated, registered a deficit of US\$1,387.3 million, higher by US\$176.6 million than the registered in 2004 (US\$1,210.7 million), which meant that the current account/GDP relation remained in 4.4%, as in 2004. This result is explained by the deficit of US\$5,433.8 million in the balance of trade, which was cleared, on one hand, by the surplus registered in the accounts of services and net current transfers, which were of US\$489.0 million and of US\$3,557.5 million, respectively; the first, lower in US\$138.9 million and the second, higher by US\$512.9 million than the registered in 2004.

#### **a) Exports**

The FOB value of the exports was of US\$3,378.5 million, higher by US\$450.1 million (15.4%) than the registered in 2004. In this result was determinant the increase in the exports of the Main Products sector of US\$235.6 million, which grew in 23.6%, as well as the Other Products sector, which increased by 11.1% (US\$214.5 million) regarding 2004. The dynamism of this last sector in 2005 is explained by the increase in the exports to Central America of 12.5% and exports to the rest of the world of 8.5%. The value of coffee exports was of US\$464.0 million, higher by US\$136.1 million (41.5%) than the registered in 2004. This result was due to the increase of 45.9% in the average export price per quintal, from US\$72.54 in 2004 to US\$105.83 in 2005; while the exported volume was reduced in 135.9 thousand of quintals, from 4,520.1 thousand of quintals in 2004 to 4,384.2 thousand of quintals in 2005. According to the International Coffee Organization -ICO-, the increase in the international price of coffee is explained by the reduction of the world coffee offer originated from the fall in the production, mainly from Brazil and Vietnam. In effect, the weather in Brazil affected the production, due to low temperatures and excessive pluvial precipitation in the main coffee producing states; while in Vietnam a drought affected the plantations of said grain.



Regarding the sugar export value, it was of US\$236.5 million, higher by US\$48.5 million (25.8%) than the registered in 2004. This increase is explained not only by the increase in the average export price per quintal, but also by the increase in the exported volume. Regarding the average price per quintal, it increased from US\$7.49 in 2004 to US\$8.45 in 2005. The increase of the sweetener price in the world market was mainly due to the reduction of the offer from Brazil, due that it destined a high part of its harvest to the production of ethanol, as a result of the increase in the international oil price. On the other hand, the exported volume increased by 2,877.2 thousand of quintals (11.5%), from 25,099.8 thousand of quintals in 2004 to 27,977.0 thousand of quintals in 2005. The increase in the exported volume is explained, according to the *Asociación de Azucareros de Guatemala -AZASGUA-*, by the increase in the demand from the People's Republic of China and of the United States of America.

Regarding the banana export value, it was of US\$236.2 million, amount higher by US\$8.0 million (3.5%) regarding the observed in 2004. This increase was due to the increase in the exported volume, from 22,038.8 thousand of quintals in 2004 to 22,723.1 thousand of quintals in 2005, to the increase in the average export price, which increased from US\$10.35 in 2004 to US\$10.39 in 2005. Said behavior was due to the higher yield of the plantations in the Southern area of the country.

The cardamom export value reached an amount of US\$70.4 million, lower in US\$3.4 million (4.6%) than the registered in 2004. This result was due to the reduction of 13.9 % in the average export price per quintal, which from US\$118.84 in 2004 was reduced to US\$102.35 in 2005. It is important to indicate that the behavior in the international price of cardamom was mainly due to the accumulation of inventories of this product from India, derived that the cardamom producers of said country foresaw an increase in the demand, as a result of the celebration of the Ramadan. However, said increased was not observed because, mainly, the Singaporean businessmen previously distributed the product in the markets of Saudi Arabia and other Arabian countries; this cardamom was acquired



from Guatemalan producers. On the other hand, the exported volume increased by 10.8% regarding 2004.

Regarding the oil exports value it was of \$225.1 million, higher by US\$46.4 million (26.0%) than the observed in 2004. Said increase was mainly determined by the increase in the average export price per barrel, which from US\$26.25 in 2004 increased to US\$36.26 in 2005. On its part, the exported volume, in barrels, was lower in 599.5 thousand, from 6,807.0 thousand in 2004 to 6,207.5 thousand in 2005. The increase in the international oil price was originated, among other factors, from the world oil deficit, derived from the increase in the demand of the large economies in expansion, mainly, from the United States of America and the People's Republic of China, as well as from the inelasticity of the world offer regarding the price, which coincided with the discontinuation of oil platforms in the Gulf of Mexico, due to the damages caused by the Katrina and Rita hurricanes. Regarding the exported volume, it was influenced by the reduction in the national production, as a result of lower yields in some oil wells, due to the reduction in the pumping pressures of the same.

Regarding the export value of the Other Products sector, in 2005, it was of US\$2,146.3 million, higher by US\$214.5 million (11.1%) than the registered in 2004 (US\$1,931.8 million). This result, as indicated, is explained by the increase of the exports to Central America and to the rest of the world, which registered an increase of 12.5% and of 8.5%, respectively.

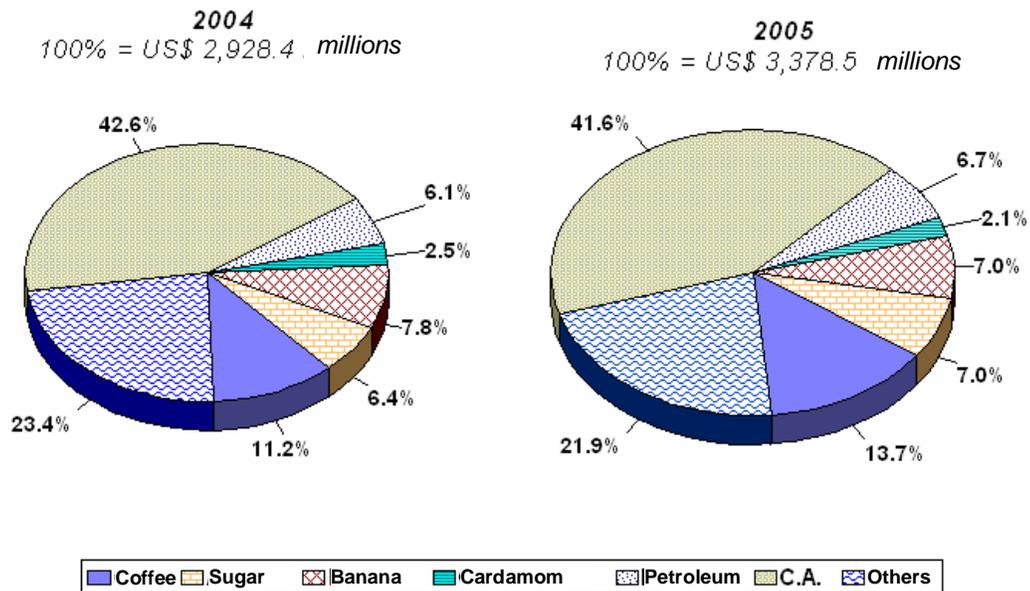
In effect, the exports destined to El Salvador were of US\$617.3 million; Honduras of US\$378.7 million; Nicaragua of US\$205.8 million; and, Costa Rica of US\$202.4 million. The goods exported to this region that stand up are the following: chemical products of US\$332.0 million; food products of US\$193.0 million; construction materials of US\$134.2 million; plastics of US\$110.5 million; fruits and preparations of US\$88.4 million; cosmetics of US\$78.5 million; and, paper and cardboard articles of US\$65.4 million.

Regarding the exports to the rest of the world, highlights the increase in the fruits and preparations sector of US\$22.5 million; clothing of US\$20.0 million; chemical products of US\$17.0 million; natural rubber of US\$7.8 million; **lumber** of



US\$5.7 million; plants, seeds and flowers of US\$4.5 million; and, metallic products of US\$1.5 million.

FIGURE 9  
FOB EXPORTS  
(Percentage composition)



In 2005 the exports were destined to 122 countries, where highlight the United States of America with 31.0%; El Salvador, 18.3%; Honduras, 11.2%; Nicaragua, 6.1%; Costa Rica, 6.0%; Mexico, 3.6%; Panama, 2.2%; Switzerland, 2.1%; Canada, 2.0%; Germany, 1.9%; Dominican Republic, Japan and People's Republic of China 1.1% each; and, Netherlands, Belize and Saudi Arabia 1.0% each; while to the rest of countries only 9.3% of the total value was exported.

### b) Imports

The CIF value of imports in 2005 was of US\$8,812.3 million, higher by US\$1,000.7 million (12.8%) than the registered in 2004. This result is mainly explained by the increase of the international oil prices and derivates, as well as by the increase in the induced import demand, on one hand, by the appreciation of the



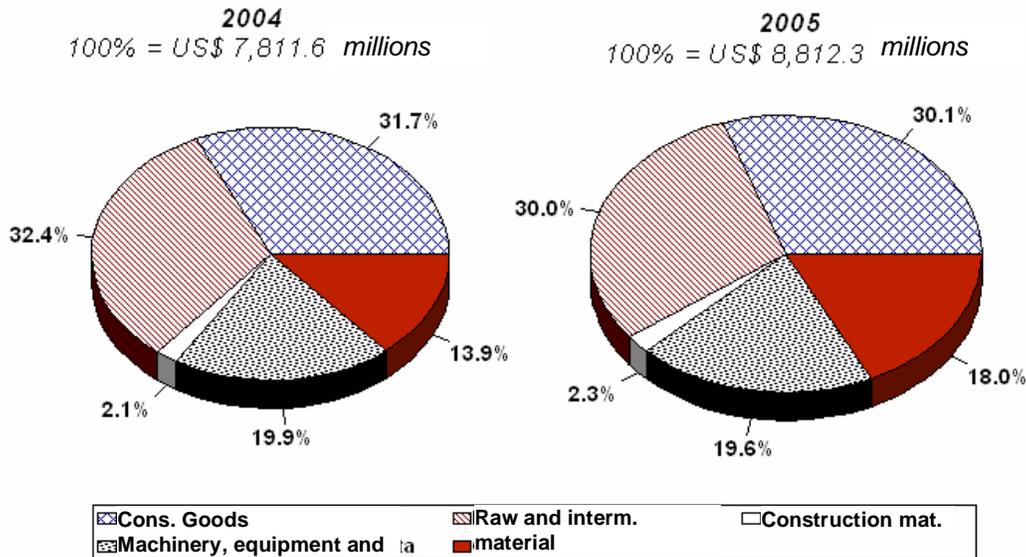
nominal exchange rate and, on the other, by the dynamism of the real economic activity.

Regarding the imports per type of good, the Consumption Goods were of US\$2,656.7 million, showing an increase of 7.2% regarding 2004. In this group, mainly highlights the behavior of the Non-Durable Consumption Goods which registered an amount of US\$1,358.2 million, higher by US\$134.0 million (10.9%) than the observed in 2004. Regarding the imports of Raw Materials and Intermediate Products, these were of US\$2,640.2 million, higher by US\$112.2 million (4.4%) regarding the previous year. Within this sector, highlight the industrial and agricultural sectors, which increased by 4.1% and 7.7%, respectively. On the other hand, the imports of Fuels and Lubricants were of US\$1,584.0 million, higher by US\$495.3 million (45.5%) than the registered in 2004. It is important to indicate that the increase in the import value of Fuels and Lubricants was influenced by the increase of the international price of said products, highlighting the increase in the import value of the following products: diesel 63.7%, propane gas 44.0% and gasoline of 40.6%. On the other hand, the imports of Construction Materials grew in 20.7%, from US\$166.9 million in 2004 to US\$201.4 million in 2005; while the imports of Machinery, Equipment and Tools showed an increased of 11.6% regarding 2004, while being of US\$1,729.6 million; highlighting the increase of 14.8% in the Capital Goods for the Industry, Telecommunications and Construction.

Regarding the relative structure of the imports per country, it was similar to the ones of the previous years. In effect, 39.4% was derived from the United States of America, 8.5% from Mexico, 5.5% from El Salvador, 4.6% from Panama, 3.8% from Costa Rica, 2.9% from Japan, 2.6% from Switzerland, 2.5% from Brazil, 2.2% from Germany, 1.7% from Colombia, 1.6% from South Korea, 1.5% from Honduras, 1.4% from Canada, 1.3% from Spain, 1.1% from Netherlands Antilles, 1.0% from Taiwan and 18.4% from other countries.



FIGURE 10  
CIF IMPORTS CUODE ECONOMIC GROUP\*  
(Percentage composition)



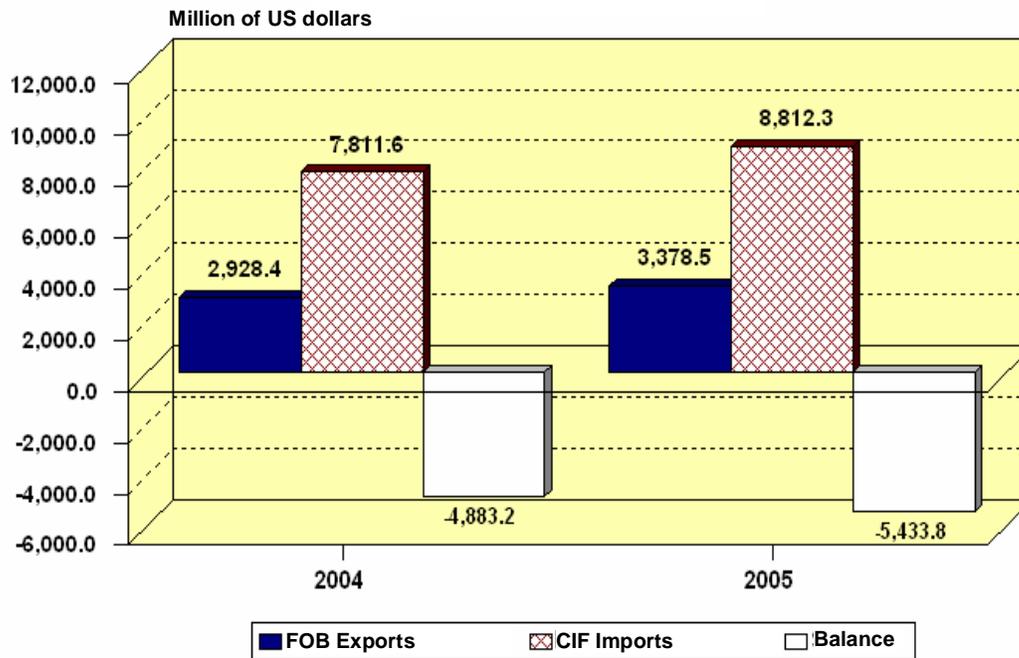
\*Clasificación Uniforme por Origen y Destino Económico.

### c) Balance of trade

The balance of trade in 2005 registered a deficit of US\$5,433.8 million, higher by US\$550.6 million (11.3%) than the observed in 2004, due that the increase of US\$1,000.7 million in the imports surpassed the increase of US\$450.1 million in the exports. The observed deficit represented 17.2% of the GDP, percentage lower than the registered in 2004 (17.9%).



FIGURE 11  
COMMERCIAL BALANCE  
YEARS 2004-2005



#### d) Services and transfers

The services registered a surplus of US\$489.0 million, lower in US\$138.9 million than the observed in 2004, as a result of a reduction of US\$118.9 million in the surplus of the non-factorial services and of an increase of US\$20.0 million in the deficit of the factorial services. In the behavior of the non-factorial services influenced the surplus registered by the Tourism and Travel and Other Services sectors. In effect, the surplus of the Tourism and Travel sector was of US\$401.8 million, higher by US\$16.0 million than the registered in 2004 (US\$385.8 million). Said results was due to the increase of the number of tourists that visited the country.

Regarding the surplus of the Other Services sector, it was of US\$441.2 million, lower in US\$159.4 million than the registered in 2004; result that was



mainly determined by the behavior of the Transformation Services (Manufacturer) sector, which registered a net balance of US\$322.1 million, lower in US\$117.1 million than the registered in 2004. This reduction is mainly associated with the releasing of the textile quotas for the People's Republic of China<sup>19</sup>.

On the other hand the Transport and Insurance sector, registered a surplus of US\$21.8 million, in contrast with the deficit observed in 2004 (US\$2.7 million).

The Factorial Services registered a deficit balance of US\$375.8 million, higher by US\$20.0 million regarding the observed in 2004, as a result, mainly, of higher expenses abroad due to the payment of interests of the foreign public debt.

Finally, the balance of the net current transfers continued being high while being of US\$3,557.5 million, higher by US\$512.9 million than the registered in 2004. In this sector highlights the net income per family remittances, which was of US\$2,959.5 million, higher by US\$441.4 million (17.5%) than the registered in 2004 (US\$2,518.1 million).

## **2. Operations of capital**

The capital account of the payment balance registered a surplus of US\$1,641.7 million, lower in US\$177.7 million than the one of 2004. This result is mainly explained by the reduction of the surplus balance of the Transfer of Capital sector and by the deficit balance of the Official and Banking Capital sector.

Regarding the Transfers of Capital (Net)), these were of US\$125.3 million, lower in US\$10.0 million than the registered in 2004 (US\$135.3 million).

On the hand, the Official and Banking Capital registered a deficit balance of US\$83.9 million, which contrasts with the surplus observed in 2004 (US\$249.3 million). Said deficit balance is associated with a lower amount of disbursement of loans for the non-financial Public Sector. Finally, the Private Capital sector registered a surplus balance of US\$1,600.3 million, higher by US\$165.5 million than the observed in (US\$1,434.8 million). While disaggregating said sector, the

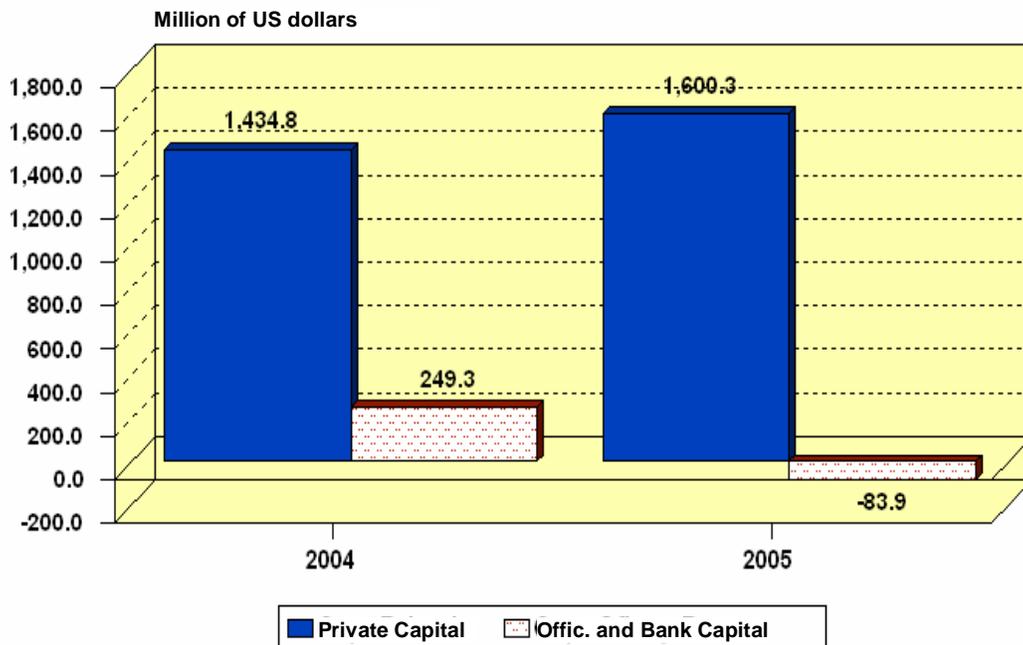
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<sup>19</sup> According to the *Comisión de la Industria de Vestuario y Textiles* of the *Asociación Gremial de Exportadores de Productos No Tradicionales -AGEXPRONT-*, with the finalization of the system of import quotas established by the World Trade Organization –WTO- in the General Agreement of Textiles and Clothing, the People's Republic of China increased its participation in the North American market.



Direct Investment was of US\$208.0 million, higher by US\$53.3 million than the registered in 2004. The Middle and Long Term Capital registered a surplus of US\$648.1 million, lower in US\$27.4 million than the one of 2004, associated with a slight reduction in the demand of foreign funding by the private sector, due to the increase in the interest rate in the international financial market. Regarding the short-term capital, it showed a surplus balance of US\$744.2 million, higher by US\$139.6 million than the one of 2004 (US\$604.6 million), which was mainly due to the higher use of credit lines abroad by the private Guatemalan sector.

FIGURE 12  
CAPITAL OPERATIONS (NET)  
YEARS 2004-2005





### 3. International Monetary Reserves

As a result of the current and capital operations of the payment balance, the net international monetary reserves were of US\$3,782.4 million; amount higher by US\$254.4 million than the observed on December 31<sup>st</sup>, 2004 (US\$3,528.0 million). This increase is mainly explained by the purchase of foreign currency made by Central Bank in the exchange market to moderate the volatility in the nominal exchange rate, by the yields obtained in the investment of said reserves abroad and by the royalties for the Central Government due to oil exploitation. The rate of net international monetary reserves in 2005 reached the equivalent to 4.3 months of import of goods and non-factorial services (4.4 months in 2004), which indicates that the country's foreign position continued being favorable.

FIGURE 13  
NET INTERNATIONAL MONETARY RESERVES  
YEAR 2005



### C. NOMINAL EXCHANGE RATE

To December 29<sup>th</sup>, 2005, the weighted average exchange rate in the institutional market of foreign currency, as indicated, registered an appreciation of



Q0.14 (1.8%), from Q7.75 per US\$1.00 on December 31<sup>st</sup>, 2004 to Q7.61 per US\$1.00 on December 29<sup>th</sup>, 2005.

The behavior of the exchange rate during 2005 can be analyzed in four periods: the first one, which covers from December 30<sup>th</sup>, 2004 to April 5<sup>th</sup>, 2005, in which the exchange rate was appreciated in Q0.17 (2.19%), from Q7.75 per US\$1.00 to Q7.58 per US\$1.00. The referred behavior is mainly associated with the excessive offer of dollars of the United States of America in the international markets, generated by the expansive monetary and fiscal policies recently applied by said country.

It was observed in the second period, which covers from April 6<sup>th</sup> to September 13<sup>th</sup>, 2005, that the nominal exchange rate stopped appreciating, because from Q7.58 per US\$1.00 it decreased to Q7.60 per US\$1.00, which is a depreciation of Q0.02 (0.26%). Said behavior was due to seasonal factors, as well as to a reduction of capital income towards the country, somehow derived from the reduction of the differentials between the domestic and foreign interest rates, which at the same time obeys to the increase of the interest rate objective of federal funds from the Federal Reserve of the United States of America.

