October 2005
IMF Country Report No. 05/362

# Guatemala: 2005 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Guatemala

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2005 Article IV consultation with Guatemala, the following documents have been released and are included in this package:

- the staff report for the 2005 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on April 15, 2005, with the officials of Guatemala on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 29, 2005. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its May 16, 2005 discussion of the staff report that concluded the Article IV consultation.

- a statement by the Executive Director for Guatemala.

The document listed below has been or will be separately released.

Statistical Annex

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

GUATEMALA

# Staff Report for the 2005 Article IV Consultation

Prepared by the Staff Representatives for the 2005 Consultation with Guatemala

Approved by Markus Rodlauer and Carlos Muñiz

April 29, 2005

- **Discussions**: Discussions for the 2005 Article IV consultation were held in Guatemala City during February 2–15, and at headquarters on April 15. The staff team met with Vice President Eduardo Stein, Minister of Finance de Bonilla, Central Bank President Sosa, Minister of Economy Cuevas, congressional leaders, other senior officials, and representatives of the private sector and civil society. The following staff members participated in one or more rounds of the discussions: O. Gronlie (head), H. Monroe, M. Rodríguez, A. Go (all WHD), and K. Alexandraki (PDR). The team was assisted by E. Offerdal (Resident Representative). The February mission worked closely with a staff team from FAD (headed by C. Silvani) that provided technical assistance in tax administration.

- **Article IV consultation**: The discussions focused on the near-term macro framework and economic vulnerabilities, as well as reforms to promote growth, competitiveness, and social progress under the government's structural reform plan, *Vamos Guatemala*. Particular attention was given to efforts aimed at raising tax revenue, reducing inflation, advancing the financial sector reforms, and improving transparency and governance.

- **Last Article IV consultation**: At the conclusion of the last consultation on October 2, 2002, Directors welcomed the authorities' medium-term economic strategy and their plans to strengthen the tax effort. They stressed the need to reduce inflation, implement financial sector reforms, and improve governance.

- **Fund relations**: Guatemala has no outstanding credit from the Fund and has accepted the obligations under Article VIII, Sections 2, 3, and 4 of the Articles of Agreement. The exchange regime is flexible in the context of a managed float without a predetermined path for the rate. The exchange system is free of restrictions on the making of payments and transfers for current international transactions.

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## EXECUTIVE SUMMARY

**Guatemala has pursued important reforms and macroeconomic stabilization since the 1996 Peace Accords**. Fiscal discipline has anchored the policy framework; international reserves have risen; and important banking reforms have been implemented. Following three years of slow growth, activity improved somewhat in 2004, but inflation also rose, partly due to higher oil prices.

**Nevertheless, the economic and social goals of the Peace Accords remain to be fully realized**. Efforts to increase tax revenues to fund higher social and investment spending have stalled in recent years. Guatemala continues to suffer from widespread poverty; and, according to a 2002 World Bank survey, perceptions of corruption, and weak integrity of some public institutions pose additional challenges.

**The government that took office last year has included the 1996 Peace Accords in the platform for its policy agenda**. The Accords embody a broad national consensus on economic, social, and security priorities. Reflecting this, the government's economic program rests on three main pillars: macroeconomic stability; financial sector restructuring; and structural reforms to boost growth and reduce poverty.

**A key objective of the program is to keep the fiscal deficit low**. Within this framework, the government is seeking to mobilize additional fiscal resources to finance a significant increase in public investment and social spending.

**Monetary policy is being geared to reducing inflation to the 4–6 percent range**. The exchange system is flexible, but the central bank has intervened in the foreign exchange over the past year to limit the nominal appreciation of the quetzal against the U.S. dollar. In January 2005 a rules-based mechanism for interventions was introduced.

**The Guatemalan banking system has been strengthened in recent years**. Prudential norms have been tightened and offshore banks have been brought into the regulatory framework. The reform process is continuing, and steps are being taken to address the persistent losses of the state mortgage bank (CHN).

**The government's structural reform program, *Vamos Guatemala,* is focused on promoting competitiveness, economic growth, and social progress**. A key goal is to foster a business climate characterized by transparency, the rule of law, and good governance; a Commissioner for Competitiveness has been appointed; and implementation of CAFTA-DR is expected to underpin the recovery. Social spending and the development effort are being stepped up, particularly in the poorest municipalities.

**Success of the program will hinge on the government's ability to strengthen the revenue effort, focus spending on priority needs, and improve transparency and governance**. To this end, the government has launched a national consultation process, engaging broad groups of Guatemalan society in a dialogue to build consensus on national priorities and their funding.

**With its record of overall fiscal discipline, low public debt, and a strengthened banking system, Guatemala's economic vulnerabilities are well contained**. Nonetheless, the policy framework is susceptible to erosion of public support, in part because of low domestic revenue and the resulting constraints on the government's capacity to address poverty and infrastructure bottlenecks. The government's program is designed to reduce this risk by mobilizing revenue, prioritizing expenditures, and improving governance

# I. BACKGROUND

## A. A Brief Perspective

1. **The 1996 Peace Accords, which ended nearly 40 years of civil conflict, embodied a broad national consensus on economic, social, and security priorities**. The advent of political stability gave rise to a significant peace dividend in the second half of the 1990s: economic growth rose to 4 percent a year and nontraditional exports increased, helping to diversify the economy. Growth slowed during 2001–03 amid falling coffee prices and weaker external demand, but macro stability was maintained by policies anchored on a strong fiscal stance, and a flexible exchange rate regime—resulting in low public debt (18 percent of GDP) and a strong international reserves position. Progress was also made on some important structural reforms (such as in the financial sector), but other reform goals of the Peace Accords—particularly in the fiscal, social, and governance areas—were only partially achieved.

2. **In particular, Guatemala continues to face serious problems of poverty and income distribution**. Some social indicators have improved, but Guatemala falls below the Latin American average for all available indicators. Governance also has been a concern, and government effectiveness and regulatory quality are perceived to have slipped since the end of the 1990s.[1]

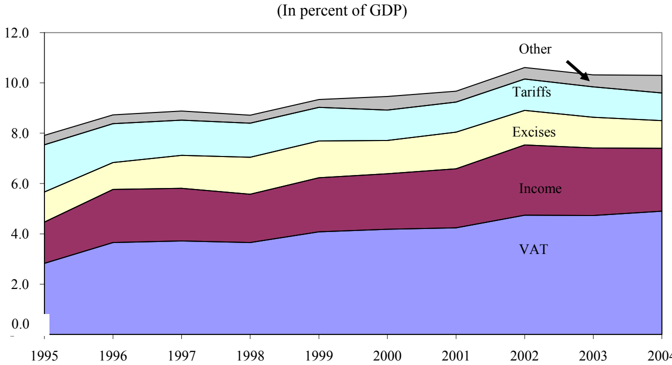
Central America: Comparative Social and Governance Indicators

| | Rank in Human Dev. Index (2004) | Life Expectancy at Birth (years, 2001) | Adult Illiteracy (percent, 2001) | Poverty Rate (percent, 1987-2001) | Control of Corruption (percentile, 2002) |
|---|---|---|---|---|---|
| Costa Rica | 45 | 78.0 | 4.2 | 9.5 | 79.4 |
| El Salvador | 103 | 70.6 | 20.3 | 45.0 | 36.6 |
| **Guatemala** | **121** | **65.7** | **30.1** | **56.2** | **30.9** |
| Honduras | 115 | 68.8 | 20.0 | 53.0 | 27.3 |
| Nicaragua | 118 | 69.4 | 33.3 | 47.9 | 39.7 |
| Latin America (average) | ... | 70.5 | 11.4 | ... | 54.9 |

Sources: UNDP Human Development Report 2004; and World Bank.

3. **Successive governments have faced serious obstacles to raising additional revenue and fund higher social spending**. Powerful interest groups have opposed higher taxes and often successfully challenged existing taxes in court (Box 1). After some progress during 2000–02 in raising the tax/GDP ratio toward the 12 percent target established under the Peace Accords, the ratio slipped again in 2003–04 as the courts overturned some key taxes. As a result, part of the increase in social spending achieved in the second half of the 1990s has been reversed since 2001 (Box 2).