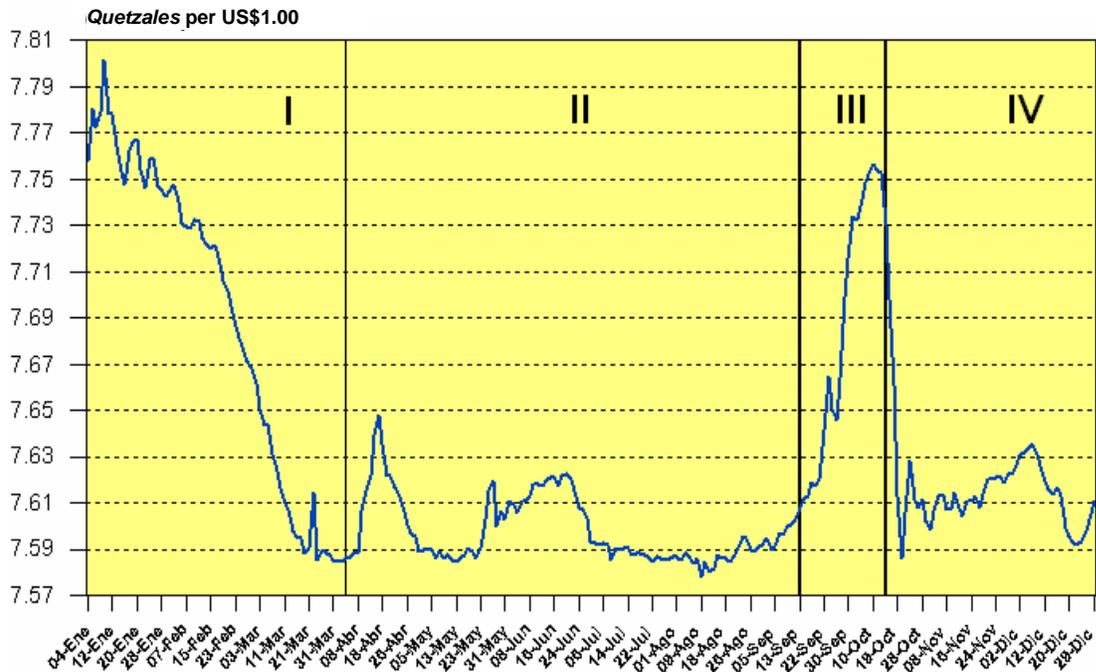
In the third period, which covers from September 14<sup>th</sup> to October 16<sup>th</sup>, the exchange rate passed from Q7.60 per US\$1.00 to Q7.75 per US\$1.00, which represented a depreciation of Q0.15 (1.97%), registering a higher volatility associated with the increase in the demand of foreign currency from fuel importer companies.

The last period covered from October 17<sup>th</sup> to December 29<sup>th</sup>, in which the exchange rate decreased from Q7.75 per US\$1.00 to Q7.61 per US\$1.00, which meant an appreciation of Q0.14 (1.81%), which was mainly due to the seasonality of the referred variable.

The following figure shows the behavior of the referred nominal exchange rate.



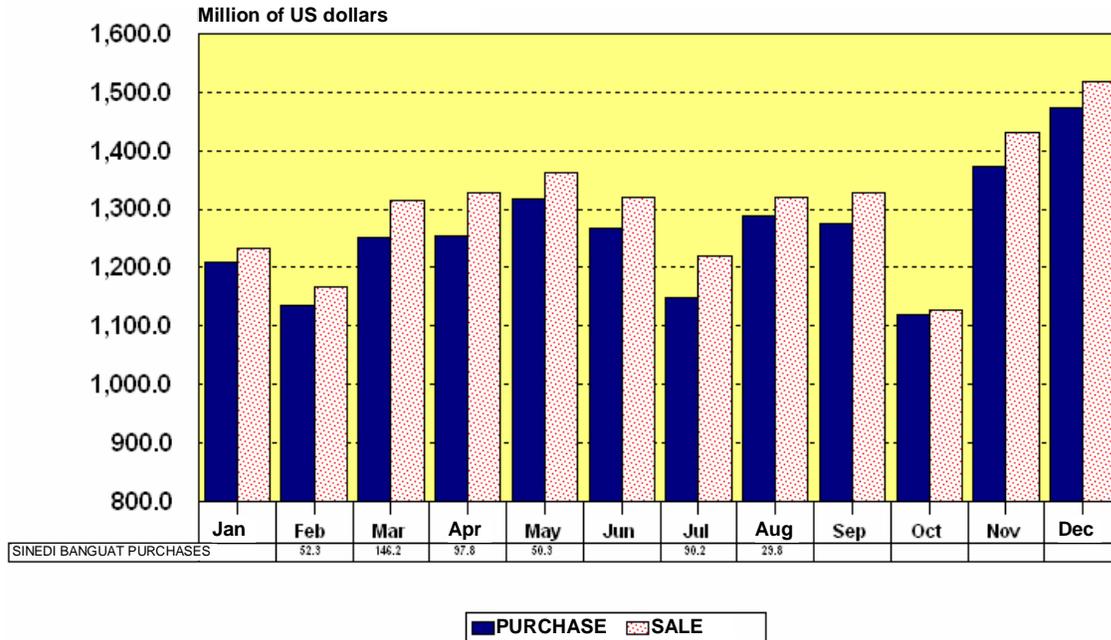
FIGURE 14  
BEHAVIOR OF THE NOMINAL EXCHANGE RATE  
JANUARY-DECEMBER 2005



In the described context, in the framework of lineaments approved in the Monetary, Exchange and Credit Policy for 2005, the *Banco de Guatemala* participated in the exchange market in order to reduce the volatility observed in the nominal exchange rate. In effect, the participation of the Central Bank in the exchange market, through the Foreign Currency Electronic Negotiation System - SINEDI- [Acronym in Spanish.], consisted in purchasing foreign currency in February, March, April, May, July and August for a total of US\$466.6 million. This amount can be considered as minimum, most of all if it is compared with the total amount of operations registered in the institutional market of foreign currency; during 2005, it registered a total of purchases of US\$15,109.1 million and a total of sales of US\$15,667.2 million.



**FIGURE 15**  
**FOREIGN CURRENCY AND SINEDI INSTUTIONAL MARKET**  
 PURCHASE AND SALE OF US DOLLARS  
 YEAR 2005



#### D. REAL EXCHANGE RATE

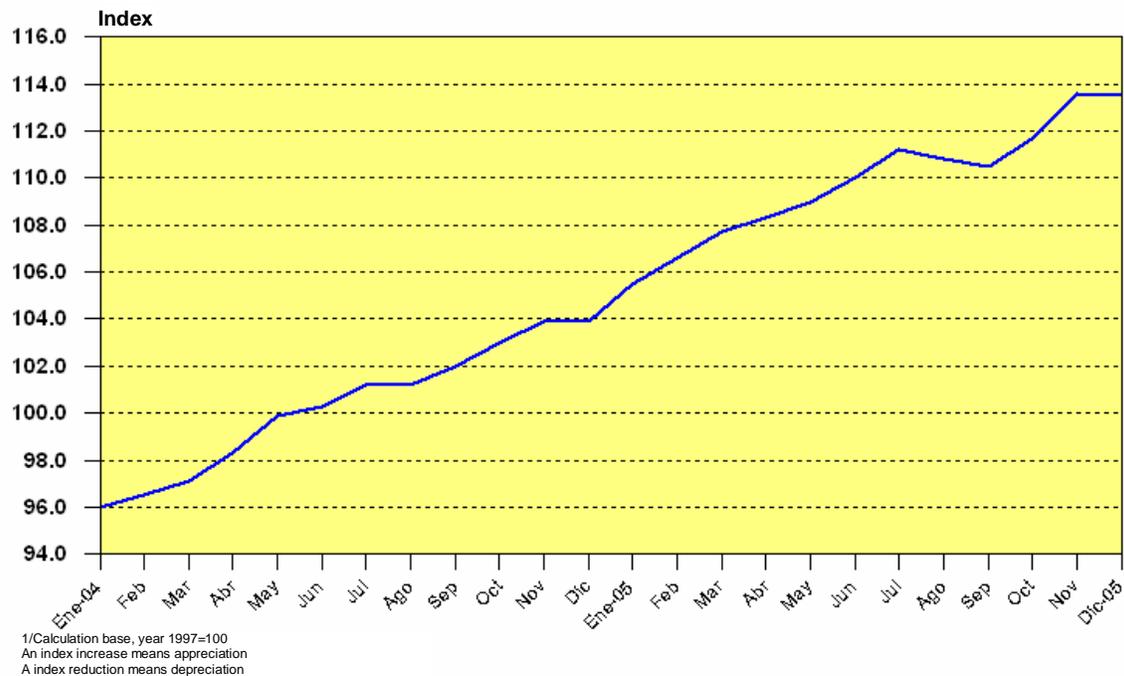
This indicator measures the relation between the nominal exchange rate and the domestic inflation regarding the main commercial associates of the country and is an estimated measure of the exchange direction in the competitiveness of its exportations. As a result of the behavior shown by the nominal exchange rate throughout the year, the domestic inflationary rate and the inflationary rate of the main commercial associates of Guatemala, the Index of the Effective Real Exchange Rate -ITCER- [Acronym in Spanish.] registered by the end of 2005 an appreciation of 9.25%, higher than the observed in 2004 (7.52%).

In effect, the behavior of the ITCER in 2005 is associated with the nominal depreciation of four of the main commercial associates that conform the countries **basket** used to calculate the ITCER (Costa Rica, Honduras, European Union and Japan), with regard to the dollar of the United States of America. Another factor



that influenced the referred behavior was the lower growth rate of the prices in El Salvador, Honduras, United States of America, European Union, Japan and Mexico, compared with the inflation in Guatemala.

FIGURE 16  
INDEX OF THE TOTAL REAL EFFECTIVE EXCHANGE RATE <sup>1/</sup>  
2004-2005



### E. FOREIGN PUBLIC DEBT

To December 31<sup>st</sup>, 2005, the balance of the foreign public debt was of US\$3,723.2 million, lower in US\$120.7 million (3.1%) than the registered during the same period of 2004 (US\$3,843.9 million). This result, as indicated, was due to the amortization of said debt, not only from the non-financial public sector of US\$118.7 million, but also from the *Banco de Guatemala* of US\$2.0 million.

The incomes of the non-financial public sector in matters of disbursement were of US\$142.8 million, from which US\$128.1 million were derived from multilateral organizations and US\$14.7 million from bilateral and governmental organizations. From the total of the disbursements received from multilateral



organizations, US\$51.7 million were provided by the *Banco Centroamericano de Integración Económica -BCIE-*; US\$34.0 million by the Inter-American Development Bank -IDB-; US\$36.5 million by International Bank for Reconstruction and Development -IBRD-; US\$3.1 million by the Organization of the Petroleum Exporting Countries -OPEC-; and, US\$2.8 million by the International Fund for Agricultural Development -IFAD-.

Regarding the amortizations carried out by the non-financial public sector, these were of US\$197.3 million, highlighting the following: IDB, US\$58.6 million; BCIE , US\$48.9 million; IBRD, US\$31.4 million; Government of the United States of America, US\$12.5 million; Agency for International Development (AID), US\$10.5 million; and, Eximbank of China, US\$9.4 million. Besides, the balance of said debt was reduced in US\$64.2 million, derived from the exchange fluctuations of some of the currencies in which part of the same are expressed<sup>20</sup>.

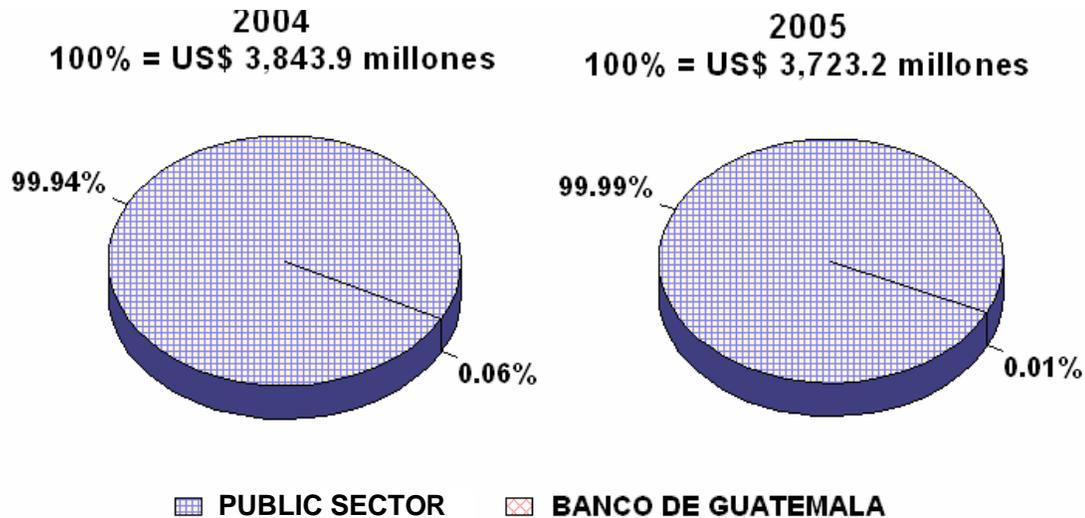
The foreign debt of the *Banco de Guatemala* was reduced in US\$2.0 million, being on December 31<sup>st</sup>, 2005 in US\$0.3 million. Said reduction included US\$1.5 million of regularization on the balances of the financial accounts of the Stabilization Bonds of 1983, 1984 and 1988.

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<sup>20</sup> It is important to indicate that in 2005, the dollar of the United States of America was appreciated regarding the **basket** of currencies composed by the euro, Japanese yen and Swiss franc.



FIGURE 17  
FOREIGN PUBLIC DEBT  
(Percentage composition)



## F. SUSTAINABILITY OF THE FOREIGN PUBLIC DEBT

The sustainability of the foreign public debt can be measured according to the parameters suggested internationally, indicating critical rates for the relations between the foreign public debt and other relevant variables<sup>21</sup>.

In that sense, for the foreign public debt and GDP relation, a critical value of 35% is established. For the case of Guatemala, in 2005 this relation was of 11.8%, lower than the one of 2004 (14.1%). Another relevant indicator is the relation between the balance of the foreign public debt and the total of exports of goods and services, the critical value of which, according to the mentioned parameters, is placed around 150%. With that regard, the result of said relation for 2005 was of 71.8%, lower than the percentage registered in 2004 (81.4%). Besides, a third

<sup>21</sup> According to the parameters suggested by the international financial organizations, the rate of monetary reserves and the foreign position of a country are committed when the relations of the balance of foreign debt regarding the export of goods and services and the relations of the public debt regarding the tax incomes, surpass the established critical rates.



indicator used internationally refers to the relation between the service of the total foreign public debt as a percentage of the tax incomes, which, for the case of Guatemala, in 2005 was of 22.8%, lower than the registered in 2004 (18.8%). It is important to indicate that for said indicator there is no critical value accepted internationally that allows establishing from which percentage a country is considered to be in risk of default of the payment of its obligations, because the interpretation of the same can vary from one country to another, depending on the consistency and solidity in the long term application of sane fiscal policies.

Regarding the mentioned foreign public debt indicators, it is important to mention that, on one hand, the economic literature indicates that the simultaneous detriment of all the mentioned indicators constitute an alarming sign regarding a possible payment crises and, on the other hand, that the detriment of only one indicator, though is not an imminent crises alert, should be a sign of caution in the future indebted management of a determined country. It is particularly concluded that in this last case, it is important that the sustainability of the public debt of a country (and in its consequent effects on the macroeconomic stability) adopts and maintains, in the long term, a disciplined fiscal policy, particularly oriented to strengthen the tax incomes of the State, complemented with a rational execution of the expenditure.

According to the international standards for the sustainability of the foreign debt and the analysis of the rates registered by Guatemala in 2005, it is evident that the rate of foreign public debt of Guatemala is moderate.

## **V. MONETARY AND FINANCIAL SITUATION**

### **A. GENERAL STATEMENTS OF THE MONETARY POLICY**

The Monetary Board, in resolution JM-160-2004 dated December 29<sup>th</sup>, 2004, determined the Monetary, Exchange and Credit Policy for 2005, designed to continue with the adoption process of a complete scheme of explicit inflation goals (*Inflation Targeting*) and oriented to consolidate the stability and confidence in the main macroeconomic and financial variables. In this sense, the main objective of



the referred policy was specified as an inflation goal for the end of the year, established in a range between 4% and 6%, as well as the maintenance of said range during the following twelve months.

The implementation of the monetary policy in 2005 was consistent with the referred scheme, which is based on the selection of the inflation goals as the nominal anchor of said policy and is consolidated with the implementation of a flexible exchange rate regimen, with the use of instruments of indirect monetary control (operations of monetary stabilization, privileging the market's decisions), as well as the higher transparency of the Central Bank's operations.

During 2005, the monetary policy was carried out before, in the foreign order, an evident increase in the oil international price; and, in the domestic order, before the support that the fiscal policy provided to the monetary policy, through the maintenance of a deposits rate in the *Banco de Guatemala* above the programmed, as well as through the formation of positive economic growth expectations from economic agents.

In the mentioned context, to December 2005 the inflationary rate was of 8.57%, lower than the one of December 2004 (9.23%). Though in 2005 the disinflation process foreseen in 2004 could not be materialized consistently, the inflation rate did not increase, though the adverse incidence of exogenous factors and the continuous rise of the international oil price. The above was possible due to application of a prudent and disciplined monetary policy, strongly supported, as indicated, by the behavior of the fiscal policy.

During 2005, the management of the monetary policy was oriented to take the necessary measures that allowed helping in the deceleration of the inflationary rate. In that sense, the Execution Committee of the *Banco de Guatemala*, in order to moderate the inflationary expectations of the economic agents and to send a certain message about the compromise of the Central Bank to continue watching for the stability in the general rate of prices, increased the leading interest rate of



the monetary policy during seven occasions<sup>22</sup>. Besides, in order to increase the effectiveness of the monetary policy, and according to the lineaments of the Monetary Board, actions were adopted to improve the operational procedures of the referred policy, oriented to advance in the adoption process of a complete monetary scheme of explicit inflation goals. With that regard, in 2005, the following measures, among others, were adopted: i) establishment of the leading interest rate of the monetary policy (CDPs up to 7 day-term); ii) scheduling of the decisions of the Execution Committee regarding the changes of the leading interest rate during the next meeting, after day 15 of each month; iii) reduction of the number of bids; and, iv) setting of quotas for the CDPs fund-raising placed by the bid mechanism.

Within the indicative or reference variables of the monetary policy, at the end of 2004, it was estimated that the total payment means (M2) would increase in 2005 between 10% and 12%, in inter-annual terms; while the total banking credit to the private sector should have increased between 11.5% and 13.5%. By the end of 2005, the inter-annual growth rate M2 (which includes national and foreign currency) was of 14.7%. On the other hand, the banking credit to the private sector had an inter-annual growth of 21.4%.

## **B. EVOLUTION OF THE MAIN MONETARY AGGREGATES**

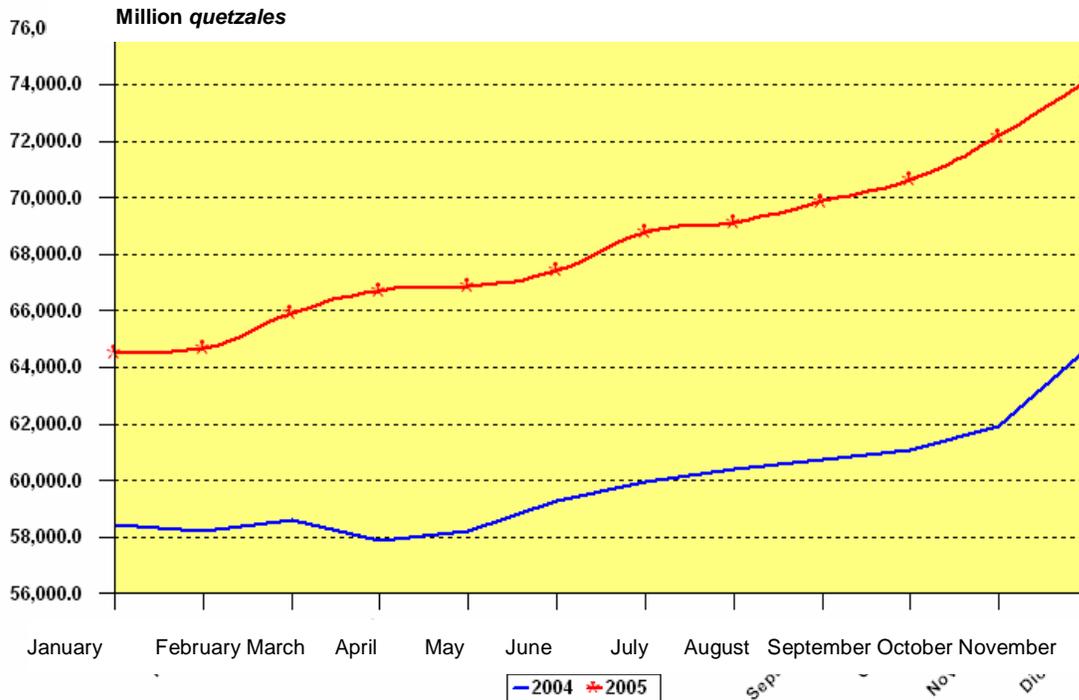
To December 31<sup>st</sup>, 2005, the total average payments were of Q74,182.5 million, which meant a growth of 14.7% regarding the rate registered by the end of 2004.

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<sup>22</sup> February 18 (2.55% to 2.75%); May 20 (from 2.75% to 3.00%); July 22 (from 3.00% to 3.25%); August 19 (from 3.25% to 3.50%); September 16 (from 3.50% to 3.75%); November 18 (from 3.75% to 4.00%); and, December 16 (from 4.00% to 4.25%).