Composition of Tax Revenues
(In percent of GDP)




[1] See World Bank, Governance Research Country Snapshot: 1996–2002, http://info.worldbank.org/governance/kkz/.

**Box 1. Legal Challenges and Instability of the Tax System**

**Legal challenges have been constant threats to the stability of the tax system**. During 2001–03 the Constitutional Court (CC) received more than fifty appeals to eliminate, clarify, or reduce taxes. Many of the appeals have been brought with reference to Article 243 in the constitution, which establishes the principle that taxes should not exceed the payment capacity of the tax payer.

**While most appeals have been rejected, the CC has ruled against the state in a number of cases**. This has created an unpredictable tax environment and eroded the tax base, and court rulings threatened to reduce tax revenue by more than 1 percent of GDP in 2004. The most recent rulings were in December 2003 when the CC eliminated the minimum corporate tax (IEMA), and in December 2004 when an injunction was issued against the excise tax on fuel. The legal challenges reflect an entrenched opposition to higher taxes in Guatemala, which have frustrated a number of previous attempts to strengthen the revenue effort.

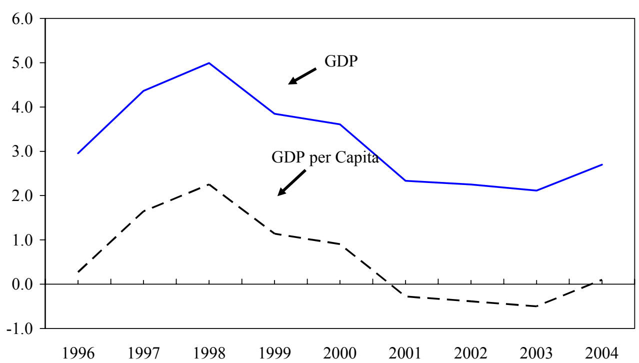
4. **The government that took office in January 2004 was elected on a platform of market-oriented economic policies and the agenda of the Peace Accords.** Its structural reform program, *Vamos Guatemala*, aims to improve economic growth, competitiveness, and social conditions. An assertive strategy to combat corruption and improve governance is also central to the agenda. The government's minority position in congress remains a significant challenge.

## B. Recent Economic Developments

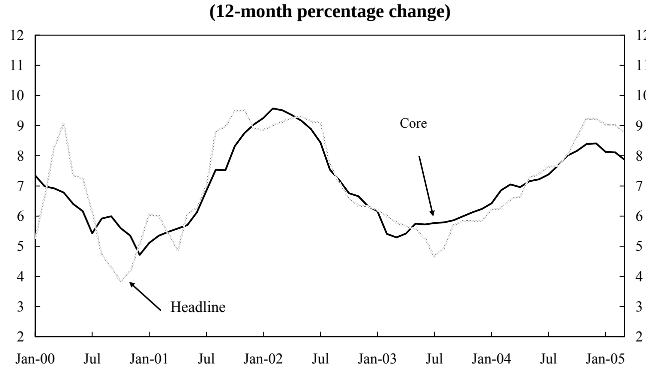
### Macroeconomic framework

5. **Economic growth has been sluggish in recent years, with only a modest recovery in 2004**. Real GDP grew by just over 2 percent per year during 2001–03, amid political uncertainty, falling coffee prices, and a deteriorating business climate. Growth is estimated at 2¾ percent in 2004, supported by private investment and consumption. The latter has been fueled, in part, by rising worker remittances.

**Real GDP**
**(percentage growth)**




**Inflation**
**(12-month percentage change)**



## Box 2. Social Expenditure

Following the signing of the Peace Accords in 1996, the government outlined a comprehensive social program with major initiatives in the areas of education, health, housing, and the justice and security systems.

The program embodied three overarching goals: (i) expanded access to services, especially for the poor and the indigenous population; (ii) decentralization, with emphasis on community and private sector participation in service delivery; and (iii) economic efficiency in the public sector through improved financial management, outsourcing, and competitive procurement practices. The programs would be financed by external donors and by an increase in the domestic tax effort to 12 percent of GDP (from 8 percent of GDP in 1995). While social expenditures increased in the second half of the 1990s, they have declined since 2001. Likewise, the tax effort was raised to 10.6 percent of GDP in 2002, but it has since declined.

**Education**

Objectives: Expanded access to primary education; drop out rates; and increase in adult literacy.

Programs:
- Expansion of a new model of community and parent managed primary schools in the rural areas.
- Increased public investment in rural schools.
- Increased bilingual education, teacher training, and education for girls.

**Health**

Objectives: Decentralization and expansion of access to public health services in rural areas; substantial reductions in infant and maternal mortality rates.

Programs:
- Community-based projects to deliver basic health services to rural areas.
- Community-based water and sanitation projects.
- Decentralization of public health care management and rehabilitation of existing health centers.

**Housing**

Objectives: Increased low and middle-income urban housing construction.

Programs:
- Development of a housing subsidy program.
- Legal and regulatory reforms to promote development of a market in low-cost urban land.

**Judicial System and Internal Security**

Objectives: Improved access and quality of the justice system (especially in rural areas).

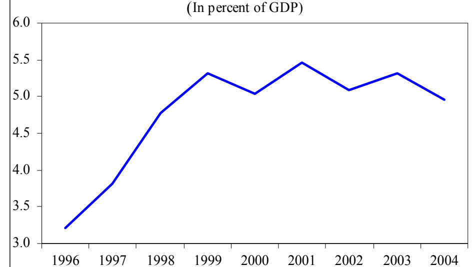
Programs:
- Creating and training a national civilian police force.
- Creating a career civil service for judges and expanding justice system personnel, courts, and public defenders in rural communities.
- Expanding and improving training programs for the police, public prosecutors, and judiciary personnel.
- Special assistance for indigenous language speakers.

Social Expenditure as defined under the 1996 Peace Accords
(In percent of GDP)

| | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|---|---|---|---|
| Health | 0.9 | 1.1 | 1.1 | 1.4 | 1.4 | 1.4 | 1.3 | 1.3 | 1.2 |
| Education | 1.6 | 1.8 | 2.1 | 2.4 | 2.5 | 2.7 | 2.5 | 2.5 | 2.5 |
| Housing | 0.0 | 0.1 | 0.5 | 0.3 | 0.0 | 0.1 | 0.1 | 0.1 | 0.1 |
| Internal Security | 0.4 | 0.5 | 0.6 | 0.7 | 0.7 | 0.8 | 0.7 | 0.8 | 0.6 |
| Judicial System | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.3 | 0.4 | 0.3 |
| Attorney General | 0.1 | 0.1 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 | 0.2 |
| **Total** | **3.2** | **3.8** | **4.8** | **5.3** | **5.0** | **5.5** | **5.1** | **5.3** | **5.0** |
| *Memorandum item* | | | | | | | | | |
| Guatemalan Army | 0.8 | 0.7 | 0.7 | 0.7 | 0.8 | 0.9 | 0.7 | 0.5 | 0.4 |

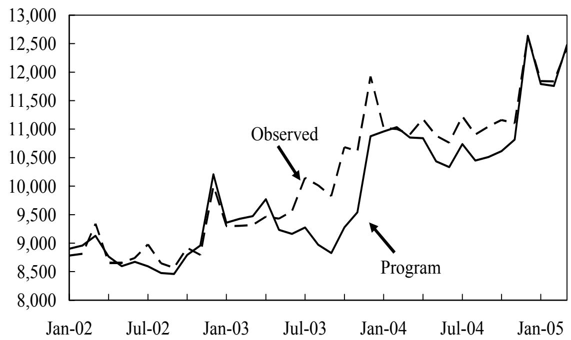
Source: Ministry of Finance.