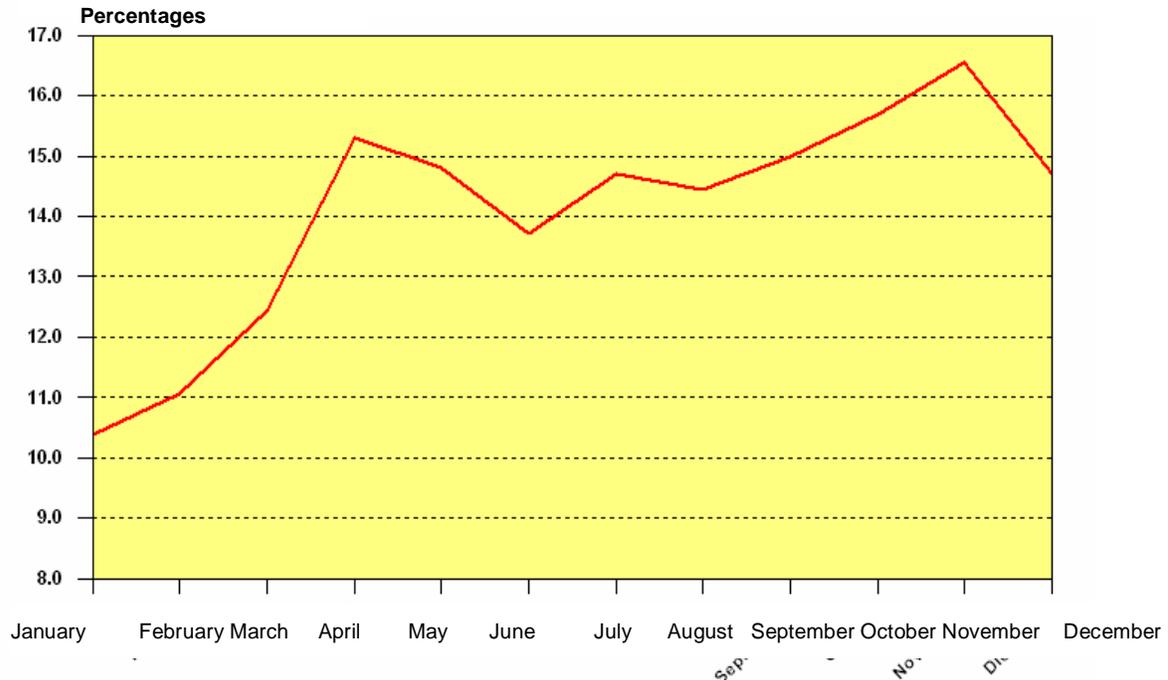
FIGURE 18  
TOTAL PAYMENT MEANS <sup>1/</sup>  
YEARS 2004-2005  
BALANCES



<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included



FIGURE 19  
TOTAL PAYMENT MEANS <sup>1/</sup>  
YEAR 2005

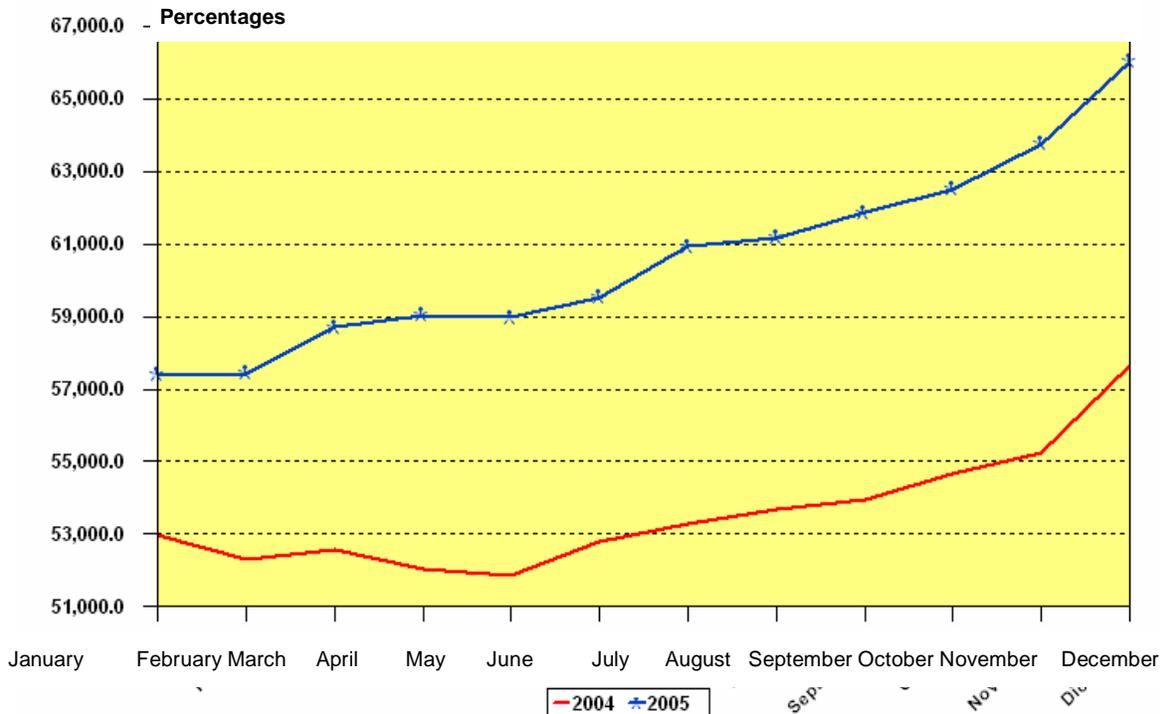


<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included

The payment means in national currency, by the end of the year, were of Q66,043.6 million, higher by Q8,408.2 million (14.6%) than the rate registered in December 2004.



FIGURE 20  
PAYMENT MEANS IN N/C<sup>1/</sup>  
YEARS 2004- 2005  
BALANCES



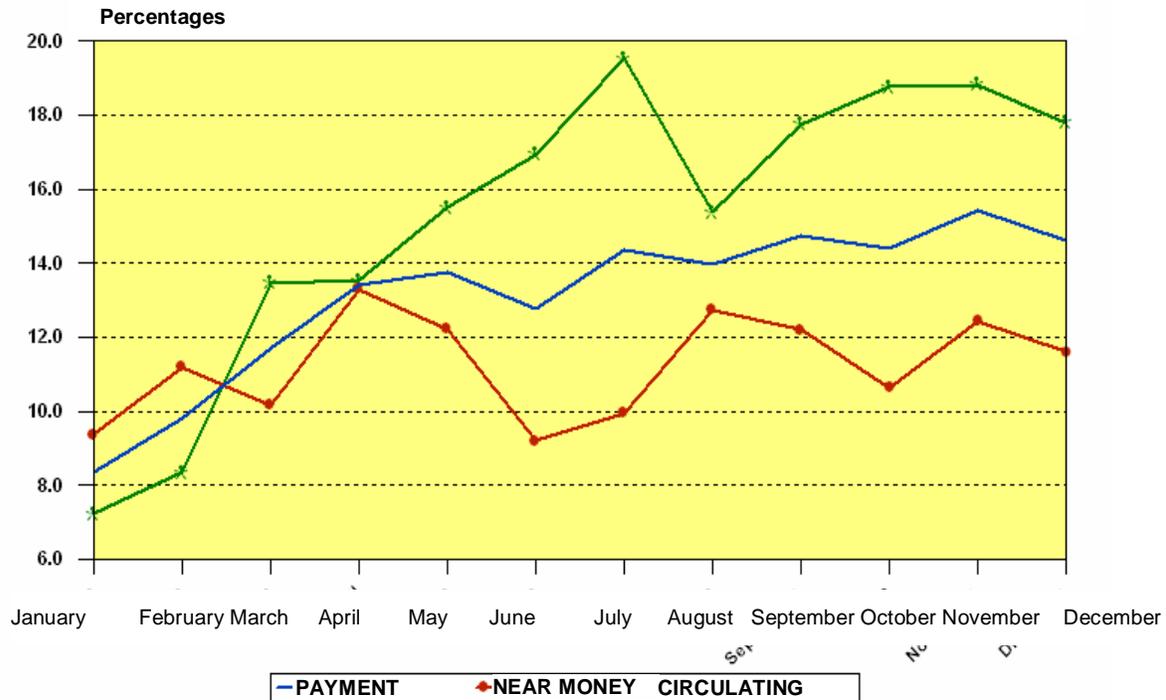
<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included

The percentage structure of the payment means in national currency was similar to the ones of the previous years, representing the current mean 49.7% and the near money 50.3%. The inter-annual growth of both components was of 17.8% and 11.6%, respectively, (6.9% and 8.9%, respectively, in 2004). The components of the current mean, currency in circulation and the monetary deposits registered an inter-annual growth rate of 11.8% and 21.8%, respectively (5.5% and 7.9% in 2004).

The highest inter-annual growth rates of the main monetary aggregates in 2005, regarding the observed in 2004, show an increase of the primary liquidity surplus registered in the economy in 2005 with regard to said surplus in 2004. With that regard, it is important to mention that the currency in circulation increased by Q1,323.4 million, from Q11,192.7 million in 2004 to Q12,516.1 million in 2005.



FIGURE 21  
MAIN MONETARY AGGREGATES IN N/C<sup>1/</sup>  
GROWTH INTER-ANNUAL RATE  
YEAR 2005



<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included

On the other hand, the payment means in foreign currency, by the end of 2005, were of Q8,138.9 million, with an inter-annual growth rate of 15.7% (Q1,106.8 million). Regarding its percentage structure, the monetary deposits represented 42.5% and the near money 57.5%.

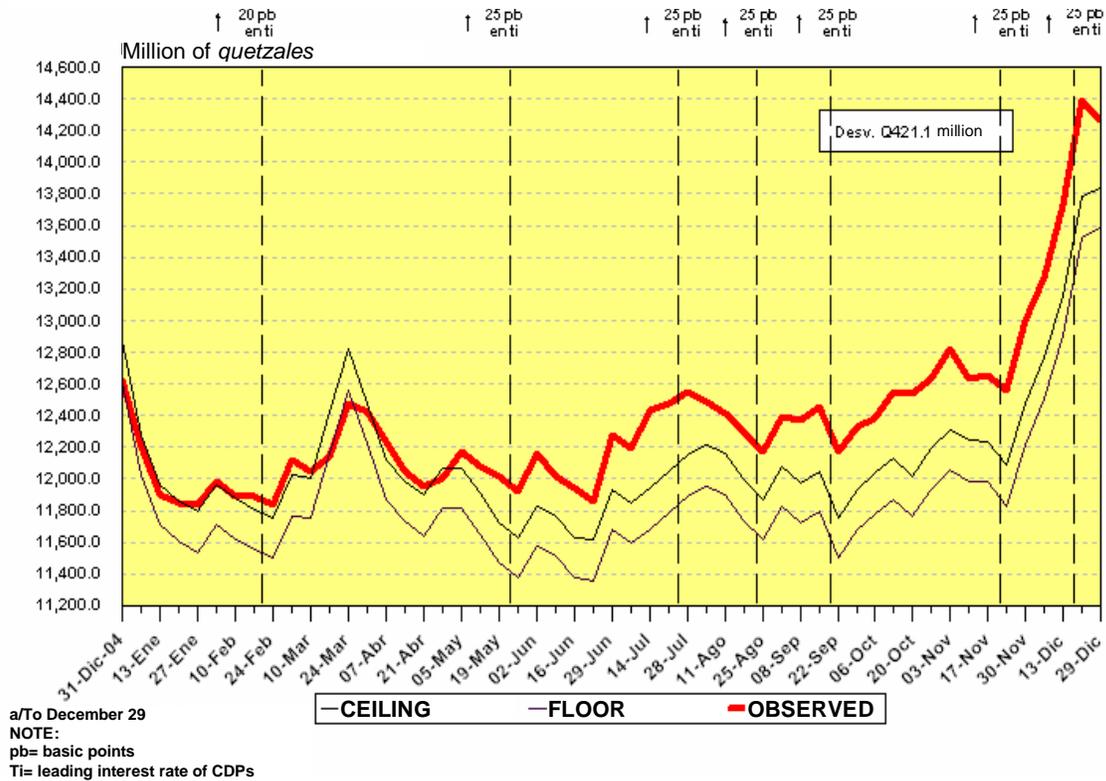
Regarding the monetary issue, according to the revised monetary program<sup>23</sup> for 2005, it was estimated that the demand of monetary issue would increase by the end of the year in about 8.0%, regarding the rate observed by the end of 2004.

The programmed and observed behavior of the monetary issue to December can be observed in the following figure.

<sup>23</sup> The revision of the monetary program was known by the Monetary Board in meeting dated June 8<sup>th</sup> and beared some adjustments derived, on one hand, from including the purchase of foreign currency by the *Banco de Guatemala* in the exchange market, in order to moderate the exchange volatility in the second trimester of the year and, on the other hand, from a revision carried out by the *Ministerio de Finanzas Públicas* of the amount of programmed disbursements of foreign debt.



**FIGURE 22**  
**PROGRAMMED AND OBSERVED MONETARY ISSUE**  
**YEAR 2005 <sup>a/</sup>**



During the period that covers from January 2<sup>nd</sup> to 20<sup>th</sup>, 2005, the course of the monetary issue remained within the programmed broker, due to the demonetizing effect generated by the increase of the operations of monetary stabilization with the private sector of about Q1,645.0 million.

Later, from January 21<sup>st</sup> to March 10<sup>th</sup>, the monetary issue was slightly higher than the ceiling of the referred broker, registering an average deviation of Q54.4 million. The issue surplus observed since the end of January is mainly explained, regarding the offer, by the higher monetization abroad –which in net terms were of Q652.0 million (US\$81.5 million)- mainly originated from the purchase of foreign currency by the *Banco de Guatemala* in the exchange



market<sup>24</sup>, which was mainly cleared by the demonetizing effect of the increase of the rest of the public sector's position of Q785.4 million, which includes a higher deposits rate of the Central Government in the *Banco de Guatemala* of Q584.1 million. On the other hand, the behavior of the operations of monetary stabilization with the private sector in said period was monetizing, while reducing the balance of said operations in Q1,024.7 million.

In the period that covers from March 11<sup>th</sup> to 31<sup>st</sup>, the monetary issue was below the floor of the programmed broker, in order to finalize the trimester within the referred broker. Said situation is explained by the demonetizing effect derived from the increase in the deposits rate of the Central Government in the *Banco de Guatemala* of about Q493.0 million.

During April the monetary issue, in general, was around the ceiling of the programmed broker, registering an average deviation of Q71.8 million, associated, on one hand, with the reduction in the total balance of the operations of monetary stabilization of about Q568.0 million and, on the other hand, with the foreign monetization of Q568.8 million (about US\$71.0 million), mainly derived from the purchase of foreign currency by the *Banco de Guatemala* in the exchange market of US\$65.0 million.

During the period that covers from May 1<sup>st</sup> to December 29<sup>th</sup>, the behavior of the monetary issue was above the ceiling of the programmed broker, registering an average deviation of Q379.1 million. The surplus of monetary issue observed in said period, is mainly explained, in matters of offer, by the domestic monetization, derived from the reduction of the deposits of the central government in the *Banco de Guatemala* of Q2,994.1 million; by the increase of the other net assets of the Central Bank of Q618.4 million, mainly originated from the highest rate of expenses regarding the products; by the reduction of the balance of the operations of monetary stabilization with the private sector in foreign currency of Q210.0 million; and, by the foreign monetization of Q108.0 million (US\$13.5 million), mainly

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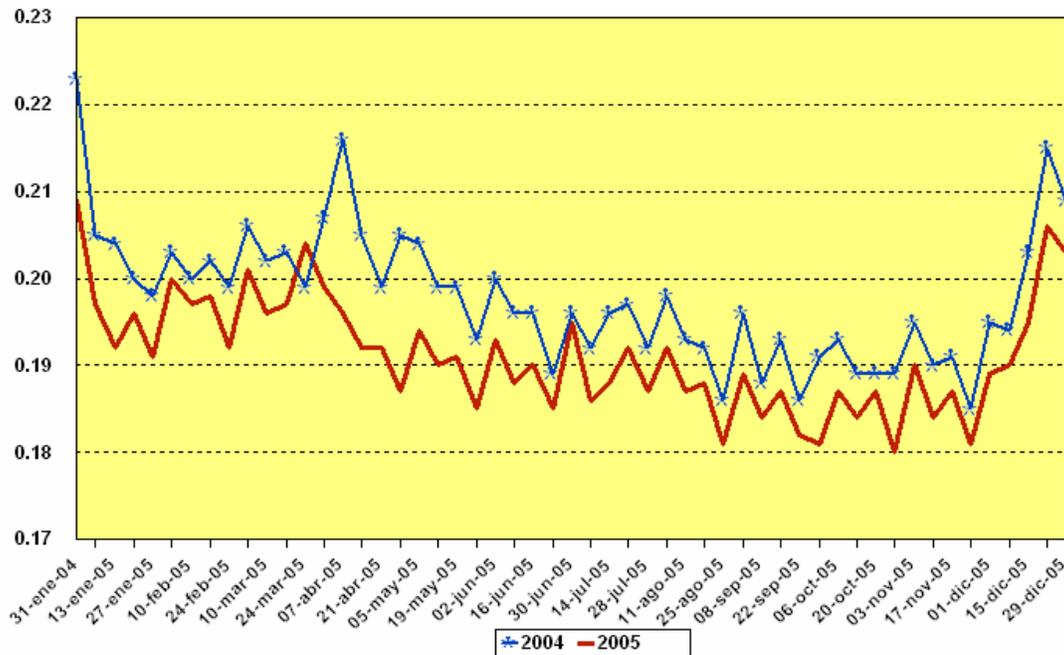
<sup>24</sup> The *Banco de Guatemala*, according to the Monetary, Exchange and Credit Policy of 2005, started participating in the exchange market since February 22nd, purchasing US\$106.4 million since that date until March 10<sup>th</sup>.



associated with the purchase of foreign currency by the *Banco de Guatemala* in the exchange market to moderate the volatility in the nominal exchange rate. The mentioned monetizing factors were partially cleared by the increase of the balance of the operations of monetary stabilization with the private sector in national currency of Q803.6 million, by the increase of the position of the rest of the public sector of Q608.5 million and by the increase in the total position of the system's banks with the *Banco de Guatemala* of Q426.1 million.

Within the demand factors that contributed in moderating the deviation of monetary issue by the end of the year, it is important to mention the coefficient of the public's liquidity preference, which was reduced in 2005; this situation allowed the inter-annual growth rate to decelerate at the end of the year.

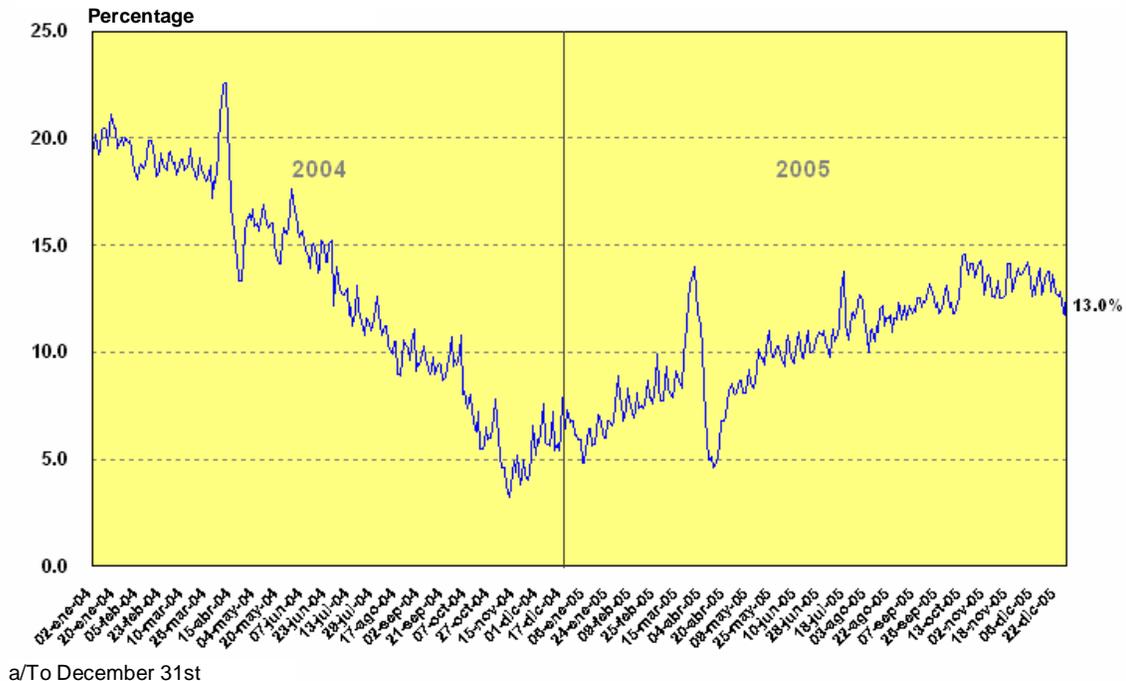
**FIGURE 23**  
**COEFFICIENT OF LIQUIDITY PREFERENCE (c)**  
**YEARS 2004-2005 <sup>a/</sup>**



C= money in circulation/total deposits in the banking system  
a/To December 31st



**FIGURE 24**  
**MONETARY ISSUE**  
**INTER-ANNUAL RELATIVE VARIATION**  
YEARS 2004-2005 <sup>a/</sup>



In relative terms, the average deviation of the monetary issue during the year was of about 2.0% regarding the average balance of the monetary issue; therefore, the same can be considered as moderated. It is important to indicate that econometric studies carried out in 2005 indicate that the sensibility of the Consumer Price Index -CPI- before increases in the deviation of the monetary issue is little significant, due that an increase of 1% in the referred deviation increased the CPI in 0.00345%, with a delay of 12 months.

Regarding the multiplier of the payment means in national currency, in 2005 was placed between 3.22 and 3.24, showing an evident stability. This behavior is due to the combined effect observed in the two coefficients that compose the multiplier; the first one refers to the coefficient of the public's liquidity preference, which was reduced from 0.1876 in January to 0.1833 in December, which reflects a slight reduction of the liquidity surplus that the non-banking private sector maintained. Regarding the second coefficient, it refers to the banking retention,



increased from 0.1491 in January to 0.1529 in December, showing the surplus of the banking cash.

YEARS	MILLION OF QUETZALES					COEFFICIENT OF THE PUBLIC'S LIQUIDITY PREFERENCE F = A / E	COEFFICIENT OF BANKING RETENTION G = B / D	MULTIPLIER 1 / (G + F(1 - G))
	MONEY IN CIRCULATION	BANKING CASH	MONETARY BASE	DEPOSITS PLUS MORTGAGE AND COLLATERAL BONDS	PAYMENT MEANS			
	A	B	C = A + B	D	E = A + D			
DEC. 2001	7,208.7	4,988.0	12,196.7	34,312.8	41,521.5	0.1736	0.1455	3.41
DEC. 2002	8,039.6	5,857.0	13,896.6	37,709.6	45,749.3	0.1757	0.1552	3.30
DEC. 2003	9,027.3	6,376.3	15,403.6	40,886.1	49,913.4	0.1809	0.1560	3.24
DEC. 2004	10,119.2	6,518.6	16,637.8	43,729.2	53,848.4	0.1879	0.1491	3.24
2005								
JANUARY	10,167.1	6,566.0	16,733.1	44,026.6	54,193.8	0.1876	0.1491	3.24
FEBRUARY	10,218.7	6,672.5	16,891.1	44,381.2	54,599.8	0.1872	0.1503	3.23
MARCH	10,295.6	6,743.8	17,039.4	44,794.4	55,090.0	0.1869	0.1506	3.23
APRIL	10,366.2	6,831.5	17,197.7	45,282.8	55,649.0	0.1863	0.1509	3.24
MAY	10,443.4	6,940.7	17,384.2	45,777.3	56,220.7	0.1858	0.1516	3.23
JUNE	10,539.1	7,020.6	17,559.7	46,221.0	56,760.1	0.1857	0.1519	3.23
JULY	10,624.7	7,190.4	17,815.1	46,750.8	57,375.5	0.1852	0.1538	3.22
AUGUST	10,712.9	7,226.7	17,939.6	47,265.0	57,977.8	0.1848	0.1529	3.23
SEPTEMBER	10,815.0	7,284.6	18,099.6	47,802.3	58,617.4	0.1845	0.1524	3.24
OCTOBER	10,899.9	7,410.8	18,310.7	48,350.4	59,250.3	0.1840	0.1533	3.24
NOVEMBER	11,002.2	7,506.8	18,509.0	48,935.6	59,937.7	0.1836	0.1534	3.24
DECEMBER	11,112.5	7,568.8	18,681.3	49,503.6	60,616.1	0.1833	0.1529	3.24

<sup>1/</sup> Does not include banks that have been requested to declare bankruptcy.

### C. CREDIT ACTIVITY OF THE *BANCO DE GUATEMALA*

In 2005 the net position of the non-financial public sector with the *Banco de Guatemala* only reflected variations in the deposits of the Central Government and of the rest of the public sector, derived from the established in article 133 of the Politic Constitution of the Republic of Guatemala, which forbids the Monetary Board to authorize the *Banco de Guatemala* to grant direct or indirect funding, guarantee or endorsement to the State, its decentralized or autonomous entities and non-banking private entities. For that reason, the deposits of the non-financial public sector in the *Banco de Guatemala*, to December 31st, 2005, registered a rate of Q7,359.7 million, lower in Q1,024.8 million than the one of the previous year. Said variation was due to a reduction in the deposits of the Central



Government in the *Banco de Guatemala* of Q1,083.8 million and an increase in the deposits of the rest of the public sector of Q59.0 million.

The referred reduction in the deposits of the Central Government in the *Banco de Guatemala* was associated, according to the *Ministerio de Finanzas Públicas*<sup>25</sup>, with the higher expense for an amount of Q978.3 million to partially finance the Rehabilitation and Reconstruction Program originated from the tropical storm Stan. In effect, during December 2005 the funds provisions were carried out to finance said program through the establishment of a trust in the banking system of Q550.0 million, the remaining Q428.3 million were used to assist the emergency derived from said climatic phenomenon, between October and December 2005.

Regarding the credit to the financial institutions, though article 48 of the Organic Law of the *Banco de Guatemala* authorizes the same to grant credit to the system's banks according to the terms and conditions referred by said norm; it is important to mention that during 2005 the financial system did not require funding from the Central Bank.

Regarding the balance of the credit to the system's banks, by the end of the year, it was reduced in Q17.6 million, from Q2,077.3 million in 2004 to Q2,059.7 million in 2005; this amount corresponds to the funds received by the *Banco de Guatemala* as a result of the reduction in the portfolio of titles issued by banking institutions<sup>26</sup>. It is important to indicate that during 2005 the financial system did not carry out amortizations on the credits granted by the Central Bank.

#### **D. CREDIT OF THE BANKS AND FIANCIAL SOCIETIES TO THE PRIVATE SECTOR**

To December 31<sup>st</sup>, 2005, the total credit of the banks to the private sector was of Q48,277.3 million, higher by Q8,505.0 million than the observed to December of the previous year, which represents an inter-annual growth of 21.4%;

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<sup>25</sup> *Ministerio de Finanzas Públicas*, Aide-Memorie year 2005. February, 2006

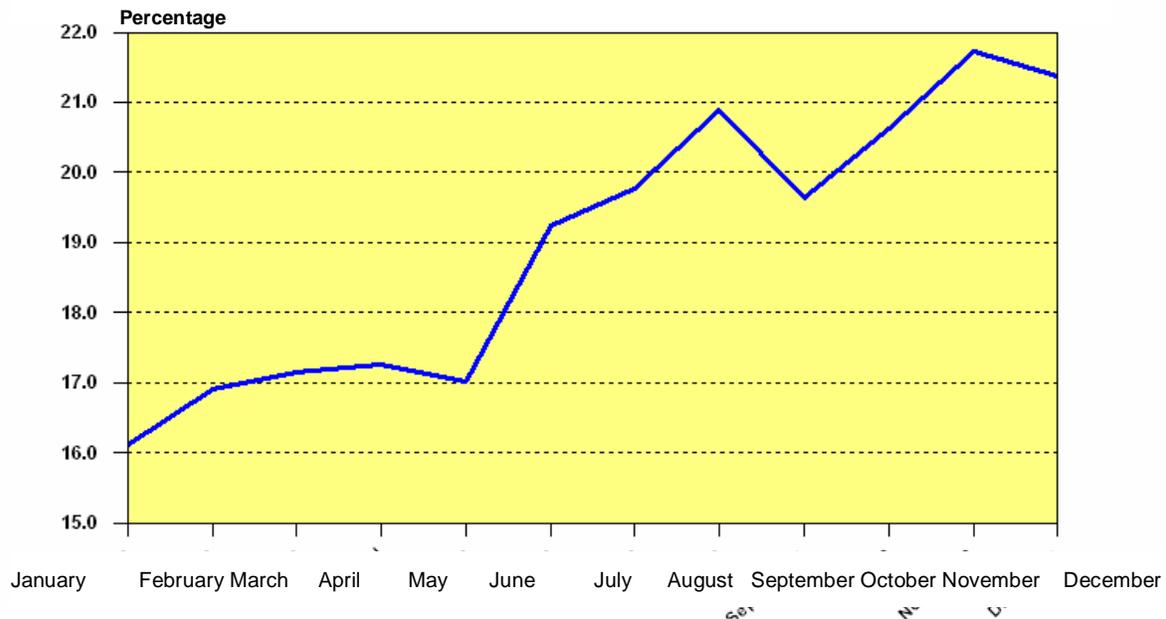
<sup>26</sup> This portfolio is integrated, entirely, by banking bonds acquired by the *Banco de Guatemala* before 1990. Said reduction is due to the amortization of capital that correspond to bonds with guarantee of mortgage booklets issued by the system's banks.



this percentage was above the range between 11.5% and 13.5% established in the monetary, exchange and credit policy.

Regarding the credit granted in national currency, it was of Q36,048.5 million, higher by Q6,623.5 million than the observed by the end of 2004, which represents an inter-annual growth of 22.5%. On the other hand, the credit granted in foreign currency by the end of the year was of about Q12,228.8 million, higher by Q1,881.6 million than the observed by the end of 2004, which represents an inter-annual growth of 18.2%.

**FIGURE 25**  
**BANKING SYSTEM <sup>1/</sup>**  
**CREDIT TO THE PRIVATE SECTOR**  
**INTER-ANNUAL RELATIVE VARIATION**  
**YEAR 2005**



<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included

On the other hand, the total credit of the financial societies to the private sector was of Q1,838.2 million by the end of December 2005, lower in Q195.4



million regarding the balance registered in December 2004, which represents a reduction in inter-annual terms of 9.6%.

**TABLE 16**

**SYSTEM'S BANKS AND FINANCIAL SOCIETIES  
CREDIT TO THE PRIVATE SECTOR  
TO DECEMBER 31st, 2004 AND 2005  
(million of quetzales)**

Concept	2004	2005	Variation	
			Absolute	Relative
<b>TOTAL</b>	<b>41,805.8</b>	<b>50,115.5</b>	<b>8,309.7</b>	<b>19.9</b>
<b>EN MONEDA NACIONAL</b>	<b>30,963.1</b>	<b>37,438.5</b>	<b>6,475.4</b>	<b>20.9</b>
System's banks	29,425.0	36,048.5	6,623.5	22.5
Financial Societies	1,538.1	1,390.0	-148.1	-9.6
<b>IN FOREIGN CURRENCY</b>	<b>10,842.7</b>	<b>12,677.0</b>	<b>1,834.3</b>	<b>16.9</b>
System's banks	10,347.2	12,228.8	1,881.6	18.2
Financial Societies	495.5	448.2	-47.3	-9.5

<sup>1/</sup> Does not include banks that have been requested to declare bankruptcy and two societies that are in the bankruptcy process.

Regarding the credit portfolio, per type of instrument, the structure observed in previous years prevailed, constituting the loans sector about 78.4% of the total granted, while the remaining 21.6% corresponds to the following sectors: investment in FHA mortgage booklets FHA, factoring, credit in accounts of monetary deposits, discounted documents, documents to be collected and other credits.

During 2005 the financial system granted new loans of Q31,054.8 million (includes extensions and renewals of Q23,039.8 million), higher by Q3,192.6 million than the granted the previous year. The branches of economic activities attended were: consumption<sup>27</sup>, Q10,819.4 million (34.8%); commerce, Q7,186.2 million (23.1%); services, Q3,720.5 million (12.0%); manufacturing industry, Q3,697.5 million (11.9%); construction, Q2,948.3 million (9.5%); agriculture,

<sup>27</sup> It is integrated by consumption, 57.5%; transfers, 35.8%; and , other destinations, 6.7%.



livestock, forestry, hunting and fishing, Q2,024.9 million (6.5%); and, other destinations<sup>28</sup> Q658.0 million (2.2%).

## **E. BANKING CASH**

The Monetary Board in resolution JM-177-2002 dated June 1<sup>st</sup>, 2002, issue the Regulation of the Banking Cash. Said regulation establishes that the percentage of banking cash, not only in national but also in foreign currency, will be of 14.6%<sup>29</sup> calculated on the total of banking deposits; being the computing period of the banking cash of one month. Regarding the banking cash in national currency, by the end of 2005, this was of Q8,626.4 million, while the banking cash in foreign currency was of US\$142.5 million (equivalent to Q1,083.0 million). On the other hand, the average position of the cash in national currency of the banking system was positive the entire year, showing the highest rates in December of Q233.0 million and in January of Q156.8 million.

## **F. INTEREST RATES**

### **1. In national currency**

During 2005 the asset and liability weighted average interest rates of the banking system continued showing a stable behavior. In effect, the asset weighted average interest rate, by the end of 2005, was of 12.7%, lower in 0.8 percentage points than the registered in the same date of the previous year. On the other hand, the liability weighted average interest rate was of 4.6%, higher by 0.1 percentage points than the observed by the end of 2004. Regarding the gap between both rates, this was of 8.1 percentage points, lower than the observed in December 2004 (9.0 percentage points).

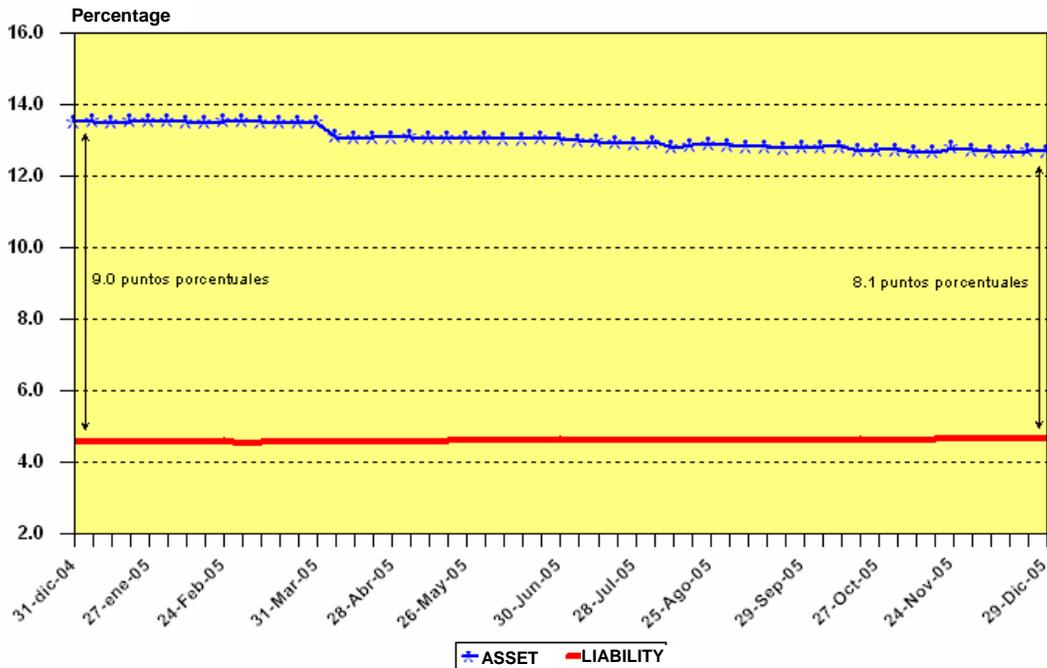
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<sup>28</sup> It is integrated by transport, 92.8% and mining, 7.2%.

<sup>29</sup> According to Resolution JM-160-2004 dated December 29th, 2004, the Monetary Board decided to maintain the banking cash rate of 14.6% for 2005.



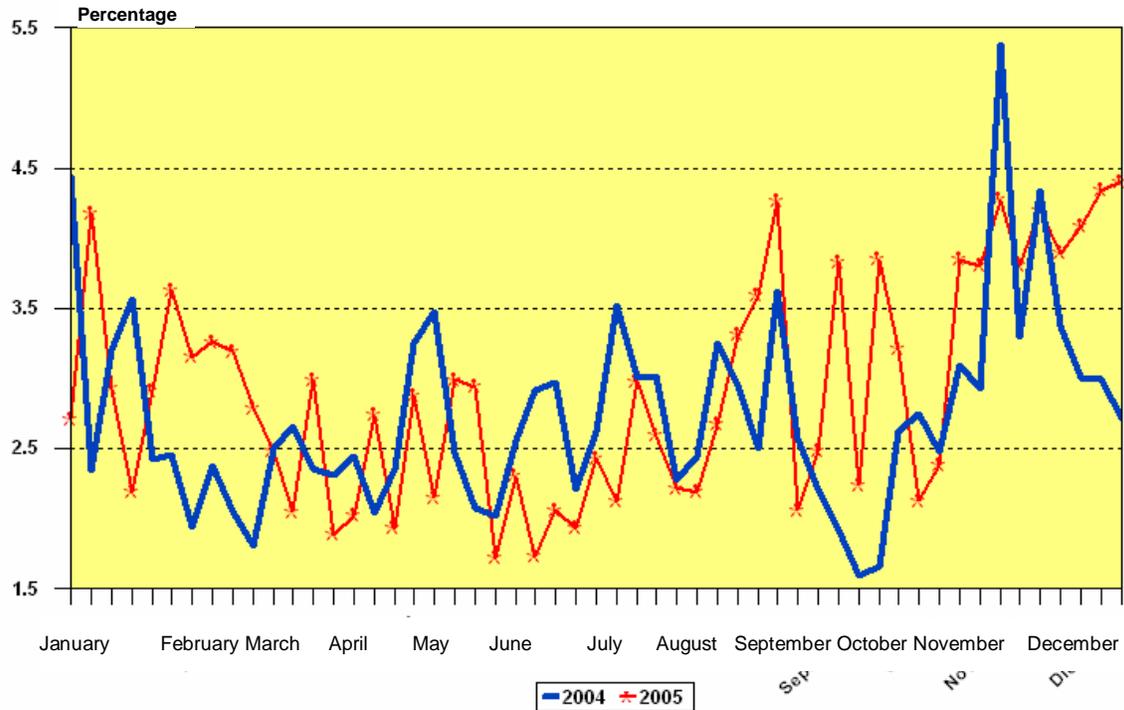
**FIGURE 26**  
**BANKING SYSTEM**  
**WEIGHTED AVERAGE INTEREST RATE IN N/C**  
**YEAR 2005**



Regarding the weighted average interest rate of the operations of repurchase agreement, were of 4.4% by the end of December 2005, percentage higher by 1.7 percentage points than the observed during the same date of the previous year (2.7%). It is important to mention that during most of the year, said rate remained around 3.0%, which is associated with the fact that the Central Bank, according to the lineaments of the Monetary, Exchange and Credit Policy determined by the Monetary Board for said year, oriented its efforts to maintain liquidity rates congruent with the stability in the general rate of prices.



**FIGURE 27**  
**REPURCHASE AGREEMENT OPERATIONS**  
**WEIGHTED AVERAGE INTEREST RATE**  
**YEARS 2004-2005**

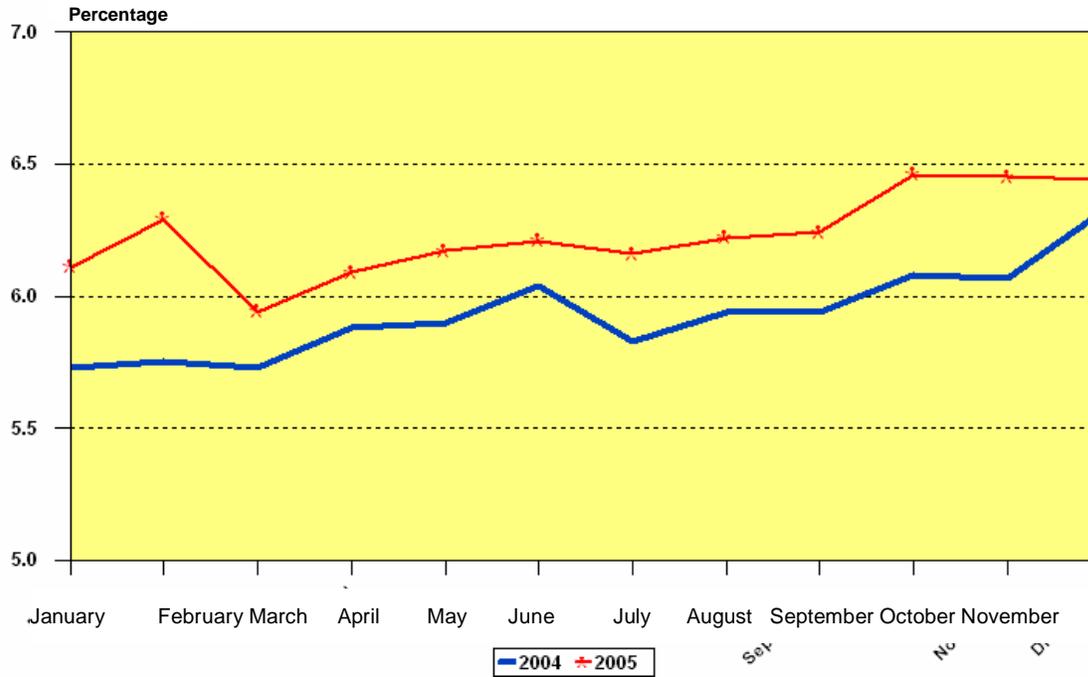


The weighted average interest rates of the balance of the Operations of Monetary Stabilization -OEMs- [Acronym in Spanish.], showed a stable behavior with a slight trend towards the rise, from 6.3% in December 2004 to 6.4% in December 2005, as a result, on one hand, of the increase in the leading interest rate of the monetary policy and, on the other hand, of the change in the structure of the balance of the OEMs, due that it was registered a transfer of the liquidity of terms shorter than 180 days to higher terms<sup>30</sup>.

<sup>30</sup>To December 31<sup>st</sup>, 2004, the operations of monetary stabilization to terms shorter than 180 days represented 31.7% of the total and to terms longer than 180 days represented 68.3% of the total; while, to December 31<sup>st</sup>, 2005, said operations represented 25.3% and 74.7%, respectively.



**FIGURE 28**  
**OPERATIONS OF MONETARY STABILIZATION**  
**WEIGHTED AVERAGE INTEREST RATE IN N/C**  
**YEARS 2004-2005**



Regarding the term deposits interest rate of the *Banco de Guatemala* expressed in dollars of the United States of America<sup>31</sup>, postures were adjudicated in the bids carried out during several months of the year and to the following average interest rates: in February, 2.85%; in March, 2.86%; in April and in May, 2.89%; in July, 3.40%; in August, 3.75%; and, in September, 3.89%.

Regarding the interest rates applied to the advances granted by the Central Bank before 2001, the same, while carrying out the periodical revisions that correspond to 2005, registered a minimum rate of 6.05% and a maximum of 7.62%. On the other hand, the interest rates applied to the contingent credit lines granted with domestic funds to the three banks administratively intervened in 2001,

<sup>31</sup> In resolution JM-99-2004 dated September 8th, 2004, the Monetary Board authorized the *Banco de Guatemala* the receipt of term deposits in dollars of the United States of America.

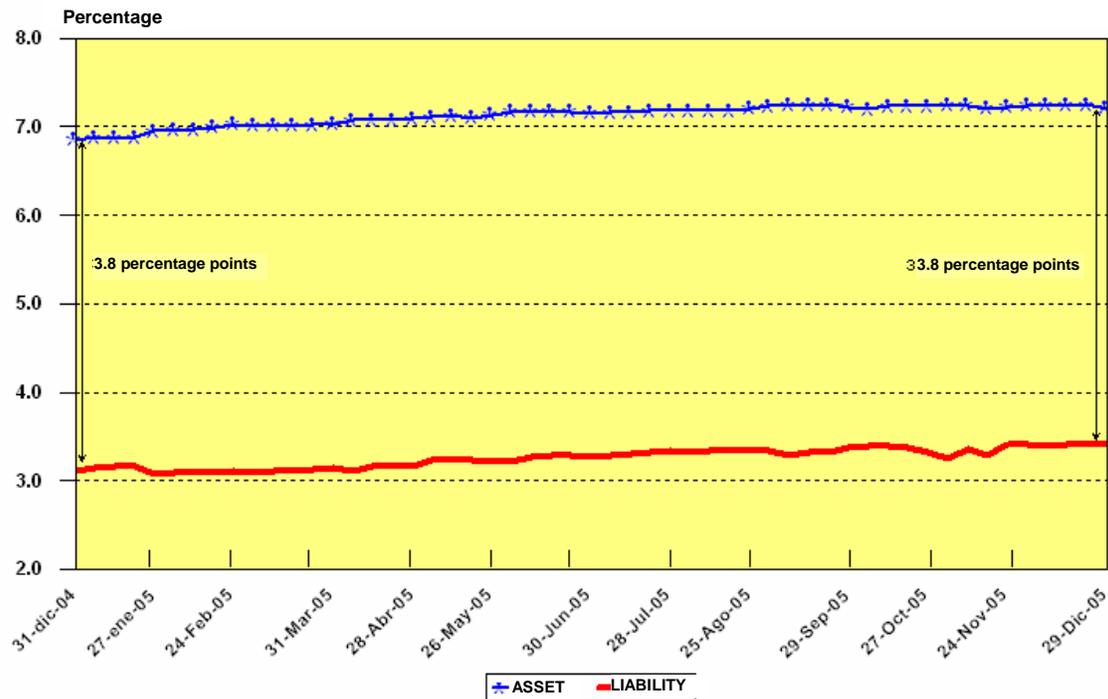


while carrying out the periodic revisions that correspond to 2005, registered a minimum percentage of 3.14% and a maximum of 4.65%.

## 2. In foreign currency

The asset weighted average interest rate of the banking system in foreign currency showed an increase, increasing from 6.9% in December 2004 to 7.2% in December 2005. On the other hand, the liability weighted average interest rate also showed an increase, being of 3.4% by the end of December 2005 (3.1% en 2004). Regarding the gap between both rates, this was of 3.8 percentage points, equal than the observed in December 2004.

**FIGURE 29**  
**BANKING SYSTEM**  
**WEIGHTED AVERAGE INTEREST RATE IN F/C**  
**YEAR 2005**





Regarding the average weighted interest rate of the repurchase agreement operations in said currency, it showed an increasing trend, from 3.5% in December 2004 to 4.5% by the end of 2005.

## **G. OPERATIONS OF MONETARY STABILIZATION**

In 2005 the OEMs, that constitute the main instrument of monetary regulation approved by the Monetary Board, were carried out taking into account the behavior of the monetizing and demonetizing factors foreseen in the monetary program, in order to make the offer of monetary issue compatible with its respective programmed demand.

### **1. In national currency**

Derived that since April 2005 the monetary issue registered rates above the ceiling of the programmed broker, the performance of operations of monetary stabilization was intensified, in order to pursue the gradual reduction of the referred deviation, so that the surplus of monetary issue will not generate inflationary pressures; therefore, the Execution Committee of the *Banco de Guatemala* increased the leading interest rate of the monetary policy<sup>32</sup> during seven occasions, from 2.55% in January to 4.25% in December.

Besides, said committee decided that since May 3<sup>rd</sup> it will be summoned to bids only to terms of 364 days and 728 days; strategy that remained during May and June, in order to adequate the liquidity fund-raising to the estimated monetization flow and, therefore, to gradually neutralize the liquidity in longer terms.