Social Expenditures
(In percent of GDP)

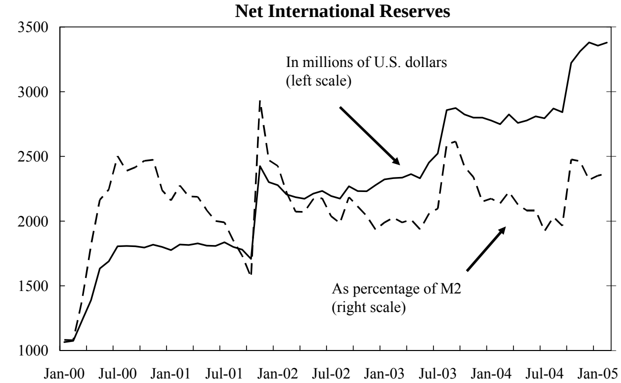


6. **Headline inflation rose to over 9 percent in 2004,** well above the central bank's target range of 4–6 percent, but has declined somewhat in 2005. Higher oil prices and relatively easy monetary conditions contributed to last year's increase. Although the central bank has raised its benchmark interest rate on several occasions since July 2003, the rate remains negative in real terms, and commercial bank rates have continued to decline.

**Currency Issue**
**(In millions of quetzales)**

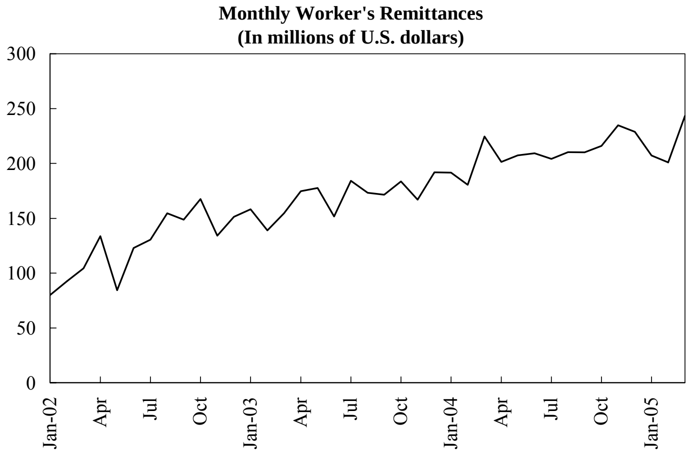


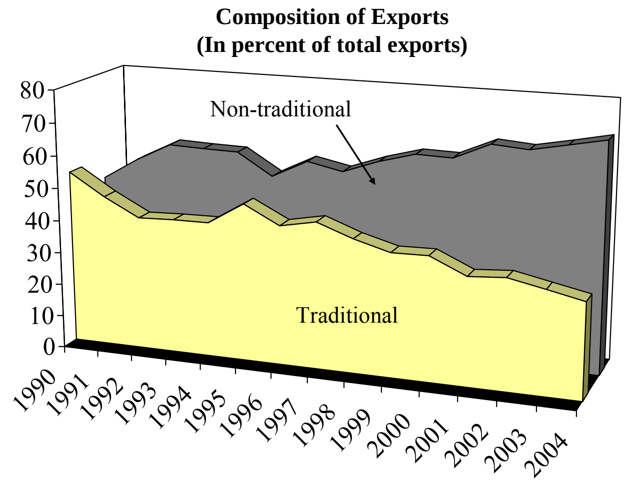

**Net International Reserves**



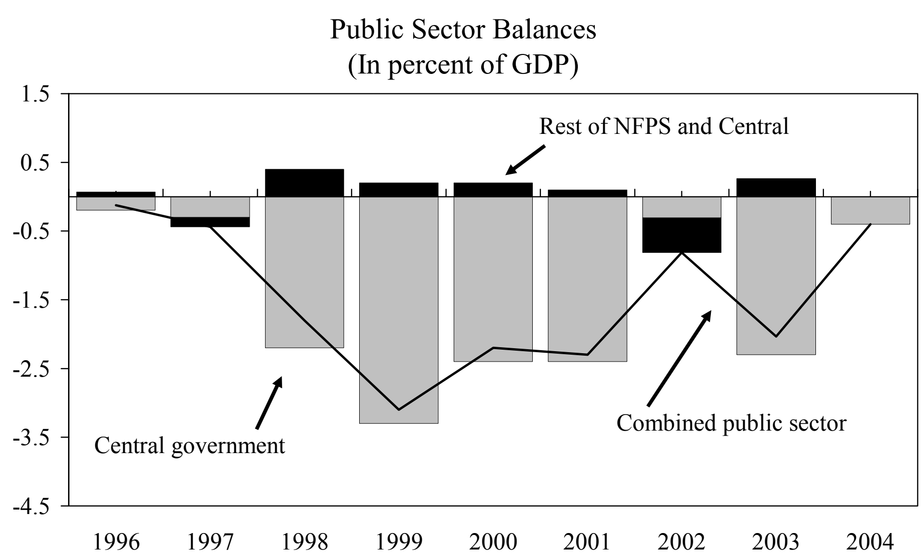

7. **The balance of payments has strengthened in recent years, with international reserves now covering 4½ months of imports**. The current account deficit has narrowed to about 4 percent of GDP, helped by a sharp rise in worker remittances, now at more than 9 percent of GDP. The rise in remittances, together with capital inflows and the global weakening of the U.S. dollar, has put upward pressure on the quetzal. To stem the pressure, the central bank intervened in the foreign exchange market for US$450 million last year, limiting the appreciation to 3 percent against the dollar.[2] The trade deficit has continued to widen, however, to about 15 percent of GDP, as import demand has been fueled by remittances and a steady real appreciation of the quetzal (by over 20 percent since 2000).

[2] In January 2005, the central bank introduced a rules-based mechanism for intervention in the foreign exchange market to "avoid an abrupt rise in the exchange rate of the quetzal." The bank indicated that, given the recent upward pressure on the quetzal, it would postpone defining a similar rule for intervention to stem an abrupt fall. Under this mechanism, the central bank offers to purchase US$10 million at a rate for the quetzal that is 0.5 percent more appreciated than its five-day moving average. If the market sells the full US$10 million, the bank would also offer to buy additional installments of US$10 million during the same day, successively, at a rate of 0.0025 per U.S. dollar above the previous rate until the market closes. This mechanism has been subject to modification since it was initially implemented, and is currently under review by the central bank.



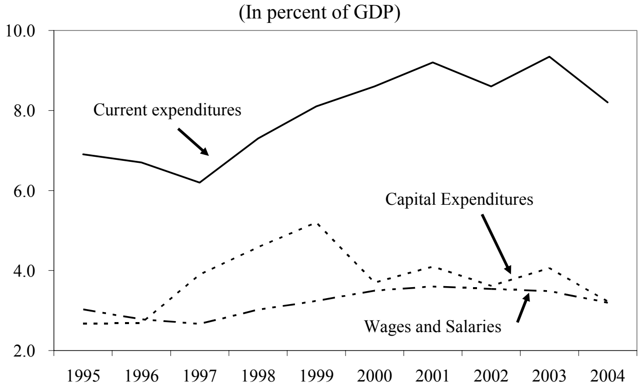

8. **While Guatemala's overall export performance has lagged in recent years, nontraditional exports have done quite well**. Growth of traditional exports (coffee, sugar, bananas, and cardamom) has been limited by adverse price developments, trade barriers in key markets, and supply-side constraints. Nontraditional exports (textiles, light manufactures, and specialty agriculture), on the other hand, have shown robust growth, in part because of preferential access to the U.S. market under the Caribbean Basin Initiative (CBI).



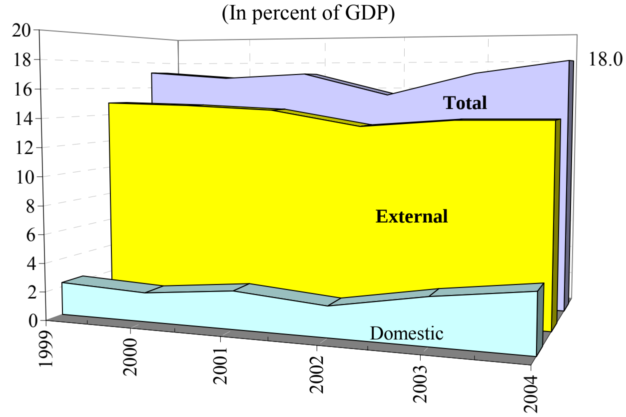
## Fiscal policy

9. **Fiscal discipline has been broadly maintained despite the weak revenue base**. The fiscal deficit widened in 2003, mainly because of court-ordered tax reductions and compensation payments to auxiliary soldiers for service in the civil conflict, but it fell to less than ½ percent of GDP in 2004. Spending was reduced sharply in 2004 as the new government faced additional tax reductions and legal problems that delayed execution of the investment program. To offset the impact of the court rulings and raise tax collections toward the 12 percent of GDP target, the government launched a tax plan soon after taking office last year, comprising policy measures and a blueprint for strengthening tax administration and tax enforcement.[3] Although an initial tax package passed by congress in June 2004 fell short of the government's proposal, the tax administration plan generated more revenue than expected, keeping tax collections at the level of 2003 (10.3 percent of GDP).