In the second trimester of 2005, the Execution Committee, taking into account the agreed in the Working Group of the *Banco de Guatemala - Ministerio de Finanzas Públicas*, regarding the coordination of the monetary and fiscal policy,

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<sup>32</sup> The Execution Committee of the *Banco de Guatemala*, in meeting dated January 21<sup>st</sup>, after knowing the result of the corresponding technical studies, established that since January 24<sup>th</sup>, the interest rate of the 7-day term would be the leading interest rate of the monetary policy, due that this was the one that has more influence on the inflation's behavior.



decided that, since July 4<sup>th</sup>, the *Banco de Guatemala* will summon to bids, on Monday to terms of 91 days and 364 days; Wednesday to terms of 182 days and 728 days (2 years), with a pre-announced quota for each of said terms, and, Fridays to terms of 1456 days (4 years), 2184 days (6 years) and 2912 days (8 years), with the difference that for these terms there was not a pre-established quota, in order to favor higher fund-raising to longer terms. Since September 26<sup>th</sup>, it was established that a pre-announced quota for the term of 2912 days (8 years), due that the Execution Committee considered that the competence observed in the postures to this term was very limited and that a restrictive fund-raising quota for said term would provide a higher competence among the participants and would limit the associated financial costs.

It is important to indicate that the highest performance of OEMs pursue to send a certain message from the Central Bank to the economic agents about the compromise of watching for the stability in the general rate of prices. In this context, the placements between April and December reached an amount of Q132.0 million, as a net result of the increase in the operations with the public sector of Q625.0 million and of the reduction of the operations with the private sector of Q493.0 million. The balance of the operations of monetary stabilization in national currency by the end of December 2005 was of Q16,977.4 million, higher by Q1,122.2 million regarding the balance registered in December 2004 (Q15,855.2 million).

Regarding the relative weight of the OEMs placement mechanisms, carried out through the bid mechanism with the private and banking sectors represented 51.8% of the total (Q8,787.2 million), the placement in window with the public and public entities represented 33.1% (Q5,629.2 million) and the placements carried out in the Electronic Banking Table of Money-MEBD- and in the stock exchange 15.1% (Q2,561.0 million).

The cost of the monetary policy derived from the liquidity neutralization through operations of monetary stabilization was of Q967.7 million (equivalent to 0.4% of the gross domestic product), lower than the registered in December 2004, which was of Q1,023.6 million (equivalent to 0.5% of the gross domestic product).



## 2. In foreign currency

During 2005 the *Banco de Guatemala* continued summoning to bids of term deposits expressed in dollars of the United States of America, in order to help reducing the volatility in the nominal exchange rate. The bids were carried out, since January 10<sup>th</sup>, every Tuesday and Thursday. Later, since September 12<sup>th</sup> bids were summoned only every Tuesday, taking into account that there was not a higher demand of the referred deposits in the market. In the above context, in 2005 the fund-raising total of this operations were of US\$30.9 million, placing US\$29.6 million to a term of 91 days with an average interest rate of 2.86% and US\$1.3 million to a term of 336 days with an average interest rate of 3.42%. The balance of the referred operations, to December 31<sup>st</sup>, 2005, was of US\$1.3 million.

## H. ACCOUNTS OF BALANCE OF THE SYSTEM'S BANKS

The consolidated balance of the system's banks, to December 31<sup>st</sup>, 2005, shows that the total assets were of Q88,679.0 million, higher by Q12,769.9 million than the one of the previous year, equivalent to an inter-annual growth of 16.8%. Said growth is explained, on one hand, by the increase of the credit portfolio sector, particularly, loans in national currency, which was expanded in Q5,475.6 million (23.8%) and, on the other hand, by the increase of the investment in securities, mainly in securities of the State of Q2,579.4 million (17.4%) and in foreign securities of Q1,278.8 million (42.5%).

Regarding the total liabilities, to December 31<sup>st</sup>, 2005, these were of Q81,251.6 million, higher by Q12,066.3 million regarding the observed by the end of December 2004, which represents an inter-annual growth of 17.4%. Said increase is explained by the increase in the sectors of obligations in the country, mainly of deposits of Q10,179.2 million (17.8%), loans abroad of Q1,422.5 million (22.1%) and bonds in circulation in national currency of Q206.6 million (8.2%). On the other hand, other creditor accounts showed a reduction of Q41.8 million (6.1%) regarding December 2004.



Regarding the accounting capital, to December 31<sup>st</sup>, 2005, it was of Q7,427.4 million, higher by Q703.7 million (10.5%) than the registered by the end of 2004; result mainly explained by the increase of primary capital, associated not only with the increase of paid capital of Q250.8 million (5.9%) but also with the increase of the capital reserve of Q106.1 million (19.5%).

## **I. LEGAL AND IMMEDIATE CREDIT EXPANSION CAPACITY OF THE SYSTEM'S BANKS**

Article 64 of the Law of Banks and Financial Groups established that the banks and financial societies should keep a permanent minimum wealth amount regarding their exposure to credit and market risks and other risks, according to the general regulations issued by the Monetary Board for said effect. Said norm foresees that the minimum wealth amount for the exposure to the mentioned risks and the corresponding weightings must be settled by the Monetary Board. With that regard, article 2 of the Regulation for the Determination of the Minimum Amount of Required Wealth for Risks Exposure, applicable for Banks and Financial Societies, approved in resolution JM-46-2004 dated May 12<sup>th</sup>, 2004, established that the referred wealth will be equivalent to the amount of: a) equivalent to ten percent (10%) of the assets and contingences weighted according to its risk category; and, b) one hundred percent (100%) of the amount of differed expenses to be amortized registered accountably since July 1<sup>st</sup>, 2004, date in which said regulation was enforced.

On the other hand, according to article 65 of said law, the computing wealth of the banking institutions is integrated by the primary capital plus the complementary capital, deducing from said amount the investments in assets of national and foreign banks, financial societies, insuring companies, bonded warehouses, specialized companies of financial services, as well as the capital assigned to branches abroad.

To December 31<sup>st</sup>, 2005<sup>33</sup>, the computing wealth of the banking system was

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<sup>33</sup> Does not include banks requested to declare bankruptcy.



of Q6,721.2 million, while the amount of the required wealth was of Q5,092.8 million; therefore, the wealth solidity position was positive by the end of the year in Q1,628.4 million; this amount, in case the banking system expands in assets with weighting of one hundred percent (100%) of ten percent (10%) of risk, would allow an increase in its asset operations and contingences up to Q16,284.0 million. It is important to mention that the credit expansion capacity of banks is associated with the funds that said institutions have available, stressing that to December 31<sup>st</sup>, 2005 they dispose of Q28.4 million of surplus liquidity to carry out new investments.

## **J. BANKING INSTITUTIONS**

By the end of 2005, 25 national banks<sup>34</sup> and a branch of a foreign bank were operating. Regarding the number of agencies and branches, during the same date, 1,367 were operating, from which 1,366 corresponded to agencies and one to a branch of a foreign bank. From the total of agencies, in the metropolitan region 48.0% (655) were operating, in the South West region 15.7% (215), in the North East 10.0% (136), in the Central region 8.4% (115), in the South East 6.1% (83), in the North West 5.5% (75), in the Northern region 4.2% (58) and in *Petén* 2.1% (29).

On the other hand, it is important to mention that in resolution JM-142-2004, dated November 17<sup>th</sup>, 2004, the Monetary Board authorized the *Financiera de Crédito, S.A.* to become a national private bank, under the name of "*Banco de Crédito, Sociedad Anónima*", which started operating on November 29<sup>th</sup>, 2005.

## **K. BALANCE ACCOUNTS OF THE FINANCIAL SOCIETIES**

To December 31<sup>st</sup>, 2005 there were 16 private financial societies and one governmental financial society. To the indicated date, the asset of the private financial societies was of Q3,944.7 million, lower in Q27.5 million than the

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<sup>34</sup> Does not include that banks request to declare bankruptcy.



registered in December of the previous year. Said reduction is mainly explained by the reduction of Q171.9 million in the availability assets sector and Q146.5 million in the net credit portfolio (mainly, loans in national currency of Q88.5 million) partially compensated by the increase of Q169.0 million in the investments in net securities sector of Q66.5 million in the fixed assets sector and of Q64.0 million in the other investments sector. The accounts with higher participation in the total asset were the net securities investment (48.3%) and the net credit portfolio (34.1%). Regarding the liability, to December 31<sup>st</sup>, 2005, it was of Q3,269.2 million, higher by Q54.7 million regarding the registered to December 31<sup>st</sup>, of the previous year. Said result is mainly due to the increase of the outstanding bonds in national currency sector of Q129.6 million and to the reduction of the credits abroad sector of Q77.5 million. The most significant sector, in relative terms, in the total liability was of the outstanding bonds in national currency with a participation of 96.8%. Regarding the accounting capital, it registered a reduction of Q81.9 million, from Q757.5 million in 2004 to Q675.6 million in 2005, as a result of the reduction of the primary capital of Q98.9 million, which was compensated by the increase of the complementary capital of Q17.0 million. Regarding the asset of the governmental financial society, *Corporación Financiera Nacional -CORFINA-*, to December 31<sup>st</sup>, 2005, it was of Q198.9 million, lower in Q124.3 million regarding the registered on December 31<sup>st</sup>, 2004. On the other hand, the liability was reduced in Q110.1 million, from Q4,488.3 million in 2004 to Q4,378.2 million in 2005 and the accounting capital was negative, being of Q4,179.2 million, lower in Q14.2 million than the observed the previous year. To December 31<sup>st</sup>, 2005, the liable amount plus the capital was reduced in Q124.3 million regarding the rate observed on December 31<sup>st</sup>, 2004.

## L. FINANCIAL GROUPS

Article 27 of Decree Number 19-2002 of the Congress of the Republic, Law of Banks and Financial Groups, defines as "Financial Group" the group of two or more legal persons that carry out financial activities, from which one should be a bank, with common control due to property, administration or use of corporative



image, or though without these relationships, according to agreement, decide the common control.

In that sense, based on article 116 of the Law of Banks and Financial Groups, to December 31<sup>st</sup>, 2005, the Monetary Board had authorized the formation of 15 financial groups, the administrative structure of which covers 76 entities that include 15 banks, 15 securities firms, 11 off shore entities, 9 financial societies, 9 companies that issue credit cards, 4 companies of financial and factoring leasing, 4 insuring companies, 4 bonded warehouses, 2 guarantee companies, 1 exchange agency, 1 company that operates family remittances and 1 company that supports consumption credits.

The following table shows the detail of the entities that integrated said financial groups:



# Study of the National Economy 20



**FINANCIAL GROUPS AUTHORIZED BY THE MONETARY BOARD  
To December 31<sup>st</sup>, 2005**

**TABLE 17**

No.	FINANCIAL GROUP	ENTITY OR COMPANY OF THE GROUP										
		Responsible Bank-Company	Offshore Entities	Financial Societies	Bonded Warehouses	Insuring Companies	Guarantee Companies	Exchange Agency	Credit Card Entities	Financial and factorial leasing	Securities firm	Other Financial Institutions
1	De Occidente JM-81-2003 dated 07/04/2003	Banco de Occidente S.A.	Occidente International Corporation	Financiera De Occidente S.A.		Aseguradora De Occidente S.A.	Afianzadora De Occidente S.A.		Tarjetas de Crédito De Occidente S.A.		Asesores Bursátiles de Occidente S.A.	Occidente Corporation USA (Operadora de remesas familiares)
2	Corporación B1 JM-82-2003 dated 07/04/2003	Banco Industrial S.A.	Westrust Bank International Limited	Financiera Industrial S.A.	Almacenes Generales S.A. Almacenedora Integrada S.A.	Seguros El Roble S.A.	Afinazadora El Roble S.A.	Mercado Cambiario S.A.	Contécnica S.A.	Servicios Múltiples de Inversión S.A.	Mercado de Transacciones S.A.	
3	SCI JM-83-2003 dated 07/04/2003	Banco SCT S.A.		Financiera De Capitales S.A.							Sociedad de Corretaje de Inversiones en Valores S.A.	
4	Banquetzal JM-91-2003 dated 07/16/2003	Banco Del Quetzal S.A.	Investment & Commerce Bank Limited						Singersa S.A.		Consersa, S.A.	
5	Agromercantil JM-95-2003 dated 07/23/2003	Banco Agromercantil de Guatemala S.A.	Mercom Bank Ltd.	Financiera Agromercantil S.A.					Agromercantil S.A.	Recursos Inmobiliarios y Servicios Diversos Especializados S.A.	Agrovalores S.A.	
6	Cuscatlán Guatemala JM-96-2003 del 23/07/2003	Banco Cuscatlán de Guatemala S.A.	Cuscatlan Bank & Trust Limited						Cuscatlán S.A.	Leasing Cuscatlán de Guatemala S.A.	Cuscatlán Valores S.A.	
7	BANEX-FIGSA JM-106-2003 dated 07/30/2003	Banco de Exportación S.A.	BANEX International Bank Corp.	Financiera Guatemalteca S.A.							BANEX Valores S.A.	
8	BAC-CREDOMATIC JM-108-2003 dated 08/13/2003	Banco de América Central S.A.	Bac Bank Inc.			Aseguradora Alianza S.A.			Credomatic de Guatemala S.A.	Negocios y Transacciones Institucionales S.A.	Bac Valores Guatemala S.A. Actividades Empresariales S.A.	
9	G&T Continental JM-140-2003 dated 10/22/2003	Banco G&T Continental S.A.	GTC Bank Inc.	Financiera G&T Continental S.A.					Guatemala S.A. G&T Conticredit S.A.		G&T Continental S.A. Asesoría en Valores S.A. Contivalores S.A.	
10	De la República JM-143-2003 dated 11/05/2003	Banco De la República S. A.	The Oxy Bank, Ltd.									
11	Reformador JM-151-2003 dated 11/19/2003	Banco Reformador S.A.	Transcom Bank (Barbados) Limited									
12	Bancafé Grupo Financiero del País JM-159-2003 dated 12/03/2003	Banco Del Café S.A.	Bancafe International Bank, Ltd.	Financiera Del País S. A.	Almacenedora Del País S. A.	Aseguradora Del País S. A.					Valores del País S. A.	
13	Banco Internacional JM-19-2004 dated 03/03/2004	Banco Internacional S.A.			Almacenedora Internacional S.A.						Internacional Casa de Bolsa S.A.	Interconsumo, S.A. (Apoyo al crédito para el consumo)
14	De Inversión JM-38-2004 dated 28/04/2004	Banco Americano S.A.		Financiera De Inversión S.A.								
15	Uno JM-175-2005 dated 14/12/05	Banco Uno S.A.		Financiera Uno S.A.					Centro Único de Crédito S.A.		Unibolsa S.A.	
<b>Total</b>		<b>15</b>	<b>11</b>	<b>9</b>	<b>4</b>	<b>4</b>	<b>2</b>	<b>1</b>	<b>9</b>	<b>4</b>	<b>15</b>	<b>2</b>

NOTE: Until December 31st, 2005 none of the financial groups have decided to be organized as a controller company.





## **M. OFF SHORE ENTITIES**

Article 112 of the Law of Banks and Financial Groups defines as off shore entities those dedicated, mainly, to the financial intermediation, constituted or registered under the laws of a foreign country, which usually carry out their activities outside of said country. According to the above, the Regulation for the Authorization of the Off Shore Entities Operation, approved by the Monetary Board in resolution JM-285-2002, dated November 15<sup>th</sup>, 2002, establishes in article 12 that the off shore entities can carry out in Guatemala, only in foreign currency, the operations established in the license issued by the country in which they are constituted and that are legally allowed in the country. Besides, it foresees that, the entire fund-raising operations (liable operations) should be constituted and maintained out of the Guatemalan territory and the off shore entities should inform the depositor or investor, by written in the corresponding contract, that the legal regimen that applies will be the one from the country that granted the authorization and, besides, that said deposits are not covered by the Fund for the Protection of Savings.

To December 31<sup>st</sup>, 2005, the Monetary Board had authorized the operation of 11 off shore entities, which are detailed in the following table:



TABLE 18

**OFF SHORE ENTITIES  
AUTHORIZED BY THE MONETARY BOARD  
To December 31<sup>st</sup>, 2005**

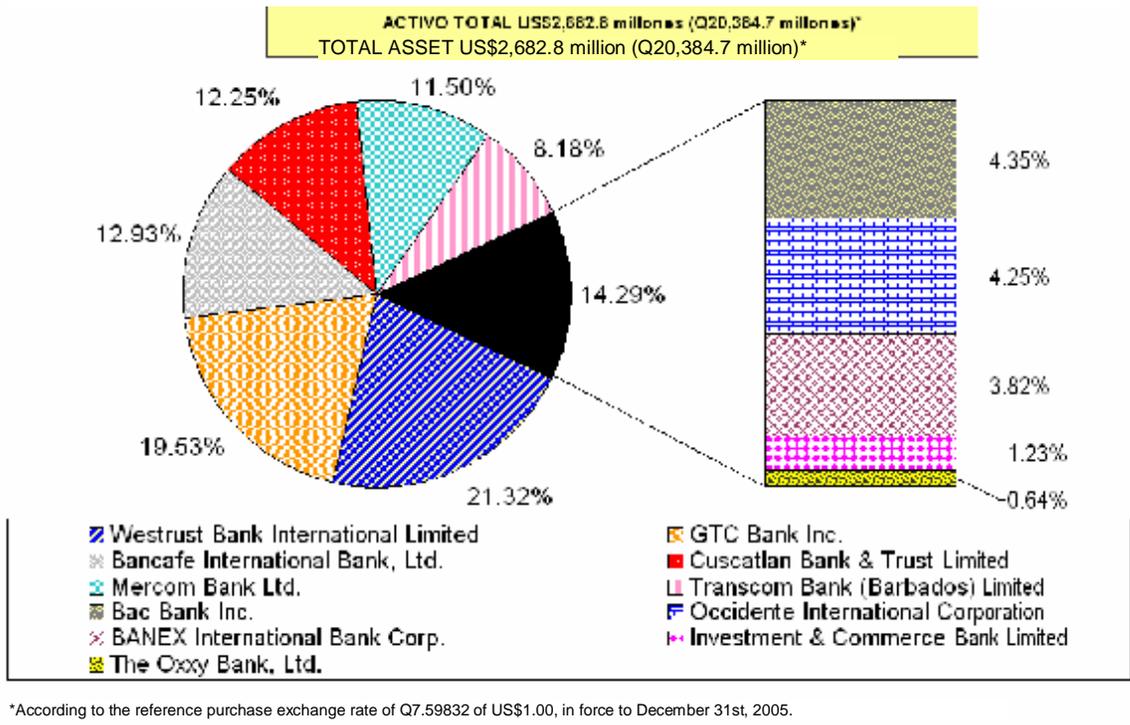
No.	DENOMINATION	RESOLUTION	FINANCIAL GROUP
1	Westrust Bank International Limited	JM-85-2003 dated 09-07-03	Corporación BI
2	Occidente International Corporation	JM-86-2003 dated 09-07-03	De Occidente
3	Investment & Commerce Bank Limited	JM-103-2003 dated 30-07-03	Banquetzal
4	Mercom Bank Ltd.	JM-104-2003 dated 30-07-03	Agromercantil
5	Cuscatlan Bank & Trust Limited	JM-116-2003 dated 03-09-03	Cuscatlán Guatemala
6	BANEX International Bank Corp.	JM-127-2003 dated 01-10-03	Banex-Figsa
7	Bac Bank Inc.	JM-128-2003 dated 01-10-03	Bac Credomatic
8	GTC Bank Inc.	JM-152-2003 dated 19-11-03	G&T Continental
9	Transcom Bank (Barbados) Limited	JM-154-2003 dated 26-11-03	Reformador
10	The Oxy Bank, Ltd.	JM-163-2003 dated 10-12-03	De la República
11	Bancafe International Bank, Ltd.	JM-164-2003 dated 17-12-03	Bancafé, Grupo Financiero del País

With illustrative purposes, regarding the participation of the off shore entities in the financial market, it was carried out a consolidation of the main sectors of the general balance that said entities reported to the *Superintendencia de Bancos* to December 31<sup>st</sup>, 2005. In that sense, it was established that the consolidated asset of the 11 entities was of US\$2.7 milliard, equivalent to Q20.4 milliard<sup>35</sup>. Said asset was distributed in the following way: Westrust Bank International Limited, 21.32%; GTC Bank Inc., 19.53%; Bancafe International Bank, Ltd., 12.93%; Cuscatlan Bank & Trust Limited, 12.25%; Mercom Bank Ltd., 11.5%; Transcom Bank (Barbados) Limited, 8.18%; Bac Bank Inc., 4.35%; Occidente International Corporation, 4.25%; Banex International Bank Corp., 3.82%; Investment & Commerce Bank Limited, 1.23%; and, The Oxy Bank, Ltd., 0.64%, as shown in the following figure.

<sup>35</sup> According to the reference purchase exchange rate of the *Banco de Guatemala* that corresponds to December 31<sup>st</sup>, 2005, of Q7.59832 per US\$1.00.



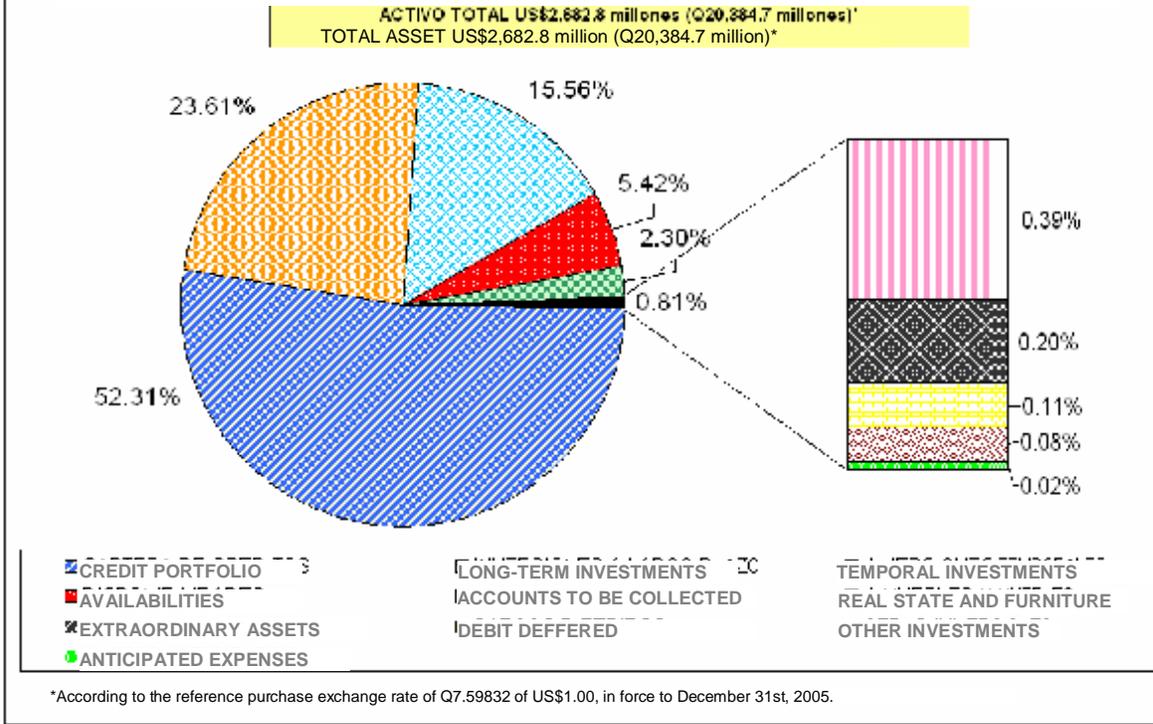
**FIGURE 30**  
**OFF-SHORE ENTITIES**  
**PARTICIPATION OF EACH ENTITY IN THE CONSOLIDATED ASSET**  
**TO DECEMBER 31st, 2005**



Regarding the structure of the main accounts that integrate the asset of the off shore entities, to December 31<sup>st</sup>, 2005, the credit portfolio represented 52.31%; the long-term investments 23.61%; the temporal investments 15.56%; the available assets 5.42%; the accounts to be collected 2.30%; and, other asset accounts 0.81%.