Composition of Central Government Expenditures
(In percent of GDP)




Nonfinancial Public Sector Debt
(In percent of GDP)




10. **Access to external market financing improved last year**. In 2003, a planned Eurobond issue was reduced by nearly half, to US$300 million, because domestic investors were reluctant to participate. By contrast, in September 2004 a 30-year US$330 million issue was significantly oversubscribed, and with the lower fiscal deficit, the public sector turned from sizeable net domestic borrowing in 2003 (1.2 percent of GDP) to a small net domestic lending position in 2004.

## The financial sector

11. **The reforms recommended in the 2001 FSSA have been pursued vigorously**. Financial sector legislation has been comprehensively modernized, and a tighter prudential framework with strengthened onsite inspections has induced notable improvements in solvency, asset quality, and liquidity. Offshore banks are now required to be part of licensed

[3] The tax plan is discussed in paragraph 23.

financial conglomerates to operate in Guatemala. The reported risk-weighted capital adequacy ratios of both onshore and offshore banks are well above the statutory minimum of 10 percent. In July 2004 the FATF removed Guatemala from its list of noncooperating jurisdictions on money laundering.

Banking System Prudential Indicators

(In percent at end of period)

| | Onshore | | | | 2004 | |
|---|---|---|---|---|---|---|
| | 2000 | 2001 | 2002 | 2003 | Onshore | Offshore |
| Statutory capital to (unadjusted) risk-weighted assets | 13.9 | 14.1 | 14.9 | 15.6 | 14.5 | 12.2 |
| Nonperforming loans to total loans | 9.6 | 8.1 | 7.9 | 6.5 | 5.8 | 3.3 |
| Provisions to nonperforming loans | 24.3 | 25.8 | 36.2 | 39.1 | 43.6 | 34.8 |
| Return on assets | 1.1 | 1.1 | 0.8 | 1.1 | 1.4 | 1.6 |
| Return on equity | 12.0 | 11.6 | 8.5 | 12.2 | 15.3 | 16.8 |
| Net open position in foreign exchange to regulatory capital | 11.5 | 37.8 | 36.3 | 44.6 | 33.1 | … |

Source: Superintendency of Banks.

12. **Dollarization of the banking system has increased**. Since 2001 when residents were first permitted to hold foreign currency deposits in domestic banks, the share of such deposits has risen to 15 percent, reflecting mainly the rapid growth in worker remittances.[4] Credit in foreign currency, however, has grown more slowly.

## Implementation of Fund policy advice

13. **The overall stance of macroeconomic policy and financial sector reforms have been broadly in line with Fund advice in recent years, although there was less progress on tax reform**.

- ***The pursuit of prudent macroeconomic policies reflects a broad consensus in Guatemala on the importance of sound fiscal and monetary polices and financial stability***. Conversely, the lack of progress after 2002 toward the tax objectives of the Peace Accords is the result of strong opposition from powerful interest groups and the perception that higher revenues would mainly lead to wasteful spending.

- ***While many of the objectives of the 2003 Stand-By Arrangement (SBA) were achieved, the midterm review was not completed***. The program was broadly successful in maintaining macroeconomic stability and advancing some structural reforms in 2003, an election year. However, slippages occurred, particularly toward the end of the year: the ceilings on the fiscal deficit and short-term external debt were

[4] The ratio is 36 percent including deposits in the offshore banks.

exceeded, and structural performance criteria on exempting the purchase of bank assets from VAT and conducting due diligence on the state mortgage bank (CHN) were not observed. Hence, the precautionary arrangement expired in March 2004 without completion of the midterm review.

- ***The authorities have made efforts at garnering support for additional revenue measures to achieve the goals of the Peace Accords***, although progress has been slower than expected. They continue to work on implementing the tax plan, as discussed below, and expressed interest in continuing the close policy dialogue with the staff during this process.

- ***Guatemala has received a considerable amount of technical assistance from the Fund in recent years*** (Appendix I). The record of implementation has been good on banking reforms, mixed on revenue mobilization (for lack of political support), and constrained by institutional bottlenecks in the area of statistics.

## C. Near-Term Outlook

14. **The economic recovery is expected to strengthen somewhat in 2005, although there are downside risks**. A favorable external environment, improvements in the business climate, and early ratification of CAFTA-DR will support the recovery.[5] The downside risks include the impact of continued high oil prices, a further real appreciation of the quetzal, and insufficient political support for the government's agenda, particularly on revenue mobilization and key structural reforms. Real GDP is projected to grow by 3.2 percent in 2005, with the external current account deficit remaining broadly unchanged. International reserves accumulation would slow to the extent the central bank intervenes in the foreign exchange market only to dampen exchange rate volatility, as capital inflows, including public sector borrowing, are expected to moderate.

[5] CAFTA-DR is the free trade agreement between Central America-Dominican Republic and the United States.

Key Macroeconomic Indicators

(In percent of GDP, unless otherwise indicated)

| | | | Est. | Proj. | |
|---|---|---|---|---|---|
| | 2002 | 2003 | 2004 | 2005 | 2006 |
| Real GDP growth (in percent) | 2.2 | 2.1 | 2.7 | 3.2 | 3.2 |
| Real GDP per capita growth (in percent) | -0.4 | -0.5 | 0.1 | 0.6 | 0.6 |
| Inflation (end of period, in percent) | 6.3 | 5.9 | 9.2 | 6.0 | 5.0 |
| External current account deficit | 5.3 | 4.2 | 4.4 | 4.4 | 4.2 |
| Combined public sector deficit | 0.8 | 2.0 | 0.4 | 1.7 | 1.2 |
| Tax revenue | 10.6 | 10.3 | 10.3 | 10.5 | 11.0 |
| NIR (US$ millions) | 2,278 | 2,799 | 3,380 | 3,655 | 3,722 |
| Nonfinancial public sector debt | 15.5 | 17.1 | 18.0 | 17.8 | 17.8 |

## II. Policy Discussions

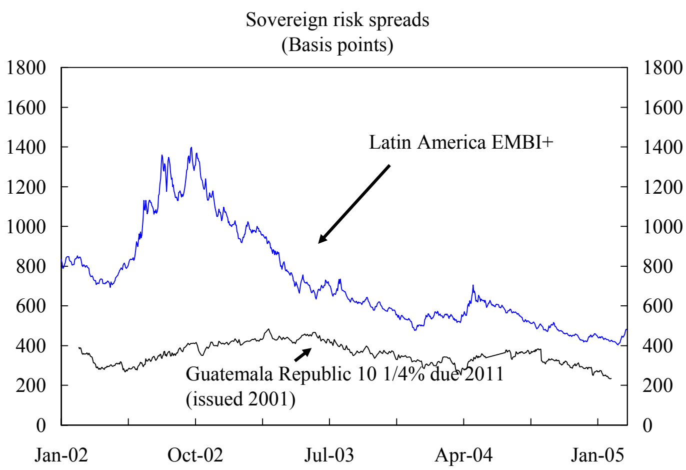
15. **The discussions focused on the near-term macro framework and economic vulnerabilities, and on reforms to promote growth, competitiveness, and social progress**. The authorities and staff agreed that raising growth, reducing poverty, and maintaining macroeconomic stability are the primary objectives of the policy framework. Against this background, the discussions focused on growth-enhancing reforms; efforts to raise revenue, reduce inflation, and advance financial sector reforms; and steps to improve transparency and governance. The key elements of the policy framework are summarized in Table 11.