**FIGURE 31**  
**OFF-SHORE ENTITIES**  
 PARTICIPATION OF EACH SECTOR IN THE CONSOLIDATED ASSET  
 TO DECEMBER 31st, 2005

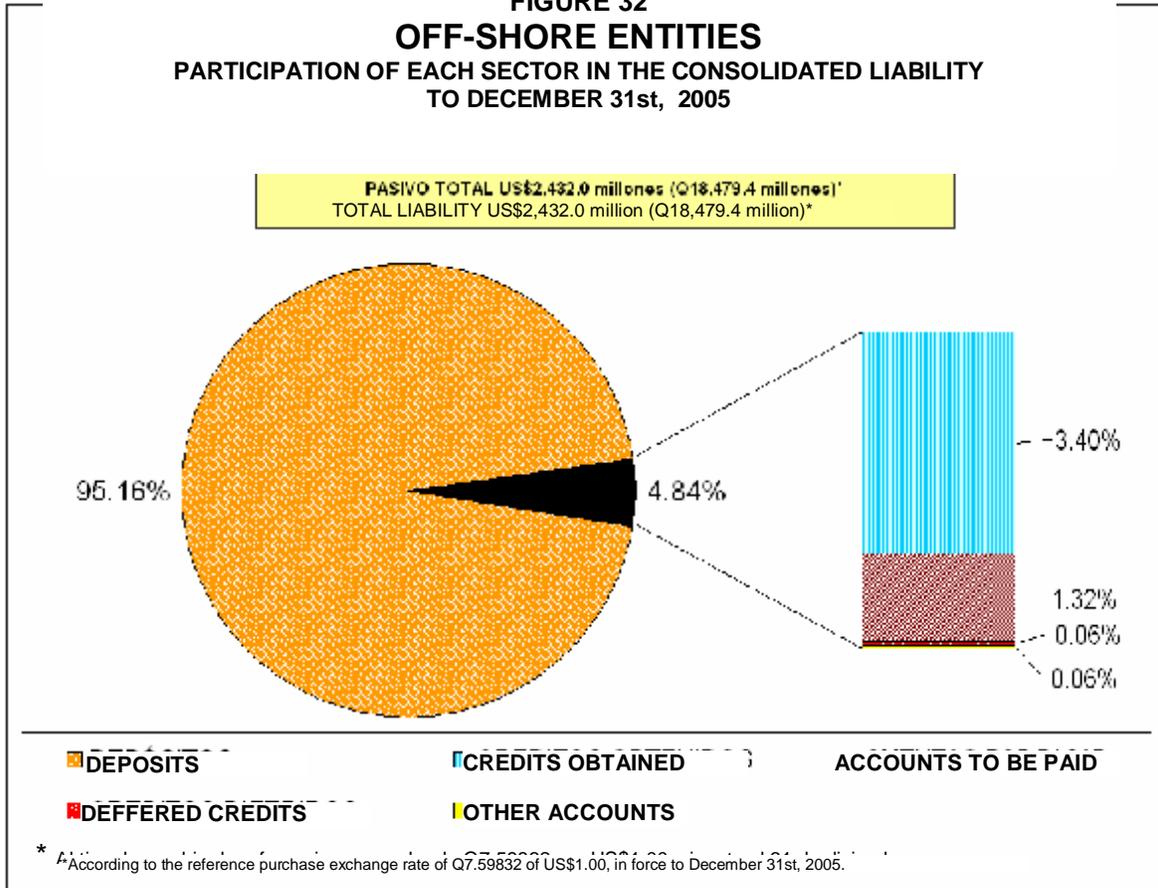


On the other hand, to December 31<sup>st</sup>, 2005, the consolidated liability was of US\$2.4 milliard, equivalent to Q18.5 milliard<sup>36</sup>; from which 95.16% corresponded to deposits; and, 4.84% to other liabilities, as shown in the following figure.

<sup>36</sup> To the reference purchase exchange rate of the *Banco de Guatemala* that corresponds to December 31<sup>st</sup>, 2005, Q7.59832 of US\$1.00.



**FIGURE 32**  
**OFF-SHORE ENTITIES**  
PARTICIPATION OF EACH SECTOR IN THE CONSOLIDATED LIABILITY  
TO DECEMBER 31st, 2005



## N. ADVANCES IN THE STRENGTHENING PROCESS OF THE NATIONAL FINANCIAL SYSTEM

### 1. Financial groups

During 2005, the Monetary Board in resolution JM-175-2005, dated December 14<sup>th</sup>, 2005, authorized the formation of “*Grupo Financiero Uno*” and its organizational structure. This group is integrated by *Banco Uno*, S. A., which is the responsible entity of the group and has the main control of the same, *Financiera Uno*, S. A., *Unibolsa*, S. A. and *Centro Único de Crédito*, S. A.

### 2. Banking System

In resolution JM-93-2005, dated May 18<sup>th</sup>, 2005, the Monetary Board issued the Regulation for the Administration of Credit Risk that has as its objective to



establish aspects related to the credit process, minimum information of the funding applicants and debtors and with the valuation of credit assets, which should be observed by banks, off shore entities and companies of a financial group that grant funding.

In resolution JM-92-2005, dated May 18<sup>th</sup>, 2005, the Monetary Board issued the Regulation for the Banking System's Investment in Security Titles issued by Private Entities. Said decision established the requirements that should be observed by the system's banks, before investing in this kind of titles which, according to the Law of Securities and Merchandise Market, Decree Number 34-96 of the Congress of the Republic, should be offered in public tender in the exchange and extra-exchange market; that the referred security titles negotiated in the international markets should have the rating granted by Standard & Poor's or equivalent rating granted by a well-known, international risk rater; and, that the issues negotiated in the national market should has a local risk rating, granted by a risk rating company registered in the Registry of the Securities and Merchandise Market.

On the other hand, the Congress of the Republic, in Decree Number 58-2005, approved the "Law to Prevent and Reprimand the Terrorism Funding", which has as objective to adopt measures for the prevention and repression of the terrorism funding, complementary of the normative against the money market and other assets. This law protects the welfare and security of the Republic's population and their goods, fulfills the compromises assumed by Guatemala in the International Agreement for the Repression of the Terrorism Funding and attends the requirements and standards issued by international organizations specialized in said matter. Besides, in Decree Number 72-2005, the "Reform to Decree number 2-70 of the Congress of the Republic, Trade of Commerce of Guatemala," was approved, adding an article in which recognizes the validity of the copies of the original issued checks, to be collected in banks abroad, and that, in case they are not paid, the originals have to be returned to the Guatemalan banks for delivery to the beneficiaries. The objective of this reform is to help the interested party to make the corresponding legal actions, using the copies of the original checks.



### **3. Strengthening of the banking security network**

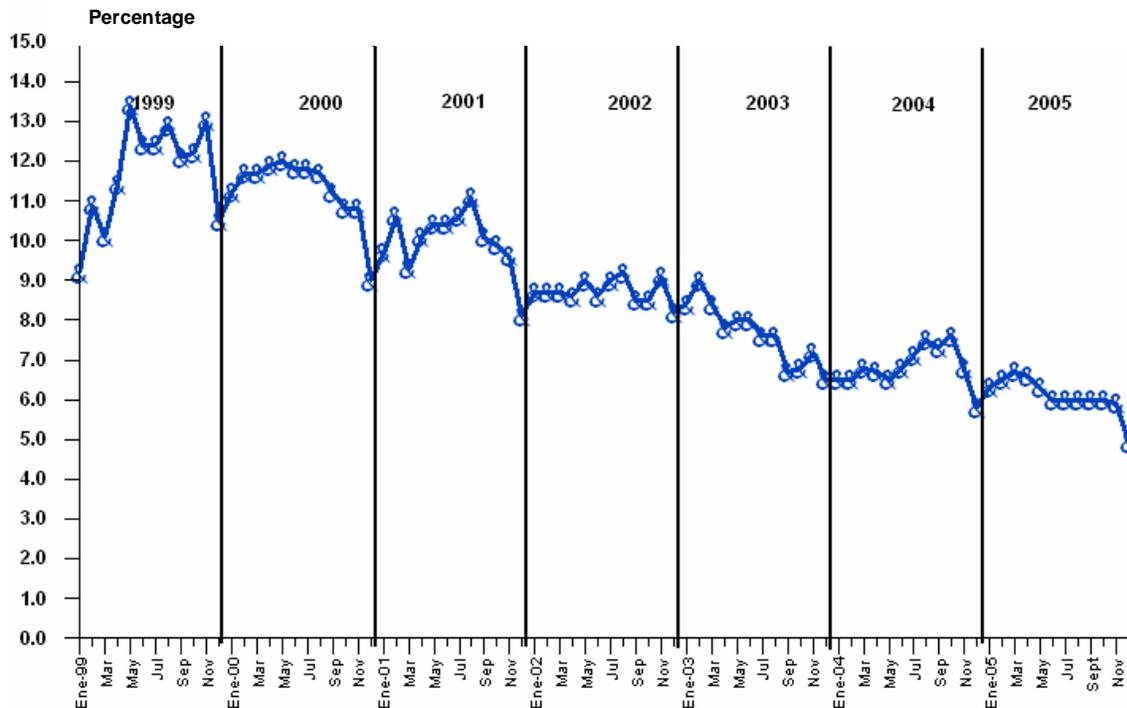
The Monetary Board in resolution JM-50-2005, dated March 2<sup>nd</sup>, 2005, decided to authorize, in order to fulfill the established in the first paragraph of article 48 of the Organic Law of the *Banco de Guatemala*, case by case, the requests of last instance credits formulated by the national private banks to solvent the temporal liquidity deficiencies. Besides, it approved the procedure that should be observed in a general and uniform way for the granting of last-instance credits in order to, on one hand, attend the requests filed according to the necessary celerity and, on the other hand, that the banking institutions know the requisites that should be fulfilled to obtain said funding.

### **O. DUE AND DEFAULT PORTFOLIO**

The due portfolio plus the default portfolio in the banking system (contaminated portfolio) showed a slight reduction. In effect, to December 31<sup>st</sup>, 2005 said portfolio was of Q2,202.5 million, which represented 4.9% of the total of the banking system portfolio, lower in 0.8 percentage points than the observed during the same date of the previous year (5.7%). The due portfolio represented 2.4% (3.2% to December 2004), while the default portfolio represented 2.5% in both years.



**FIGURE 33**  
**BANKING SYSTEM <sup>1/</sup>**  
**DUE AND DEFAULT PORTFOLIO**  
**January 1999 - December 2005**

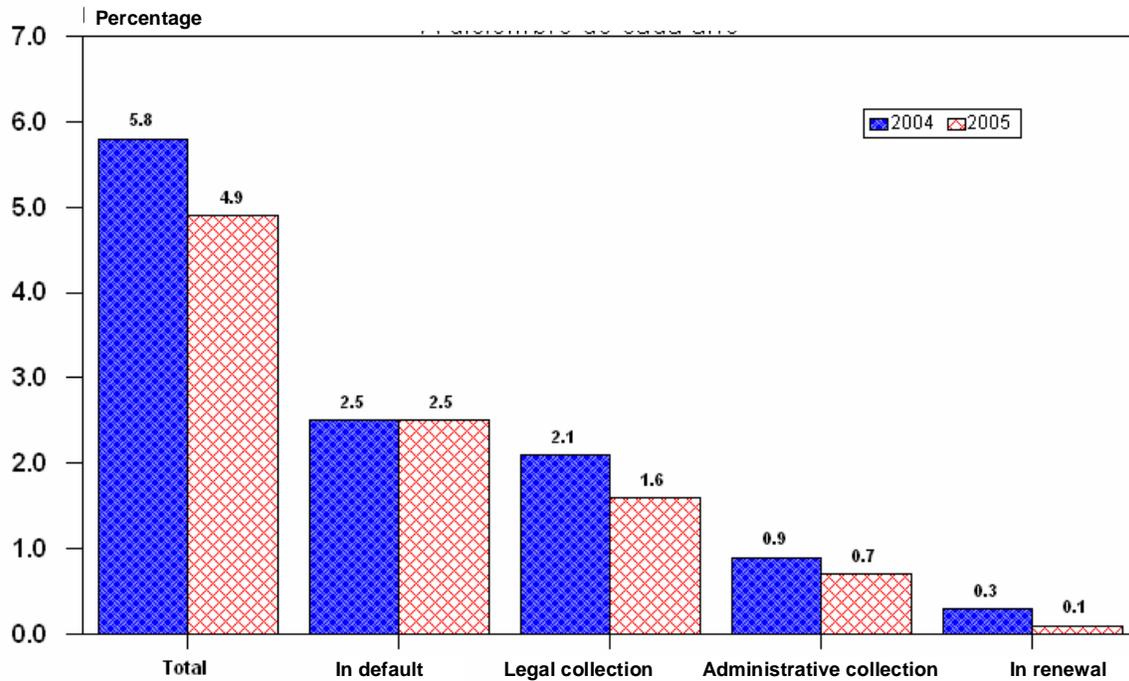


<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included

While examining the proportion that each of the sectors that integrated the portfolio in the recovery process represent in the total portfolio, it is observed that from December 2004 to December 2005, the portfolio to be collected by judicial means showed a slight reduction from 2.1% to 1.6%; the portfolio in administrative collection was reduced from 0.9% to 0.7%; and, the portfolio in the renewal process was reduced from 0.3% to 0.1%; while the default portfolio remained in 2.5%.



**FIGURE 34**  
**BANKING SYSTEM <sup>1/</sup>**  
**PROPORTION OF THE PORTFOLIO IN THE RECOVERY PROCESS**  
**To December of every year**



<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included

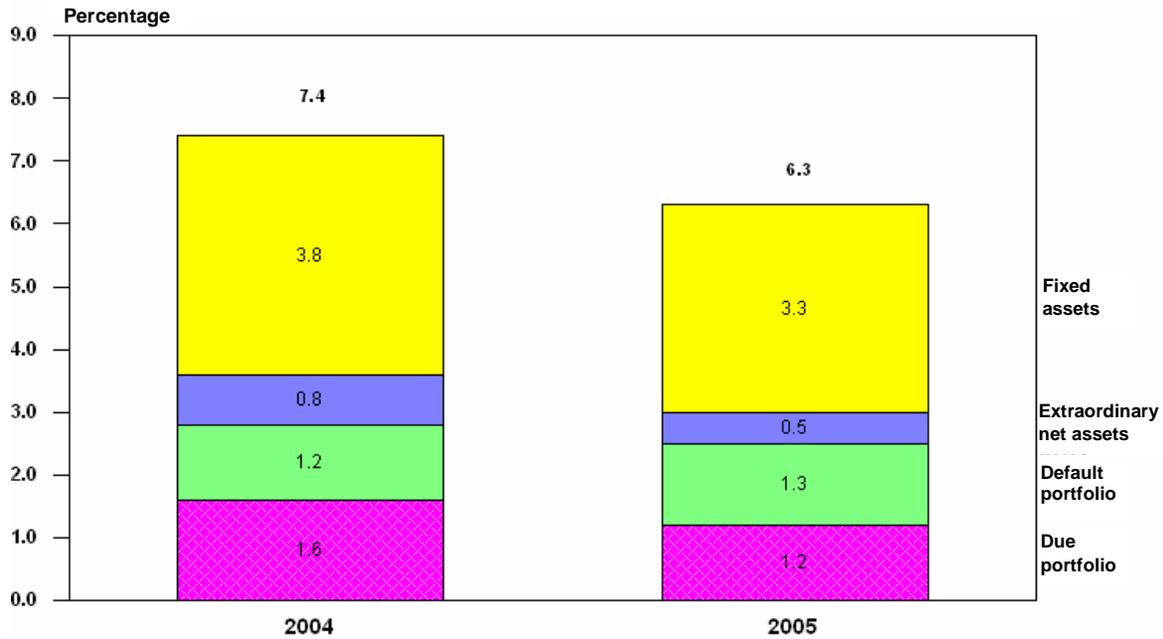
## P. IMPRODUCTIVE ASSETS

The unproductive assets<sup>37</sup> of the banking system, as a proportion of the total assets, continued with a trend towards the fall, being of 6.3% in December 2005 (7.4% in December 2004).

<sup>37</sup> It is integrated by the contaminated portfolio, extraordinary net assets and fixed assets.



**FIGURE 35**  
**BANKING SYSTEM <sup>1/</sup>**  
**PROPORTION OF THE UNPRODUCTIVE ASSETS REGARDING THE SYSTEM'S**  
**TOTAL ASSETS**  
To December of every year

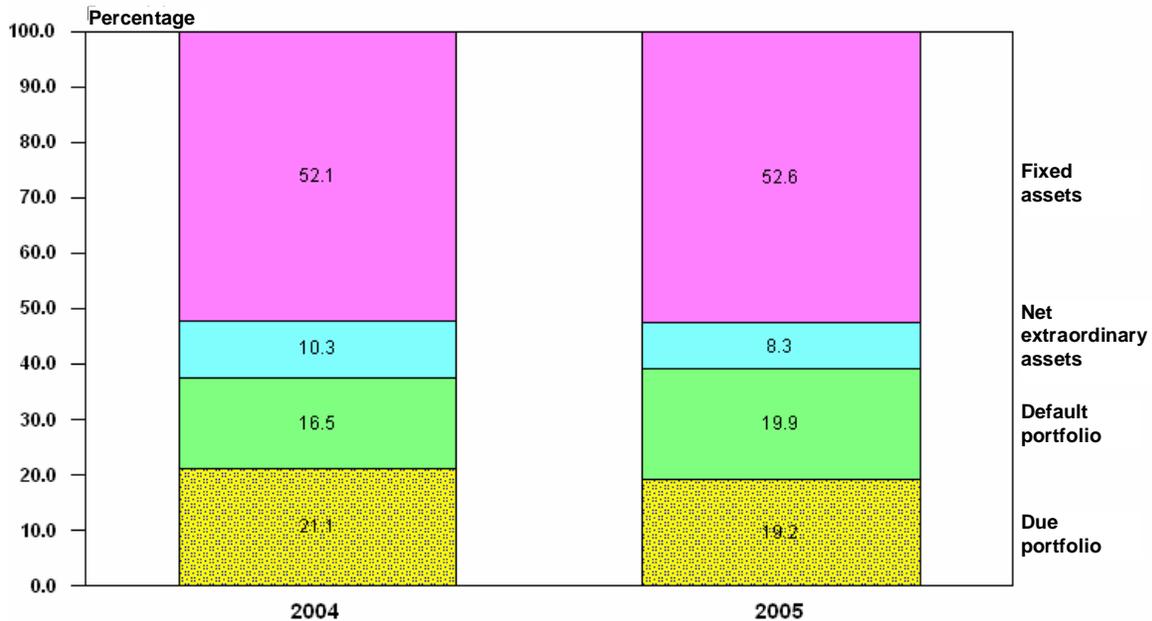


<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included

Regarding the structure of the unproductive assets, it is important to indicate that from December 2004 to December 2005 the net extraordinary assets and the due portfolio reduced their participation regarding the total of unproductive assets, from 10.3% to 8.3% and from 21.1% to 19.2%, respectively. In contrast, the fixed assets and the default portfolio increased their participation, from 52.1% to 52.6% and, from 16.5% to 19.9%, respectively.



**FIGURE 36**  
**BANKING SYSTEM <sup>1/</sup>**  
**STRUCTURE OF THE UNPRODUCTIVE ASSETS**  
**To December of every year**

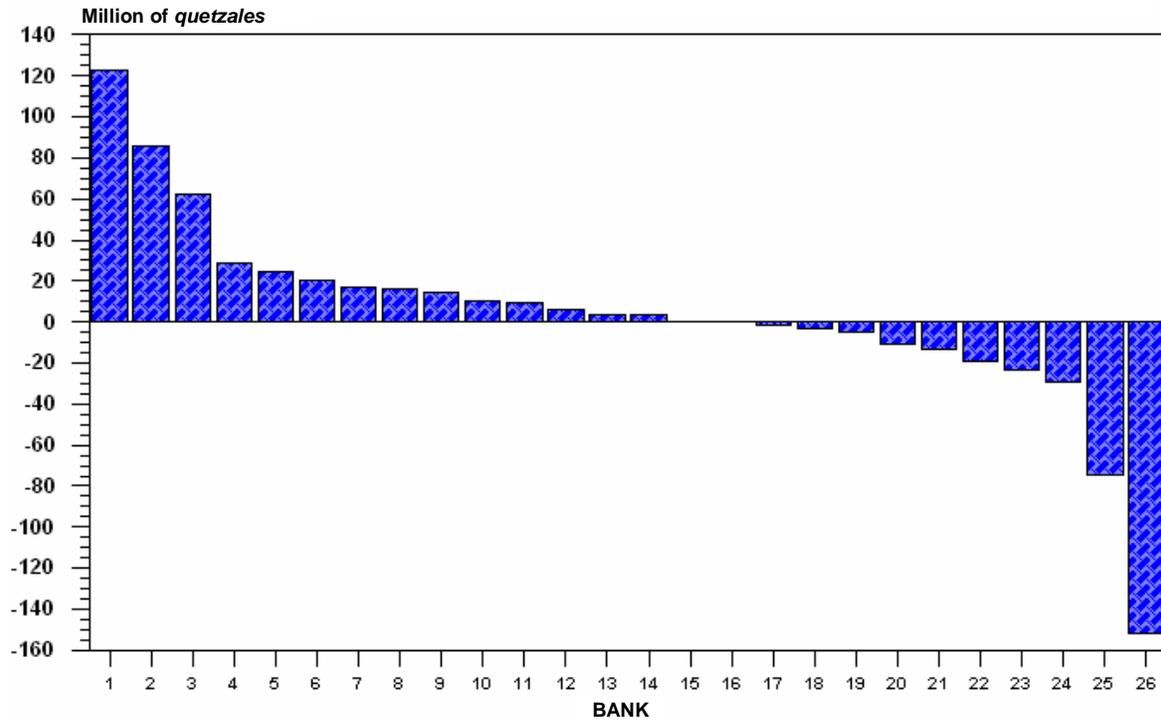


<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included

The increase of fixed assets is associated, in part, with the increase of assets derived from the operation of a larger number of banking agencies in the country, due that from 1,343 that operated in December 2004 it increased to 1,367 in December 2005. The reduction of the net extraordinary assets is the result of the increase of the estimations due to the valuation of the same and of the sale of some of those assets; while the reduction of the due portfolio is explained by the amortization of credits from the private sector. It is important to mention that though the contaminated portfolio (due portfolio plus default portfolio) as a proportion of the total portfolio showed a reduction, the rate of the same, from December 2004 to December 2005, registered an increase of Q90.9 million. In effect, 16 banks increased their contaminated portfolio in Q423.1 million, while 10 banks reduced it in Q332.2 million.



**FIGURE 37**  
**BANKING SYSTEM <sup>1/</sup>**  
**INTER-ANNUAL VARIATION OF THE CONTAMINATED PORTFOLIO**  
**December 2004-2005**



<sup>1/</sup>Banks that have been requested to declare bankruptcy are not included



## **VI. PUBLIC FINANCES**

### **A. GENERAL STATEMENTS OF THE BUDGET**

The General Income and Expense Budget of the State for the fiscal year 2005 was approved by the Congress of the Republic through Decree number 35-04 for an amount of Q32,385.2 million, while its analytical distribution was approved through Governmental Agreement number 422-2004. According to the considerations of the referred decree, the approved budget was prepared in order to promote the social and productive investment that reactivates the country's economy within the Framework of the Governmental Program, if it fulfills the goals established in the Peace Agreements and if it advances in the compromises acquired in the Fiscal Pact.

During 2005, said budget was enlarged on one occasion through Decree number 17-05 of the Congress of the Republic for an amount of Q35.0 million; as a result, the same reached an amount of Q32,420.2 million, higher by 5.2% than the enlarged budget of 2004. It is important to mention that the total budget for 2005 represented 13.4 % of the GDP (14.2% in 2004).

In the income budget, including the increase, Q24,452.5 million of current incomes were estimated; Q561.3 million of foreign donations; Q3,585.0 million of domestic public indebteding through the placement of bonds; Q1,999.7 million of foreign indebteding; and, Q1,821.7 million of use of cash funds.

On the other hand, in the expense budget, including the increase, Q19,812.1 million were assigned for operational expenses, including Q3,062.4 million to pay interests and commissions of the domestic and foreign public debt; Q10,080.9 million for investment expenses; and, Q2,527.2 million for the payment of the public debt.

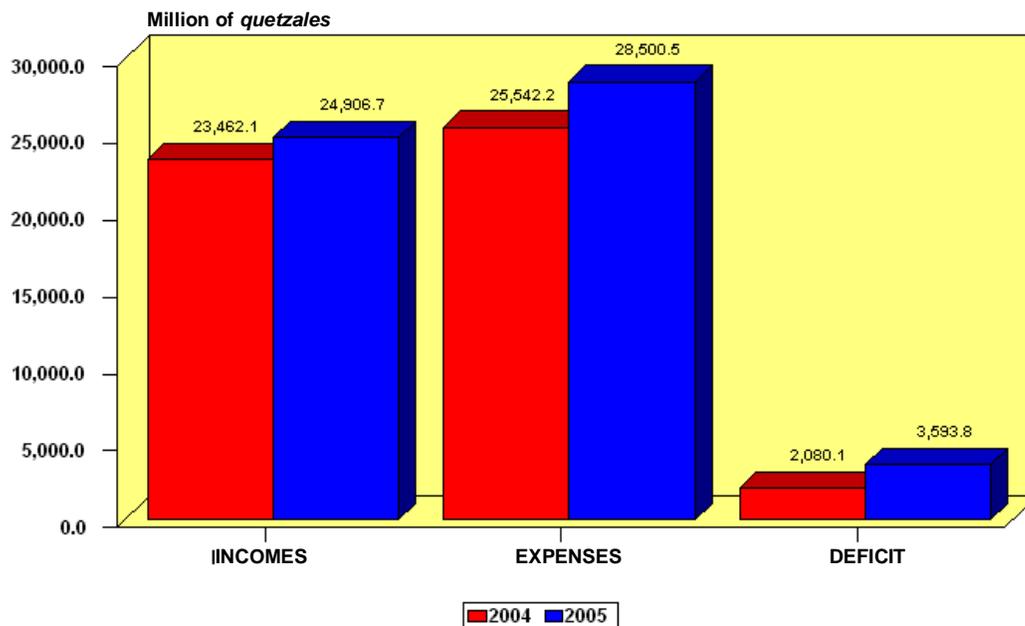
### **B. BUDGETARY EXECUTION**

According to the Settlement of the Income and Expense Budget of the State for the Fiscal Year 2005, the fiscal incomes reached Q24,906.7 million (higher by 6.2% than the one of 2004), while the total expenses reached Q28,500.5 million



(higher by 11.6% than the registered in 2004). The highest dynamism shown in the growth of the governmental expenses regarding the increase of the fiscal incomes caused the public finances by the end of 2005 to register a fiscal deficit of Q3,593.8 million, higher by Q1,513.7 million (72.8%) than the registered in 2004. Due to the above, the fiscal deficit relation on the GDP increased from 1.0% in 2004 to 1.5% in 2005.

**FIGURE 38**  
**CENTRAL GOVERNMENT**  
**BUDGETARY EXECUTION**  
**YEARS 2004-2005**



The tax income rate during 2005 allowed the tax burden to be of 9.6%, lower in 0.5 percentage points than the registered in 2004. This lower coefficient is mainly explained by the higher increase registered by the GDP regarding the increased observed by the tax income.

The tax burden in 2005 was derived from the indirect tax fund-raising of 74.0% (75.5% in 2004) and from direct taxes of 26.0% (24.5% in 2004).



On the other hand, the tax elasticity in 2005 was of 0.5, lower than the registered in 2004 (0.9), which indicates a lower dynamism of the tax incomes regarding the growth shown by the economic activity. It is important to indicate that said elasticity is the lowest during the last ten years.

CENTRAL GOVERNMENT FISCAL INDICATORS YEARS 1996 - 2005						
YEARS	Tax Incomes	Fiscal deficit	Nominal GDP	Tax elasticity <sup>1/</sup>	Tax burden <sup>2/</sup> (%)	Fiscal deficit / PIB (%)
-Million of <i>quetzales</i> -						
1996	7,952.2	71.1	95,478.6	1.9	8.3	0.1
1997	9,440.0	835.4	107,873.4	1.4	8.8	0.8
1998	10,753.1	2,692.7	124,022.5	0.9	8.7	2.2
1999	12,612.1	3,803.9	135,287.0	1.9	9.3	2.8
2000	14,113.8	2,697.3	149,743.1	1.1	9.4	1.8
2001	15,927.8	3,090.2	164,870.1	1.3	9.7	1.9
2002	19,294.7	1,769.6	182,274.7	2.0	10.6	1.0
2003	20,280.7	4,565.9	197,598.7	0.6	10.3	2.3
2004	21,974.0	2,080.1	216,749.4	0.9	10.1	1.0
2005	23,310.1	3,593.8	241,596.0	0.5	9.6	1.5

<sup>1/</sup> Relation that measures in a proportional way the relative variation of the tax incomes regarding the relative increase of the gross domestic product.

<sup>2/</sup> Relation between tax incomes and gross domestic product.

SOURCE: *Ministerio de Finanzas Públicas AND Banco de Guatemala.*

Regarding the budgetary execution indexes, the total incomes received represent 99.6% of the total budget while the total expenses were executed in 95.3% due that the operation and capital expenses were executed in 95.5% and 95.0%, respectively, as shown in the following table.



**CENTRAL GOVERNMENT**  
**INDEX OF COLLECTION OF INCOMES AND EXECUTION OF**  
**EXPENSES REGARDING THE BUDGET**  
**YEARS 1996 - 2005**

TABLE 20

Years	Total Incomes			Operation Expenses								
	Budgeted Million of quetzales	Executed Million of quetzales	Index %	Total			Current			Capital		
				Budgeted Million of quetzales	Executed Million of quetzales	Index %	Budgeted Million of quetzales	Executed Million of quetzales	Index %	Budgeted Million of quetzales	Executed Million of quetzales	Index %
1996	9,774.2	8,577.5	87.8	10,949.7	8,648.6	79.0	6,854.3	6,169.0	90.0	4,095.4	2,479.6	60.5
1997	11,617.4	10,179.4	87.6	13,161.0	11,014.8	83.7	6,922.4	6,758.6	97.6	6,238.6	4,256.2	68.2
1998	12,426.0	12,000.3	96.6	15,915.7	14,693.0	92.3	9,488.5	9,128.4	96.2	6,427.2	5,564.6	86.6
1999	15,064.8	14,164.5	94.0	19,840.5	17,968.4	90.6	11,907.3	11,051.6	92.8	7,933.2	6,916.8	87.2
2000	15,688.9	15,577.7	99.3	19,523.8	18,275.0	93.6	12,977.6	12,902.0	99.4	6,546.2	5,373.0	82.1
2001	19,206.6	18,219.8	94.9	24,031.3	21,310.0	88.7	15,746.0	15,387.9	97.7	8,285.3	5,922.1	71.5
2002	20,326.0	20,771.5	102.2	24,236.1	22,541.1	93.0	16,248.7	15,753.2	97.0	7,987.4	6,787.9	85.0
2003	22,295.7	21,767.5	97.6	29,363.6	26,333.4	89.7	18,701.1	17,609.5	94.2	10,662.5	8,723.9	81.8
2004 <sup>a/</sup>	22,295.7	23,462.1	105.2	27,249.8	25,542.2	93.7	18,556.5	17,498.7	94.3	8,693.3	8,043.5	92.5
2005	25,013.8	24,906.7	99.6	29,893.0	28,500.5	95.3	19,812.1	18,927.3	95.5	10,080.9	9,573.2	95.0

a/ The collection and execution indexes correspond to the adjusted budget.

SOURCE: *Ministerio de Finanzas Públicas*.

In 2005 the current incomes were higher than the current expenses, which generated a saving in current account of Q5,596.9 million, lower in Q53.8 million reached in 2004. In terms of the GDP, this variable represented 2.3%; lower than the one of the previous year (2.6%). The saving in current account allowed financing 58.5% of the investment expenditure (70.3% in 2004).

By the end of the fiscal year 2005, the net funding of the government was of Q3,593.8 million, higher by Q1,513.7 million than 2004.

The net domestic funding was positive in Q2,621.3 million, as a result of net negotiations of Q3,585.0 (gross negotiations of Q5,279.7 million and repurchase of Q1,694.7 million). It is important to mention that in order to fulfill the established in clause b) of article 9 of the Organic Law of the *Banco de Guatemala*, the State, through the *Ministerio de Finanzas Públicas*, dated August 29<sup>th</sup>, 2005 issued in favor of the *Banco de Guatemala* Representative Certificates of Treasury Bonds of the Republic of Guatemala of Q963.7 million to cover the Central Bank's net deficiency of the fiscal year 2003; amount included in the referred domestic funding.

On the other hand, the net foreign funding was negative in Q336.8 million, as a result of disbursements of Q1,087.2 million and amortizations of Q1,424.0 million. Within the disbursements received from the Central Government highlight the ones obtained from the *Banco Centroamericano de Integración Económica - BCIE-*, Inter-American Development Bank -IDB- and International Bank for



Reconstruction and Development -IBRD - which, jointly, were of Q931.1 million. Due that the funds derived from the domestic and foreign funding were not enough to cover the fiscal gap, a financial deficit of Q1,309.3 million was generated, which was covered by the reduction of the fiscal cash availability for the same amount.

### **C. INCOMES**

The total incomes, including donations, were of Q24,906.7 million, higher by 6.2% than the registered in 2004. Within this total, the tax incomes were of Q23,310.1 million, higher by Q1,336.1 million (6.1%) than the ones of the previous year, while the non-taxable incomes were of Q1,214.1 million, higher by Q38.7 million (3.3%) than the registered in en 2004.

The highest tax fund-raising is explained, in part, by the implementation of the Institutional Strategic Plan of the *Superintendencia de Administración Tributaria -SAT-*, which pursues to combat the corruption, to improve the service to the contributors, to strengthen the control of contributors and to impulse the development and use of computing applications; as well as by the legal reforms regarding taxation approved by the Congress of the Republic by the middle of 2004, which consisted in Reforms to the Law of Income Tax, the creation of the Law of Extraordinary and Temporal Tax to Support the Peace Agreements; and, the Law of Tax on the Distribution of Distilled Alcoholic Beverages, Beers and Other Fermented Beverages.

Regarding the fund-raising of direct taxes, this was of Q6,057.9 million, higher by Q681.3 million (12.7%) than the one of 2004. The higher fund-raising was determined by the Income Tax *-ISR-* [Acronym in Spanish.] which was of Q4,375.2 million, higher by Q1,088.5 million (33.1%) than the collected in 2004. Said growth was determined by the improvement of the effective tariff of the tax paid by companies, derived from the legal reforms of 2004. In effect, the ISR of the companies was higher by Q815.8 million (28.0%), while the ISR of individual people increased by Q272.7 million (73.2%) regarding the observed in 2004. Regarding the Extraordinary and Temporal Tax to support the Peace Agreements -



*IETAAP*- [Acronym in Spanish.], Q1,647.3 million were collected higher by Q421.3 million (34.4%) than the registered in 2004.

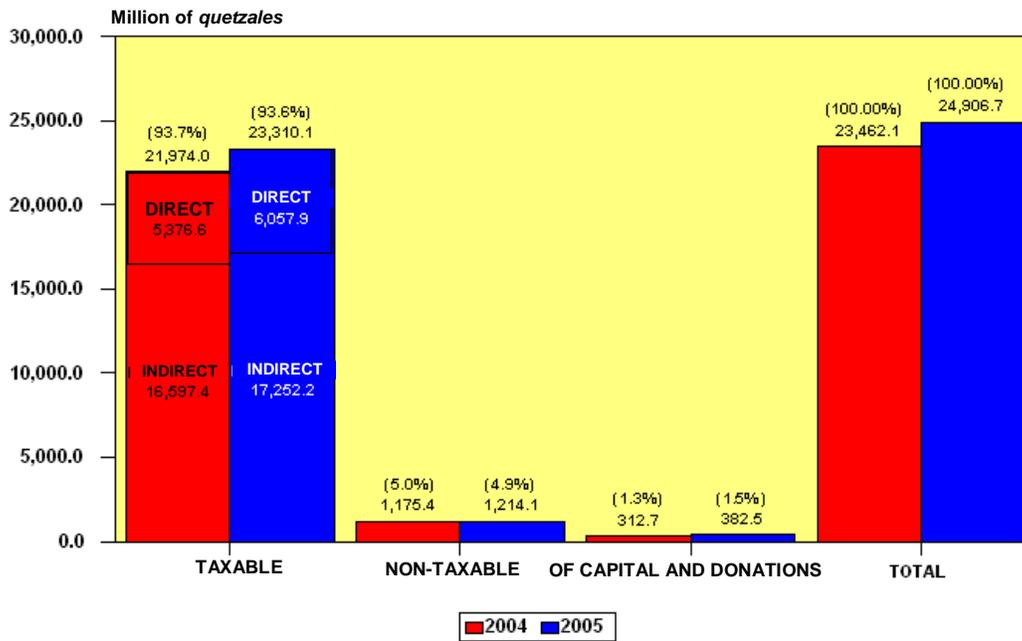
Regarding the indirect taxes, the amount collected was of Q17,252.2 million, higher by Q654.8 million (3.9%) than the collected in 2004. Said result was determined by the incomes derived from the Value Added Tax -VAT-, which were of Q10,752.7 million, higher by Q270.4 million (2.6%) than the registered in 2004. With that regard, it is important to indicate that the limited growth in the collection of this tax was due to the reduction of 7.4% in the collection of the domestic VAT, while the fund-raising of the imports VAT grew in 8.8% regarding 2004. On the other hand, the Tax for the Distribution of Crude Oil and Fuels derived from Petroleum reached an amount of Q485.3 million, lower in Q1,283.4 million (72.6%) than the previous year. Said reduction was because on December 16<sup>th</sup>, 2004 the *Corte de Constitucionalidad* decided to leave without effect the decree in which said tax was created. The fund-raising of the Import Tax was of Q3,714.5 million, higher by Q1,287.4 million (53.0%) than the collected in 2004, due that the Government of the Republic, in order to counteract the reduction of the tax incomes for the payment of Tax for the Distribution of Crude Oil and Fuels derived from oil, on December 17<sup>th</sup>, 2004, through Ministerial Agreement number 601-2004 agreed to establish a tariff for the import of crude oil and derivatives.

The non-taxable incomes were of Q1,214.1 million, higher by Q38.7 million (3.3%) than the obtained in 2004. Among the most significant non-taxable incomes are the incomes derived from the contributions to the security and social prevision of Q549.8 million and from the sale of goods and services of the public administration of Q182.9 million.

The capital incomes were of Q25.6 million, higher by Q25.0 million than the registered in 2004. The donations provided abroad were of Q356.9 million, higher by Q44.8 million (14.4%) than the received in 2004, from which Q347.2 million were provided by the government and Q9.7 million from organizations and international institutions.



**FIGURE 39**  
**CENTRAL GOVERNMENT**  
**STRUCTURE OF THE TOTAL INCOMES**  
**YEARS 2004-2005**

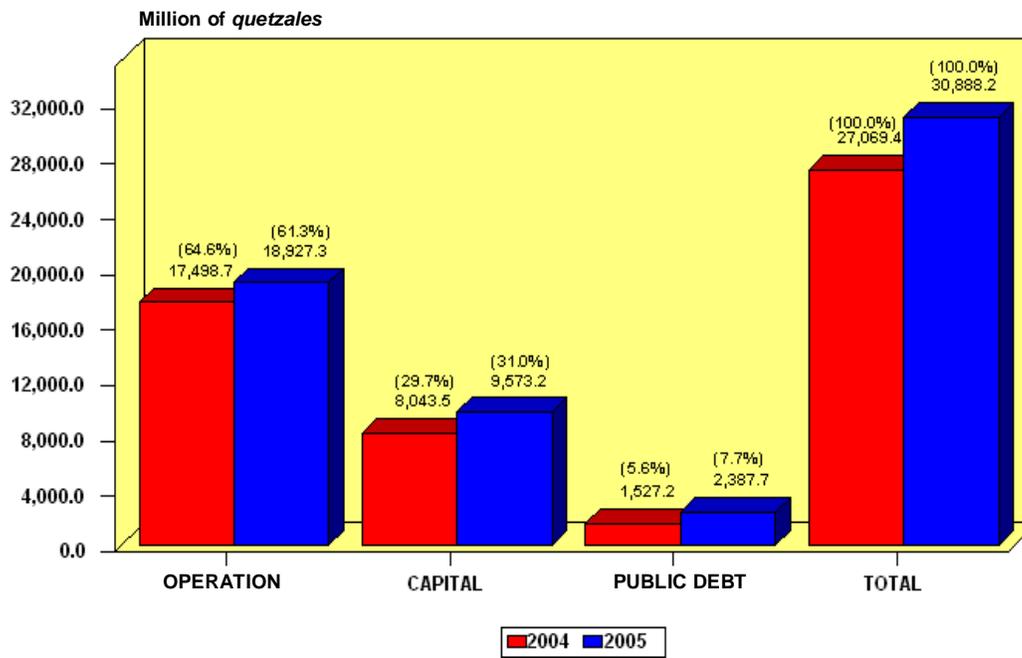


#### D. EXPENSES

The total of expenses of the Central Government in 2005 was of Q30,888.2 million, higher by Q3,818.8 million (14.1%) than the registered in 2004. The operational expenses were of Q18,927.3 million, higher by Q1,428.6 million (8.2%) than the registered in 2004; the capital expenses were of Q9,573.2 million, higher by Q1,529.7 million (19.0%) than the carried out in 2004; and, the expenses of public debt were of Q2,387.7 million, higher by Q860.5 million (56.3%) than the one of 2004. Said sectors represent 61.3%, 31.0% and 7.7% of the total, respectively, while in 2004 said structure was of 64.7%, 29.7% and 5.6%, respectively.



**FIGURE 40**  
**CENTRAL GOVERNMENT**  
**STRUCTURE OF THE TOTAL EXPENSES**  
**YEARS 2004-2005**



### 1. Expenses according to the type of program and specific objective

Meeting the composition of the expense per type of program, the most relevant sectors were Transfers of Capital, (22.6%); Personal Services, (22.2%); Current Transferences, (22.2%); and, Service of the Public Debt (17.2%).

Regarding the Transfers of Capital sector, it reached a total of Q6,968.8 million, higher by Q1,071.8 million (18.2%) than the one of 2004, which was mainly due to the transfer of funds to finance the Rehabilitation and Reconstruction Program originated from the tropical storm Stan.

Regarding the Personal Services sector, which includes, among others, the salaries and wages, which was of Q6,852.2 million, higher by Q17.0 million (0.2%) regarding the one of 2004.

Regarding the Current Transfers sector, it was of Q6,850.0 million, higher by Q882.1 million (14.8%) than the registered in 2004. From this total, Q3,002.4 million corresponded to transfers to the public sector's entities, higher by Q381.7



million (14.6%) than the ones of the previous year. The most import transfers were made to the *Organismo Judicial* of Q682.1 million, to the *Universidad de San Carlos de Guatemala* of Q707.7 million and other institutions of the Central Government of Q912.2 million. The transfers to the private sector were of Q3,339.9 million, higher by Q405.1 million (13.8%) than the ones of 2004. Within them, the benefits of social security (retirements and pensions) were of Q1,665.4 million. On the other hand, the transfers to the foreign sector were of Q507.7 million.

Finally, the expenses of the Service of the Public Debt sector were of Q5,311.0 million, higher by Q1,182.5 million (28.6%) regarding 2004. From that total Q1,424.0 million corresponded to the amortization of foreign loans, Q963.7 million to the amortization of the monetary policy cost of 2003 and Q2,923.3 million to the payment of interests and commissions.

## **2. Expenses per institutional destination**

While analyzing the execution of the governmental expense per institutional destination, it was observed that the entities that executed the highest amount of expenses were the *Ministerio de Educación* with Q4,280.4 million, Q589.4 million (16.0%) higher than the previous year; the *Ministerio de Comunicaciones, Infraestructura y Vivienda* with Q2,429.3 million, Q279.3 million (13.0%) higher than the previous year; Secretaries and other entities of the Executive with Q1,897.9 million, Q354.9 million (23.0%) higher than the previous year; and, *Ministerio de Salud Pública y Asistencia Social* with Q1,858.6 million, Q194.0 million (11.7%) higher than in 2004.

On the other hand, the Obligations of the State that are under the responsibility of the Treasury, which include the financial compromises derived from constitutional mandate and specific laws, from international treaties and contributions to non-governmental organizations and decentralized entities, registered an amount of Q10,145.8 million, Q931.5 million (10.1%) higher than in 2004.



### **3. Expenses according to their nature**

#### **a) Operational expenses**

The operational expenses were of Q18,927.3 million, higher by Q1,428.6 million (8.2%) than in 2004. Regarding their structure, the operational expenses represented 48.4%, transfers 36.2% and interests and commissions of the public debt 15.4%.

Regarding the operational expenses, the same, while being of Q9,154.2 million, increased Q224.6 million (2.5%) regarding the observed in 2004. This variation was due to the increase registered by the expenses for the Acquisition of Goods and Services, which were of Q212.3 million.

The expenses due to transfers were of Q6,849.8 million, which represented an increase of Q882.0 million (14.8%) regarding the previous year.

Regarding the expenses due to interests and commissions of the public debt, these were of Q2,923.3 million, higher by Q322.0 million (12.4%) than the ones of 2004. Said result was influenced by the increase of Q236.1 million (20.0%) in the payment of interests of the domestic public debt.