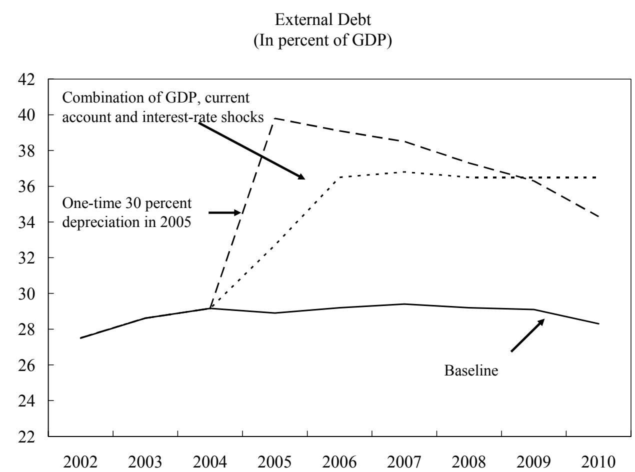
16. **Overall, staff considered that the government's economic strategy is well suited to achieve its policy objectives, but recommended a somewhat faster pace of implementation**. The strong macroeconomic framework, trade opening, and improvements in the business climate should help boost productivity, investment, and growth. The staff noted that moving the reform agenda more rapidly than currently envisaged would hold out prospects for a stronger recovery and earlier achievement of key social and economic goals. In particular, the staff recommended that the authorities proceed quickly with actions to mobilize additional fiscal resources, reduce inflation, and address the remaining financial sector vulnerabilities.

17. **The authorities shared the staff's assessment and recognized the potential benefits of advancing the timetables for their reforms**. They noted, however, that the pace of implementation was constrained by the need to build support for key elements of their agenda, a task made more difficult by the fragmented political landscape and the lingering distrust in the integrity of some public institutions.

### A. Medium-Term Outlook and Vulnerabilities

18. **The medium-term outlook is favorable under strong policies, although with downside risks**. Under a "baseline" scenario prepared by the staff based on the government's program, real GDP growth could rise to 3.5–4 percent. The external current account would strengthen somewhat as a result of rising nontraditional exports, continued—albeit somewhat slower—growth in remittances, and appropriately tight demand management policies. Reliance on debt-creating capital inflows would be reduced as FDI rises in response to improvements in the investment climate and the ratification of CAFTA-DR. The public debt would decline to 15 percent of GDP by 2010, from 18 percent in 2004, while total external debt (public and private) would remain stable at around 28 percent of GDP. All indicators of external vulnerability would remain sound.




19. **Guatemala's external and public debt outlook is quite robust to alternative assumptions for the underlying macroeconomic variables**. Specifically, using 10-year historical averages for the key assumptions does not significantly alter the medium-term projection. Additional temporary negative shocks to key variables, such as interest rates, the exchange rate, and GDP growth, would lead to some increase in the level of public and external debt, but the ratios return to a declining path once conditions normalize.

20. **Nonetheless, vulnerabilities remain under the baseline scenario**. The most serious risk derives from political obstacles or legal actions that could delay or thwart implementation of key fiscal and structural reforms and further delay achievement of the Peace Accord objectives. The government faces significant obstacles to implementing its program because of a highly fragmented political environment that reflects limited credibility of some state institutions, related mainly to a history of weak management of public resources, and deep distributional inequities that permeate much of the political discourse. The congressional coalition supporting the government is fragile, and a number of pressure groups with disparate agendas wield significant influence. Other sources of vulnerability include:

- ***Terms of trade and dependence on the U.S. market***. Although export diversification has helped reduce trade-related vulnerabilities, one-third of Guatemala's exports remain commodity-based. Moreover, the United States absorbs 30 percent of non-*maquila* exports, making them sensitive to changes in the U.S. market.

- ***Productivity and real appreciation of the quetzal***. Rising worker remittances and capital inflows have contributed to a steady real appreciation of the quetzal in recent years. Recognizing this challenge, the authorities emphasized that their policies have been framed with a view to raising productivity and strengthening competitiveness.

- ***Banking system***. Notwithstanding the significant reforms, stress tests suggest that the main risks to the nonperforming loan ratio (currently below 6 percent) come from sharp reductions in economic activity and major increases in interest rates.[6]

21. **To illustrate some key risks, the staff prepared a weaker policy scenario where tax revenue is not raised, inflation remains at current levels, and the momentum on financial reform stalls**. With tax collections remaining at around 10 percent of GDP, budgetary expenditure would be reduced by about 1 percent of GDP relative to the baseline, constraining social programs, while the fiscal deficit would rise by ½ percent of GDP. Under such a scenario, the public debt would remain at 18 percent of GDP in 2010 instead of declining; the ratio of public debt to tax revenue would still be the lowest in Central America; and Guatemala's protection against vulnerabilities would remain relatively strong. However, higher inflation, stagnant revenue and social spending, and a halt to financial sector reforms could affect the investment climate and market sentiment, and raise the cost of borrowing. Real GDP growth would be lower and could negate the rise in per capita income in prospect under the baseline scenario. There would also be a heightened risk of financial sector problems, potentially leading to a more serious setback to growth.

## B. Fiscal Policy

22. **The government's fiscal strategy aims to raise revenue toward the target of the Peace Accords, maintain a low budget deficit, and improve the quality of public spending**. Following the sharp compression of expenditure and the deficit in 2004, as explained in paragraph 25, spending is set to recover in 2005 and 2006, temporarily widening the deficit before it narrows again as the authorities continue to implement their tax plan.

23. **Staff expressed broad support for this strategy, stressing the key challenge of raising tax revenue to the 12 percent of GDP target of the Peace Accords, now long**

[6] Stress tests for the banking system are simulation exercises that consist in subjecting the system to low-probability and extremely stressful macroeconomic shocks. They are used to distinguish between different sources of risk and to device strategies to attenuate their effects.

**overdue**.[7] To achieve this, staff recommended that a VAT increase be a central part of an additional revenue effort and that the tax administration plan be underpinned with legislative support, as needed. The authorities underscored their commitment to achieving the target, but noted that resistance to a stronger tax effort remains considerable, and that more time would likely be needed to mobilize sufficient domestic support. They expect tax collections to increase to 10½ percent of GDP in 2005 and 11 percent in 2006, for a total effort of more than 2 percent of GDP during 2004–06.[8] [9] The government's tax plan includes three elements:

- A tax package approved in June 2004 that (i) reintroduced excises on alcoholic beverages (revoked in 2003); (ii) introduced a turnover tax as an option under the corporate income tax regime; (iii) established a presumptive minimum corporate income tax (IETAAP) with a lower rate and different structure than the one revoked in 2003; and (iv) provided for a small minimum corporate tax that will take effect after the IETAAP is phased out by 2007.

- A comprehensive plan launched last year to strengthen tax administration, following FAD recommendations (Appendix II).

- A second set of fiscal measures to be put in place in 2005 and to take effect in 2006, with the measures still to be specified.

24. **The authorities underscored their commitment to tax administration reform and a revenue package in 2005**. They would introduce a package of efficient measures, calibrated to take account of progress in collecting additional revenue under the tax administration plan, so as to raise collections to at least 11 percent of GDP in 2006. The staff noted that last year's tax package had contained distortionary elements (such as an optional corporate turnover tax), and urged the authorities to introduce a set of efficient measures this year, and also take the opportunity to remove existing tax distortions and make the system more buoyant. The government's strategy to mobilize support for a new revenue package and full implementation of the tax administration plan rests on engaging broad segments of society in a public dialogue and education campaign to build consensus on national priorities,

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[7] The 1996 Peace Accords called for raising the tax/GDP ratio to 12 percent (originally to be achieved in 2000) to fund much needed increases in social spending, restructure the security forces and the judicial system, compensate the victims of the conflict, and finance a land purchase program.

[8] Tax collections were set to fall to less than 9 percent of GDP following the tax reductions ordered by the court in 2003. The congress has not yet approved a proposal to reinstate the excise tax on fuel, requiring the government to extend a temporary tax on fuel imports.

[9] An additional effort of about ½ percent of GDP will likely be needed to offset the mandated phasing out of the minimum corporate income tax (IETAAP) by 2007, the effect of inflation on specific excise taxes, the estimated first-year revenue loss under CAFTA-DR, and the implementation of WTO valuation procedures.

including the Millennium Development Goals, and their funding. The campaign was announced in February 2005, and a series of round-table discussions on health, education, and security are being implemented. The authorities are also taking a leading role in efforts to improve coordination of tax administration and tax policy at the regional level.[10] Moreover, they expect that the track record being established on fighting corruption and raising the quality of public spending will help allay long-standing concerns in the private sector about misuse of public funds, and thereby build support for the stronger tax effort.[11]

25. **Raising public investment and social spending are key priorities under the government's program**. The authorities explained that while spending was reduced last year because of the prospective tax loss and the legal issues that delayed the investment program, priority was nevertheless given to peace-related programs: the army was reduced by one-third (12,000 personnel) at a severance cost of 0.4 percent of GDP, and compensation payments were made to auxiliary soldiers for service during the civil conflict.[12] With rising revenue, falling military outlays, and a moderately higher budget deficit, social spending and public investment would rise significantly in 2005 and 2006, allowing further progress towards the Peace Accords objectives and the Millennium Development Goals.

26. **Keeping the public debt low and improving its structure remain key objectives**. The maturity structure of external and domestic debt was extended in 2004, and the authorities intend to increase the borrowing from multilateral institutions in 2005 (Appendices III and IV). In the past, the government had accumulated debt to domestic suppliers (0.4 percent of GDP at end-2003) and to exporters as a result of delayed VAT refunds (0.5 percent of GDP at end-2003). The former was reduced by half in 2004, and the stock of overdue VAT refunds has also been lowered and is expected to be eliminated by the middle of 2006.

### C. Monetary and Exchange Rate Policies

27. **The monetary framework was strained in 2004 by the weakening of the U.S. dollar, strong inflows of private capital and remittances, and the cost-push from higher oil prices.** The authorities pointed to the increases in central bank interest rates over the past

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[10] Better coordination of taxes and fiscal incentives is seen as important as the region steps up its efforts to attract foreign direct investment in the context of CAFTA-DR. In March 2005, Guatemala hosted a regional conference on tax harmonization, supported by FAD, and the topic is on the agenda of the summit meetings of the Central American presidents.

[11] An FAD mission in January 2005 provided technical assistance on public expenditure management and prepared the fiscal ROSC for Guatemala. Key recommendations of the mission were to address poor budget coverage, execution, and control; unreported contingent liabilities; the risk of unreported arrears; and inadequate controls on sub-national public debt.

[12] The compensation payments were disbursed to a trust fund pending resolution of a constitutional challenge to these payments.

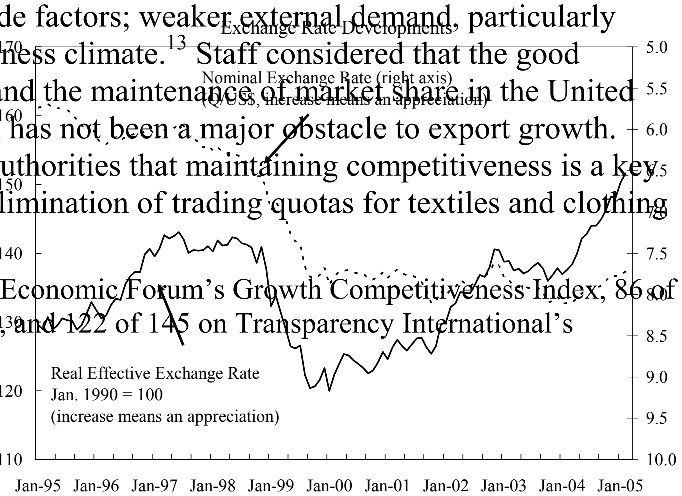
year in their effort to contain any second-round effects from the oil price shock, and explained that aggressive interest rate hikes to stem inflation would have risked encouraging additional capital inflows and further appreciation of the quetzal. In this situation, they chose a policy mix of moderate monetary tightening, tight fiscal policy, and central bank intervention in the foreign exchange market to prevent excessive appreciation of the quetzal, without pursuing an exchange rate target, noting that the interventions had been justified by developments that were perceived to be temporary, such as the global pressures against the U.S. dollar. They explained that the intervention rule introduced earlier this year was mainly a tool for avoiding short-term volatility, and while the rule only refers to purchases of foreign exchange, the central bank intends to pursue a broadly symmetrical intervention policy, also dampening excessive depreciation, as needed. The authorities underscored that the central bank had gained considerable credibility in recent years for its success in reducing inflation, and that the lengthening of the yield curve for public debt last year pointed to improved confidence.

28. **The staff recommended that the central bank focus on the goal of maintaining low inflation.** It welcomed the increases in interest rates implemented last year, but noted that monetary conditions had nevertheless remained relatively lax, with currency emission (the intermediate target) exceeding the limit set by the bank. The staff considered that bringing inflation back to within the target range will require greater exchange rate flexibility and adherence to a path for currency emission consistent with that objective. It noted that the new foreign market intervention rule reduced discretion, but needed to be made symmetrical, i.e., responding to both appreciation and depreciation pressures, and implemented consistently and in a transparent manner. The staff encouraged the central bank to continue its work, with the support of MFD, toward adopting an inflation targeting framework. The authorities agreed with the staff about the appropriateness of moving toward such a framework, and noted that inflationary pressures had abated in recent months, supporting achievement of the end-year target for inflation of 4–6 percent.

## D. Growth and Competitiveness

29. **Real appreciation of the quetzal, driven recently by a surge in worker remittances and strong private capital inflows, has contributed to a widening trade deficit and slow export growth since the end of the 1990s**. Exports and economic growth have also been constrained by supply-side factors; weaker external demand, particularly falling coffee prices; and a difficult business climate.[13] Staff considered that the good performance of nontraditional exports, and the maintenance of market share in the United States, suggest that the real appreciation has not been a major obstacle to export growth. Nevertheless, the staff agreed with the authorities that maintaining competitiveness is a key challenge, accentuated recently by the elimination of trading quotas for textiles and clothing

[13] Guatemala ranks 80 of 104 on the World Economic Forum's Growth Competitiveness Index, 86 of 103 on the Business Competitiveness Index, and 122 of 145 on Transparency International's Corruption Perceptions Index.



(Box 3). There was also broad agreement that the challenge of competitiveness could not be met on a sustained basis by targeting the exchange rate—hence the need for a strong and comprehensive effort to strengthen the underlying determinants of competitiveness, notably by actions to raise productivity, lessen infrastructure bottlenecks, and implement appropriately tight fiscal policies. In this regard, the authorities noted that their program has been framed to (i) strengthen the traded goods sector; (ii) foster a business climate characterized by transparency, the rule of law, and good governance; and (iii) promote social progress.

**Box 3. Elimination of Textile and Clothing Quotas**

**Guatemala, like other Central American exporters of textiles and clothing, risk losing a sizeable part of their exports to the United States** following the January 1, 2005 elimination of quotas under the Agreement on Textiles and Clothing. Net exports of textiles and clothing account for 6.1 percent of Guatemala's current account receipts, and the sector accounts for 2.6 percent of employment.

**Rapid growth in Central America's textile and clothing exports in the 1990s** reflected country-specific import quotas, mainly in the United States, and outsourcing of labor-intensive stages of production to other countries, such as Guatemala. Under the quota arrangement, many Central American countries benefited from foreign direct investment, often by Asian firms, designed to benefit from unused quotas in the region. Typically, Central American exporters import cloth produced and cut in the United States, sew and warehouse the finished products, and export them to U.S. retailers based upon daily sales data, replenishing retailer inventory weekly.