#### **b) Capital expenses**

Regarding the capital expenses, these were of Q9,573.2 million, higher by Q1,529.7 million (19.0%) than the ones of 2004. From that total, Q2,531.6 million (26.4%) corresponded to the direct investment and Q7,041.6 million (73.6%) to the indirect investment. Regarding the direct investment, highlighted the expense carried out in the Good and Services sector of Q2,475.6 million, higher by Q514.7 million (26.2%) than the one of 2004; while regarding the indirect investment, highlighted the transfers to the public and foreign sector for an amount of Q5,123.3 million and Q1,004.9 million, respectively, higher by Q261.0 million (5.4%) and Q597.1 million (146.4%), respectively, than the ones of 2004.

It is important to mention that from the total of indirect investment, Q6,968.8 million were destined to transfers of capital and Q72.8 million to financial disbursements. From the capital transfers, Q5,123.3 million were destined to the



public sector, Q1,004.9 million to the foreign sector and Q840.6 million to the private sector. Regarding the transfers to the public sector, highlighted the ones made to the country's municipalities of Q2,776.7 million, higher by Q497.5 million (21.8%) than the ones of 2004. On the other hand, Q869.0 million were transferred to the non-financial decentralized and autonomous entities, while to the *Consejos de Desarrollo Urbano y Rural*, Q856.3 million were transferred.

Regarding the destination per sector, highlighted the expenses destined to Housing and Urban Development for an amount of Q4,925.9 million, higher by Q1,439.7 million (41.3%) than the registered in 2004, as well as the destined to Transport for an amount of Q2,267.2 million, higher by Q172.6 million (8.2%) than the ones of 2004.

## **E. FISCAL CASH**

During the fiscal year 2005, the Central Government had available funds of Q31,273.6 million, which included the ones derived from negotiations of domestic and foreign public debt; while it paid an amount of Q32,582.9 million. Consequently, a negative variation of Q1,309.3 million was registered in the fiscal cash.

Regarding the fiscal cash incomes, the current incomes were of Q24,524.2 million (78.4%); the ones derived from the placement and disbursement of public debt of Q6,366.9 million (20.4%); the ones that correspond to donations were of Q356.9 million (1.1%); and, the capital incomes were of Q25.6 million (0.1%).

Regarding the expenses, Q28,500.5 million (87.5%) corresponded to operational and investment programs; Q1,694.7 million (5.2%) to repurchase of public securities; Q1,424.0 million (4.4%) to amortization of the foreign public debt; and, Q963.7 million (2.9%) to amortize the cost of the monetary policy of the fiscal year 2003.



### Rehabilitation and Reconstruction Program derived from the Tropical Storm Stan

The execution of the Central Government expense in 2005 was influenced by the impact that the tropical storm Stan represented for the national economy, which directly and indirectly affected 133 municipalities of the country and about 3.5 million people. The damages and losses, according to the report carried out by the Economic Commission for Latin America -CEPAL-<sup>1</sup> were estimated in Q7,472.7 million, not only in the social but also in the productive environment, besides the destruction and detriment of the public and private infrastructure.

The severity of the damages caused, forced the government to declare the public calamity estate for a thirty-day period, through Governmental Decree number 1-2005 dated October 5<sup>th</sup>, 2005, which was ratified by the Congress of the Republic through Decree number 70-2005. Said term was extended for another thirty days, through Decree Number 79-2005 of the Congress of the Republic. On the other hand, the Governmental Agreement 528-2005 authorized the *Ministerio de Finanzas Públicas* to approve the necessary transfers or amendments in order to finance the Rehabilitation and Reconstruction Program originated by the Tropical Storm Stan.

Based on the mentioned decisions, Governmental Agreement number 533-2005 was issued, which declared as national interest and urgency the purchase and contracting of goods, supplies, works and services in order to satisfy the requirements of the affected population and, the repair or rehabilitation of the damaged infrastructure.

In the mentioned context, the total amount of funds executed in 2005 within this program was of Q978.3 million, representing 3.4% of the total expenses and near of 0.4% of the GDP. From the indicated amount, Q428.3 million were used to assist the emergency derived from said climatic phenomenon that occurred between October and December 2005 and, with the remaining Q550.0 million, in December of said year, the provision of funds was made to finance the program through the establishment of a trust in the *El Crédito Hipotecario Nacional de Guatemala*.

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<sup>1</sup> *Secretaría de Planificación y Programación de la Presidencia y Comisión Económica para América Latina y el Caribe*. "The Disaster of October 2005 in Guatemala. Preliminary estimation of its Socioeconomic and Environmental Impact". <http://www.segeplan.gob.gt/stan/informes.htm>



## F. DEBT OF THE PUBLIC SECTOR

### 1. Domestic public debt

#### a) Circulation of the domestic public debt

To December 31<sup>st</sup>, 2005 the balance of the domestic debt of the non-financial public sector was of Q16,425.7 million, higher by Q3,584.9 million than the registered in the same date of 2004, which caused the domestic debt and GDP relation to increase from 5.9% in 2004 to 6.8% by the end of 2005.

<b>YEARS</b>	<b>BALANCE</b> <b>(Million of <i>quetzales</i>)</b>	<b>BALANCE/GDP</b> <b>(%)</b>
1996	5,754.8	6.0
1997	5,865.6	5.4
1998	6,259.5	5.0
1999	7,807.1	5.8
2000	8,629.6	5.8
2001	9,281.5	5.6
2002	8,168.5	4.5
2003	11,036.7	5.6
2004	12,840.8	5.9
2005	16,425.7	6.8

SOURCE: *Ministerio de Finanzas Públicas* and *Banco de Guatemala*.

The growth of the domestic public debt of Q3,584.9 million was due to the negotiation of security titles of Q5,279.7 million and to the payment of bonded debt, to its expiration, of Q1,694.8 million. Regarding the negotiations, Q1,619.1 million were made directly and Q3,660.6 million through bid and auction mechanisms. It is important to mention that the total of security titles was carried out through Treasury Bonds of the Republic of Guatemala.



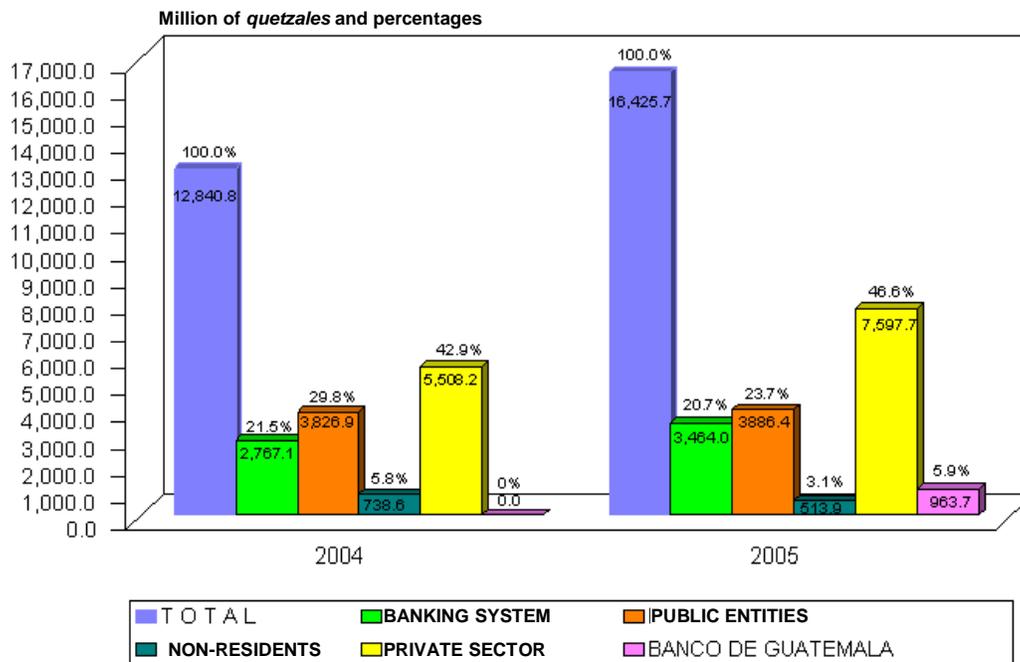
### **b) Balance and distribution per holder of the domestic public debt**

In the balance of the domestic public debt, to December 2005, highlight the Treasury Bonds in dollars of the United States of America, which represent 36.5% of the referred balance (US\$771.8 million), lower than the percentage registered in 2004, which was of 54.1% (US\$892.6 million).

Regarding the distribution per holder of the domestic public debt, it varied as a result of the higher negotiations carried out with the private sector. In effect, in 2005, the participation of said sector within the total of the domestic public debt was of 46.6%, higher than the percentage registered in 2004 (42.9%). On the other hand, the public, banking and non-resident sector reduced their participation in the same period, from 29.8%, 21.5% and 5.8% in 2004 to 23.7%, 20.7% and 3.1% in 2005, respectively. It is important to indicate that, in August 2005 the *Ministerio de Finanzas Públicas* issued Treasury Bonds in favor of the *Banco de Guatemala* of Q963.7 million (5.9% of the total of domestic debt of 2005), in order to cover the Central Bank's net deficiency of the fiscal year 2003.



**FIGURE 41**  
**BALANCE OF THE DOMESTIC PUBLIC DEBT**  
**PER HOLDER**  
**YEARS 2004-2005**



### c) Interest rate

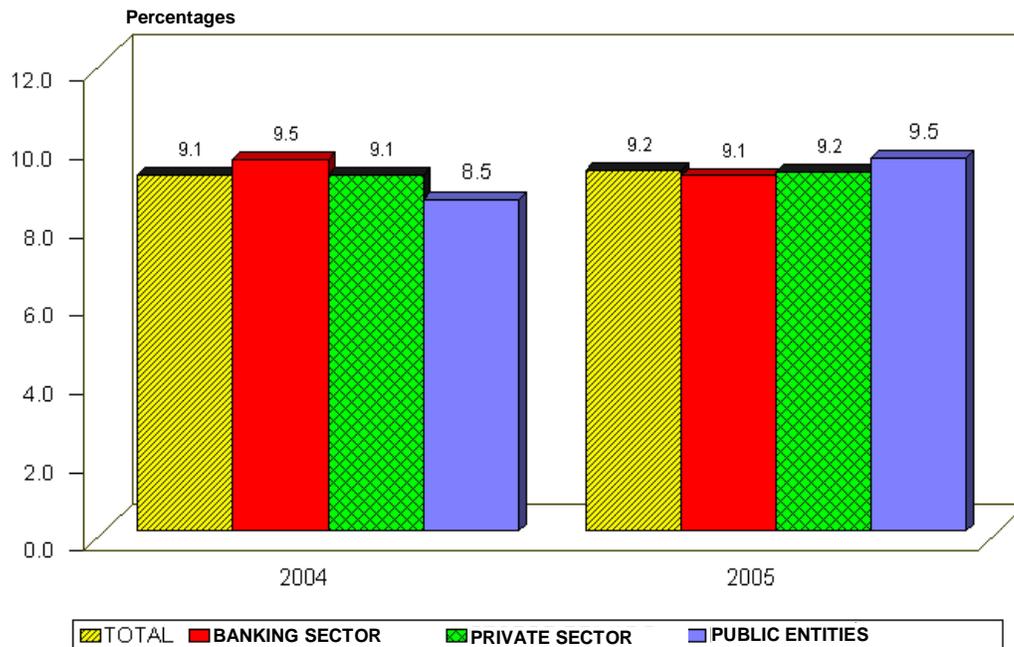
During 2005, the weighted average interest rate, applied for the placements in national currency in the domestic market, registered a slight increase, from 9.1% in 2004 to 9.2% in 2005. It is important to indicate that in said year there were no placements in foreign currency in the domestic market.

In the following figure appears a weighted average interest rate, in national currency, of the bonded domestic debt per holder<sup>38</sup>.

<sup>38</sup> The estimation of the weighted average interest rate does not include the Treasury Bonds issued by the *Ministerio de Finanzas Públicas* in favor of the *Banco de Guatemala*, to restore its net deficiency of the fiscal year 2003, which is of 3.87% annually.



**FIGURE 42**  
**WEIGHTED AVERAGE INTEREST RATE OF THE**  
**BONDED DOMESTIC DEBT**  
**IN NATIONAL CURRENCY PER HOLDER**  
**YEARS 2004-2005**



Regarding the expiration date of the domestic public debt, by the end of 2005, 9.5% of the balance was placed to less than six months (8.7% in 2004), 11.0% was concentrated in terms between six months and one year (4.5% in 2004) and 79.5% in terms higher than one year (86.8% in 2004). It is important to indicate that due to interests and commissions on the domestic debt, in 2005, Q1,392.8 million were paid, higher by Q211.6 million than the one of 2004.

## 2. Foreign public debt<sup>39</sup>

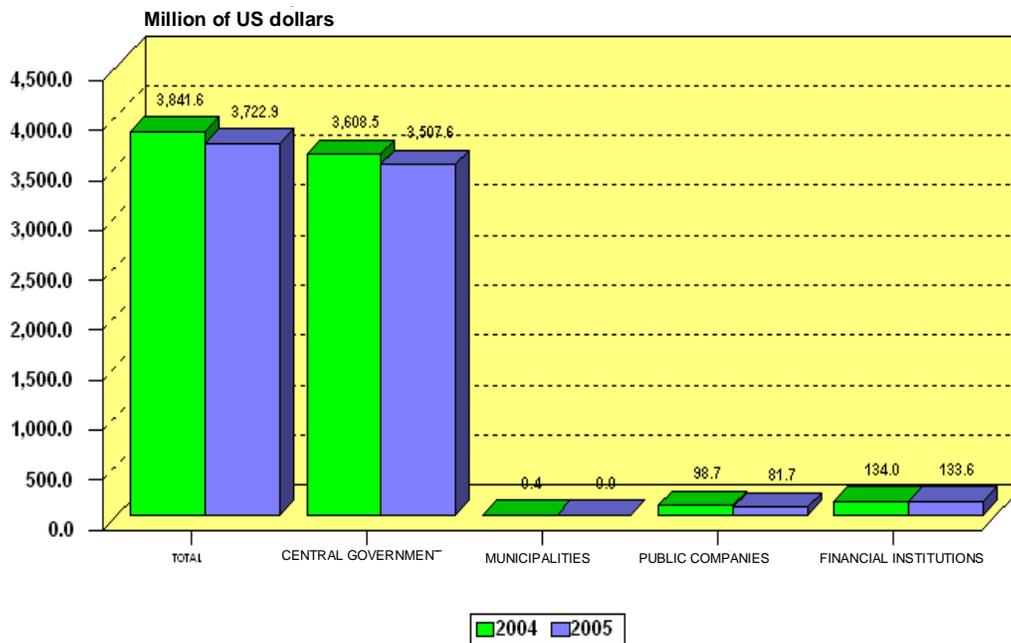
To December 31<sup>st</sup>, 2005, the balance of the foreign public debt was of US\$3,722.9 million, equivalent to 11.8% of the GDP, lower in US\$118.7 million

<sup>39</sup> Does not include the foreign debt of the *Banco de Guatemala*, the balance of which to December 2005 was of US\$0.3 million.



than the registered in the same date of 2004. Said result is explained by loans disbursement of US\$142.8 million, amortization of foreign loans of US\$197.3 million and a reduction in the debt balance of US\$64.2 million, due to the registry in favor of the Central Government because of the appreciation of the dollar of the United States of America with regard to the currencies in which some loans abroad are expressed.

**FIGURE 43**  
**BALANCE OF THE FOREIGN PUBLIC DEBT <sup>1/</sup>**  
**YEARS 2004-2005**



<sup>1/</sup> PRELIMINARY DATA

Regarding the disbursement of loans abroad of US\$142.8 million received during 2005, highlighted the ones provided by the BCIE of US\$51.7 million, IBRD of US\$36.5 million and IBD of US\$34.0 million. According to the *Ministerio de Finanzas Públicas*, the funds obtained from foreign sources were destined to finance social developmental projects (35.5%), roads (14.6%), investment funds (13.7%), education (8.8%), health and social assistance (8.1%), agriculture and livestock (5.7%) and other destinations (13.6%).



Regarding the integration of the balance of foreign public debt, per debtor, to December 31st, 2005, US\$3,507.6 million (94.2%), corresponded to the Central Government, US\$133.6 million (3.6%) to the public financial institutions and US\$81.7 million (2.2%) to the public companies.

Regarding the balance of the foreign public debt per creditor, 55.0% of the total corresponded to multilateral financial organizations, mainly to the IBD with a balance of US\$1,233.1 million, which represented 33.1% of the total; 11.8% corresponded to bilateral financial organizations and governments, being the Government of the United States of America the highest creditor, whose Agency for International Development (AID) and the Department of Agriculture jointly represented 3.6% of the total; 29.7% corresponded to Treasury Bonds in dollars of the United States of America; and, 3.5% to the *Banco Bilbao Vizcaya Argentaria*.

The payment of the foreign public debt service in 2005 was of US\$396.8 million, from which, US\$197.3 million corresponded to capital and US\$199.5 million to interests and commissions. From the amortizations, US\$143.4 million (72.7% of the total) were paid to multilateral financial organizations, while the payment of interests and commissions to said creditors was of US\$83.5 million (41.9% of the total). To the bilateral financial organizations and governments, US\$53.9 million were paid due to capital and US\$15.4 million due to interests and commissions, while US\$100.6 million were paid due to interests and commissions of Treasury Bonds placed abroad.

Finally, it is important to indicate that among the indicators that are usually used to measure the sustainability of the foreign indebtedness is the one of the foreign public debt regarding the gross domestic product, which was placed in 11.8% in 2005, lower in 2.3 percentage points than the one of 2004; the foreign public debt as a proportion of the export of goods and services was placed in 71.8%, lower in 9.6 percentage points than the ones of 2004; and the service of the debt regarding the export of goods and services, was of 7.6%, lower in 0.7 percentage points than



in the previous year<sup>40</sup>.

CUADRO 22

**PUBLIC SECTOR <sup>1/</sup>**  
**FOREIGN DEBT**  
**YEARS 1996 - 2005<sup>a/</sup>**

YEARS	BALANCE US\$ MILLION	BALANCE / GDP (%)	BALANCE / EXPORTS OF GOODS AND SERVICES (%)	SERVICE / EXPORTS OF GOODS AND SERVICES (%)
1996	1,751.0	11.2	61.8	8.3
1997	1,926.4	10.8	59.0	5.0
1998	2,212.0	11.5	61.7	5.2
1999	2,504.4	13.7	70.3	5.5
2000	2,540.9	13.2	62.3	5.7
2001	2,833.7	13.5	67.1	7.6
2002	3,038.4	13.1	73.6	7.4
2003	3,396.8	13.7	79.0	7.3
2004	3,841.6	14.1	81.4	8.3
2005	3,722.9	11.8	71.8	7.6

1/ Does not include the debt of the *Banco de Guatemala*.

a/ Preliminary data.

SOURCE: *Ministerio de Finanzas Públicas* and *Corporación Financiera Nacional - CORFINA* -

## G. MAIN DECISIONS REGARDING THE PUBLIC FINANCES IN 2005

1. Decree number 31-2005 of the Congress of the Republic approves the Free Trade Agreement, Dominican Republic, Central America and the United States of America, subscribed in the city of Washington, D. C., on August 5<sup>th</sup>, 2004.
2. Decree number 38-2005 of the Congress of the Republic establishes Reforms to the Law of tax for the Distribution of Crude Oil and Fuels derived from oil, Decree number 38-92 of the Congress of the Republic. Said

<sup>40</sup> According to the parameters established by international financial organizations, the rate of the international monetary reserves and the foreign position of a country are committed when the relations of the foreign public debt regarding the gross domestic product and the balance of the foreign public debt regarding the export of goods and services surpass 35% and 150%, respectively, and, when the relation of the foreign public debt service regarding the export of goods and services surpass 25%.



reforms pursue to restore the current legal frame for said tax. In that sense, among other changes, Article 2 was reformed regarding the tax generating factor, which was suspended by the *Corte de Constitucionalidad* as of December 16<sup>th</sup>, 2004.

3. Decree number 77-2005 of the Congress of the Republic introduces Reforms to the Law of the Income Tax, which are contained in Decree number 26-92 of the Congress of the Republic. Said reforms refer, particularly, to the application of 30% as taxable income, derived from the gross incomes obtained by the owners of producing companies, distributors and intermediary companies abroad due to the use in Guatemala of Cinematographic films, films for television, radio soap operas, phonographic disks, magnetophonic tapes, comic strips, picture novels and any other means of projection, transmission or diffusion of images and sounds, to be exhibited, transmitted or spread in the Republic of Guatemala.
4. Ministerial Agreement number 0350-2005 of the *Ministerio de Economía* publishes resolution number 135-2005 (COMIECO-EX) of the *Consejo de Ministros de Integración Económica* through which the amended version of resolution number 132-2004 (COMIECO-XXX) is extended for a six-month period, which contains modifications to the Central American Import Tariff, applicable only for Guatemala, mainly for the following sectors: oil, aviation gasoline, the rest of gasoline, the rest of kerosene, diesel oil, diesel oil, bunker C, the rest of fuel oils and natural gas.
5. Ministerial Agreement number 0373-2005 of the *Ministerio de Economía* publishes Resolution number 138-2005 (COMIECO-EX) of the *Consejo de Ministros de Integración Económica*, through which Resolution number 132-2004 was revoked, amended through Resolution number 133-2005 and extended through Resolution number 135-2005 (COMIECO-EX), leaving without effect the mentioned modifications, except the tariff to “the rest of gasoline” (Tariff code 27101130) which would remain until September 4<sup>th</sup> of said year with an Import Tariff Right -DAI- [Acronym in Spanish.] of 40%.



6. Governmental Agreement number 0387-2005 authorizes the Secretary of the *Coordinación Ejecutiva de la Presidencia* to subscribe, jointly with the legal representative of *El Crédito Hipotecario Nacional de Guatemala*, the Trust “Forest and water for the Concordia”, the objective of which is to contribute in improving the quality of life of Guatemalan people, the reforestation in governmental, municipal and communal lands, the maintenance of the municipal water fountains and the development of the forestry culture in the Guatemalan rural areas. The initial wealth of the trust is of Q890.0 million.
7. Governmental Agreement number 528-2005 authorizes the *Ministerio de Finanzas Públicas*, with urgent character, to authorize the necessary transfers and amendments in the General Income and Expense Budget of the state for the fiscal year 2005, to finance the “Rehabilitation and Reconstruction Program originated from the Tropical Storm Stan”. Besides, it was authorized to renegotiate the destinations of the resources provided by the reimbursable and non-reimbursable foreign cooperation, so that the same is compatible with the situations derived from the emergency and reconstruction.
8. Governmental Agreement number 704-2005 authorizes the Ministry of the *Ministerio de Finanzas Públicas*, in fulfillment of the Special Power of Attorney with Representation granted by the *Procurador General de la Nación*, to subscribe with the legal representative of *El Crédito Hipotecario Nacional de Guatemala* the public deed that establishes the “Trust for Rehabilitation and Reconstruction, Tropical Storm Stan”, which has as objective the administration, execution and payment of the acquisition and contracting of works, supplies, goods and services carried out by public entities. The initial wealth of the trust is of Q600.0 million.