**Staff simulations for the Spring 2005 WEO indicate that the elimination of quotas could reduce Central American and Caribbean exports of these products by nearly half, the largest potential decline by any region**. The projected decline in exports would be equivalent, for Guatemala, to a reduction in current account receipts of 2.9 percent and a reduction in employment of 1.2 percent. Preliminary data for the first quarter of 2005, released on an expedited basis, show that U.S. imports of textiles and apparel from China increased by 65 percent and from India by 29 percent. The growth rates of Chinese exports of knit shirts and blouses, cotton trousers, and underwear to the United States were particularly high, at 1250, 1550, and 300 percent, respectively. However, preliminary U.S. import data for the first quarter of 2005 indicate that Guatemala did not lose market share.

**It should be noted that these estimates represent a worst-case scenario, ignoring a number of moderating factors that are difficult to quantify:** (1) the CAFTA-DR will ensure continued preferential access to the U.S. market and will relax rules of origin to permit some use of non-U.S. inputs; (2) transportation costs and delivery times for Central American countries are less than half of those for Asian suppliers; (3) having anticipated the lifting of quotas, some exporters have sought market niches and have moved up the supply (and value-added) chain; and (4) the United States has initiated safeguards proceedings under China's WTO accession protocol in the three product categories mentioned above, which could limit textile and clothing imports from China (but would not affect other countries); certain other products are already subject to safeguards.

30. **To boost exports and help reduce the trade deficit, the government is pursuing a three-pronged strategy to strengthen the competitive position of the traded goods sector**:

- First, ***a robust macroeconomic framework*** has been adopted, with prudent fiscal and monetary policies to support and complement productivity-enhancing reforms aimed at strengthening the overall competitive position of the economy.

- Second, ***trade liberalization*** is being pursued through the free-trade agreement with the United States (CAFTA-DR) and efforts to complete a customs union in Central America.[14] In addition, Guatemala—as a member of the Central American Common Market—is working toward trade agreements with the European Union and other Latin American trade blocks. A commitment to liberalize trade at the multilateral level in the context of the Doha Round remains an integral part of the government's trade policy.
- Third, ***export and investment procedures*** are being simplified, and a Commissioner for Competitiveness has been appointed. Barriers to trade, such as delays in rebating VAT to exporters and cumbersome customs procedures, are being addressed. Also, as investment incentives linked to exports are due to be eliminated by 2009 under the WTO framework, the authorities plan to promote export diversification and growth through "third-generation" incentives, including measures to support technological innovation, enhance labor skills, and improve market intelligence.

31. **Policies to foster a better business climate and strengthen public institutions are high on the government's agenda**.

- ***Promoting fiscal transparency***. To make public sector operations more transparent, the government has drafted a fiscal transparency law (with assistance from the Fund) that will be introduced in congress in 2005. Revisions to the organic budget law have also been prepared.

- ***Improving expenditure control***. The Integrated Financial Management System (SIAF) is being extended, and will cover nearly 100 additional municipalities and decentralized agencies by the end of 2005. The on-line procurement system, *GuateCompras*, is also being expanded.

- ***Strengthening the legal system***. In September 2004 the Supreme Court submitted to congress a set of initiatives aimed at modernizing the legal system, and reforms are being introduced to reduce delays in the judicial process.

- ***Strengthening state institutions***. A plan is being implemented to improve efficiency and eliminate duplication of responsibilities through external management audits of all ministries. Two key components of this effort are: (i) new civil service legislation and (ii) strict enforcement of regulations for government procurement and contracting.

- ***Combating corruption***. The government reaffirmed its commitment to fighting corruption. A high-profile campaign against corruption is underway: a number of former high-level officials are being prosecuted, stricter penalties are being introduced, and a code of ethics for the civil service has been promulgated.

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[14] Guatemala ratified the CAFTA-DR agreement in March 2005.

- ***Reviewing pension obligations***. In 2005 the authorities will initiate a comprehensive financial evaluation of the Social Security Institute (IGSS) and the government's other pension obligations. Although there is no indication of a near-term cash problem, the authorities indicated that the review is important in order to ascertain the longer-term viability of these obligations, an issue that has been brought into focus by a recent court ruling that suspended an earlier decision to raise the retirement age gradually from 60 to 65 years.

32. **Social programs are being expanded and made more efficient**. The government has restructured the budget to improve the targeting of expenditure on priority elements of its multiyear program for growth, competitiveness, and social progress, *Vamos Guatemala*. The program's social component, *GuateSolidaria*, is designed to foster participatory socio-economic development by focusing on education, health, housing, security, and justice, with emphasis on projects to build productive capacity in the poorest municipalities. The plan provides for partnerships with the private sector, particularly in the area of education, and the authorities are enlisting support from the multilateral development agencies in the form of expertise and financing.

## E. Financial Sector Reforms

33. **Significant reforms have been introduced in the financial sector, but challenges remain**. Notably, provisions are low in offshore banks; four small private banks and the state mortgage bank (CHN) remain weak; the level of related-party lending is high; and illegal offshore banks have been operating in Guatemala (action to deal with them is under way). The authorities indicated that they are fully committed to addressing these challenges, noting also that a well-coordinated regional approach would be helpful, as cross-border lending and financial integration is advancing rapidly. They therefore support efforts to improve cooperation and convergence of banking regulations and prudential norms in Central America.

34. **The main areas of ongoing financial sector reforms are as follows:**

- ***Bringing offshore banks into the regulatory framework***. Registration of financial conglomerates (including offshore banks)—a necessary legal step for them to operate as conglomerates—began in July 2004 and will be completed by mid-2006.

- ***The bank resolution framework***. The new framework will be completed and made operational. The Trust Fund for Bank Capitalization was funded at the end of 2004, and the authorities are seeking to implement the central bank's lender-of-last resort facility in 2005.

- ***Bank consolidation***. To facilitate consolidation in the banking industry, legislation will be introduced in 2005 to exempt the sale of bank assets from the VAT.

- ***The public mortgage bank***. A plan has been drawn up to address the persistent losses of the public mortgage bank (CHN). The fiscal costs, which will be estimated as part of a forthcoming due-diligence process, will be incorporated into future budgets.

- ***Related lending and general provisions***. The Bank Superintendency will continue to supervise closely institutions with high levels of lending to related parties (*Préstamos vinculados*). The authorities will review the need to tighten the statutory limits on such lending this year, and will also consider requiring general provisions to further improve the soundness of banks.

- ***Central bank recapitalization***. The bank will be recapitalized, compensating for losses incurred mainly through its open market operations. Beginning in 2005, the government will assume, year-by-year, the losses incurred after 2002, and it will seek approval for the issuance of a long-term zero-coupon bond to cover the stock of past losses.

- ***The payments system*** is being modernized. A Matrix for Modernization of the Payments System will be implemented in 2005, which calls for the introduction of real-time gross settlements and upgrading the clearing house for bank settlements.

### F. Statistics

35. **The authorities are intensifying their efforts to upgrade Guatemala's economic statistics** (see Appendix V). Although the quality of data is broadly adequate for surveillance purposes, weaknesses in the national accounts and balance of payments data constrain the policy analysis. In October 2004, a ROSC mission from STA found significant shortcomings in macroeconomic statistics. To improve the balance of payments statistics, the central bank is in the process of designing a new reporting system, and work is underway to adopt the 1993 system of national accounts and bring the base-year from 1958 to 2001. Guatemala joined the General Data Dissemination Standard at the end of 2004.

## III. Staff Appraisal

36. **Guatemala's economic performance in recent years has been mixed.** Macroeconomic stability has been maintained, with economic vulnerabilities well contained, but growth has been sluggish and poverty remains widespread. On the positive side, the public debt is low, the overall external position has been strengthened, and the financial system has been made more robust. At the same time, weak domestic consensus and legal ambiguities have undermined efforts to increase taxes and fulfill the aspirations raised by the Peace Accords. Indeed, social expenditure has declined, and Guatemala's social indicators are low.

37. **Against this backdrop, the government that took office in early 2004 has included the Peace Accords in the platform for its policy agenda**. The staff welcomes this renewed commitment to the Accords and the goals for economic and social progress they

enshrine. The government has laid out a well-focused and ambitious policy agenda, although it still needs to secure broad political support for some key elements.

38. **The government has put appropriate focus, right from the start, on the challenge of curbing corruption and restoring trust in the integrity of public institutions**. The staff welcomes this approach, which has already been successful in promoting transparency and fighting corruption. The government has also been efficient in targeting scarce resources under the *Vamos Guatemala* plan, and innovative in seeking to build partnerships with the private sector. These and other early steps have gained the government credibility and good will that should be leveraged into broader support for its economic policy agenda.

39. **The government's economic program rests on three pillars: structural reforms to spur growth and reduce poverty; macroeconomic stability anchored on prudent fiscal and monetary policies; and financial sector restructuring.** The authorities consider well-targeted social programs to be a prerequisite for strong economic growth over the longer term. The staff shares this view, and also welcomes the programs designed to encourage private investment and strengthen the competitive position of the traded goods sector. To be successful, these programs must be appropriately funded, underscoring the need for a strong revenue effort. Supported by strong fiscal policies, these structural reform programs should help contain the impact on competitiveness of the growing flow of remittances, which is expected to continue.

40. **A sustained improvement in the tax effort is critical to Guatemala's development prospects.** The staff regrets the decline in the tax/GDP ratio after 2002, with the threat of a further major decline in 2004 leading to a sharp compression of spending until the new government's tax strategy was in place. Unfortunately, last year's tax package, an integral part of the strategy, was reduced by congress, and its yield will decline over time. This has left the government to rely on the tax administration plan while mobilizing support for additional revenue measures. Although the plan is generating more revenue than expected, a comprehensive and sustained reform of tax administration requires legislative action, and thus congressional support.

41. **The staff welcomes the authorities' commitment to introducing additional measures in 2005 to help achieve the revenue goal of the Peace Accords**. To marshal support for this effort, which should be centered on high-quality tax measures and provide for the elimination of existing distortions, the government has initiated a public dialogue and education campaign designed to build consensus on national priorities and their funding. The government is also taking a lead in efforts to enhance cooperation on tax issues at the regional level, and is building a track record of more efficient public resource management that should help broaden domestic support for a stronger revenue effort.

42. **The central bank is encouraged to focus on achieving low inflation**. Relatively lax monetary conditions contributed to the rise in inflation last year, and staff recommends that conditions be kept appropriately tight to ensure achievement of the target for 2005. A flexible exchange rate regime remains appropriate for Guatemala and staff urges the authorities to allow the exchange rate of the quetzal to be determined by the market and limit

interventions to what is needed to avoid excessive short-term volatility. Finally, staff supports ongoing work toward adopting inflation targeting as the framework for monetary policy, which will further strengthen the credibility of the central bank and help keep inflation low.

43. **The staff commends the authorities for the progress on financial sector reform**. Bringing the offshore banks into the regulatory framework is a significant accomplishment. At the same time, it is important to address remaining vulnerabilities, notably by reducing lending to related parties, building general provisions, and dealing with the persistent losses of the state mortgage bank (CHN).

44. **The staff encourages the authorities to continue their work to strengthen Guatemala's macroeconomic statistics**. In particular, the plan for updating the national accounts should be implemented, information on external flows strengthened, and the reporting of data by the non-budgetary fiscal sector upgraded. Staff recommends that the authorities give priority to these issues, which will require additional resources and close inter-agency collaboration.

45. **The medium-term economic outlook is favorable under strong policies, although it is not without risks.** The prospects for exports and growth depend crucially on productivity-enhancing structural reforms, continued prudent fiscal policy, and trade promotion. Remaining weaknesses in the banking sector, while not a systemic risk, also need to be addressed. Nevertheless, Guatemala has considerable room for maneuver to deal with shocks. The combination of low public debt, a strengthened banking system, a flexible exchange rate regime, and adequate international reserves would make for a fairly resilient policy framework. At the same time, it is important that the government muster sufficient domestic consensus to carry its ambitious economic program forward.

46. **Staff proposes that Guatemala remain on a 12-month consultation cycle**.

Table 1. Guatemala: Selected Economic and Social Indicators

I. Social and Demographic Indicators

| | | | |
|---|---|---|---|
| Population 2001 (millions) | 11.9 | Gini index (1998) | 55.8 |
| Percentage of indigeneous population (2001) | 55.0 | Life expectancy at birth (2001) | 65.7 |
| Percentage of population below the poverty line (2000) | 56.2 | Adult illiteracy rate (2001) | 30.1 |
| Rank in UNDP development index (2004) | 121 of 177 | GDP per capita (US$, 2003) | 2,079 |

II. Economic Indicators 2000-2006

| | | | | 2003 | | Prel. | Proj. | |
|---|---|---|---|---|---|---|---|---|
| | 2000 | 2001 | 2002 | Prog. | Actual | 2004 | 2005 | 2006 |
| (Annual percentage change, unless otherwise indicated) | | | | | | | | |
| **Income and prices** | | | | | | | | |
| Real GDP | 3.6 | 2.3 | 2.2 | 2.4 | 2.1 | 2.7 | 3.2 | 3.2 |
| Consumer prices (end of period) | 5.1 | 8.9 | 6.3 | 4 - 6 | 5.9 | 9.2 | 6.0 | 5.0 |
| **Monetary sector** | | | | | | | | |
| Credit to private sector | 9.6 | 12.5 | 6.1 | 9.3 | 7.3 | 16.2 | 11.2 | 10.5 |
| Liabilities to private sector | 22.3 | 8.1 | 13.2 | 12.4 | 11.0 | 11.4 | 14.1 | 10.7 |
| Interest rate (annual, domestic-currency time deposits) | 15.3 | 11.3 | 9.6 | … | 6.7 | 6.9 | ... | ... |
| **External sector** | | | | | | | | |
| Exports | 10.9 | -7.3 | -1.4 | 5.7 | 8.6 | 12.1 | 10.9 | 2.7 |
| Imports | 13.4 | 8.4 | 12.4 | 7.2 | 6.6 | 16.2 | 9.2 | 2.7 |
| Terms of trade | 1.7 | -1.0 | -2.5 | … | -4.4 | 1.0 | -0.5 | -0.3 |
| Real effective exchange rate 1/ | 1.9 | 3.2 | 8.3 | … | -1.9 | 7.5 | ... | ... |
| (In percent of GDP, unless otherwise indicated) | | | | | | | | |
| **Current account** | **-5.4** | **-6.0** | **-5.3** | **-5.5** | **-4.2** | **-4.4** | **-4.4** | **-4.2** |
| Trade balance | -10.8 | -13.1 | -15.0 | -15.0 | -14.8 | -16.3 | -16.2 | -15.7 |
| Exports | 16.0 | 13.6 | 12.1 | 11.1 | 12.4 | 12.8 | 13.0 | 12.7 |
| Imports | -26.8 | -26.6 | -27.0 | -26.0 | -27.2 | -29.1 | -29.2 | -28.4 |
| Other (net) | 5.4 | 7.1 | 9.7 | 9.5 | 10.6 | 11.9 | 11.8 | 11.5 |
| **Capital account** | **9.2** | **8.3** | **5.2** | **6.5** | **6.3** | **6.6** | **5.4** | **4.4** |
| Public sector (including official capital transfers) | 1.2 | 1.4 | 0.8 | 2.9 | 1.8 | 1.5 | 1.1 | 1.2 |
| Private sector | 8.0 | 6.9 | 4.4 | 3.6 | 4.6 | 5.1 | 4.3 | 3.2 |
| **Net international reserves (in millions of U.S. dollars) (incr** | **-728** | **-499** | **23** | **-250** | **-521** | **-581** | **-275** | **-68** |
| (Stock in months of next year imports of goods and services) | 3.6 | 4.0 | 3.7 | 3.8 | 4.0 | 4.4 | 4.6 | 4.5 |
| **Gross domestic investment** | **17.8** | **17.1** | **19.8** | **17.4** | **19.4** | **19.4** | **19.7** | **19.9** |
| Public sector | 4.2 | 4.3 | 3.4 | 3.4 | 4.1 | 3.4 | 3.8 | 4.0 |
| Private sector | 13.7 | 12.8 | 16.3 | 14.0 | 15.4 | 16.0 | 15.9 | 16.0 |
| **Gross national saving** | **12.4** | **11.1** | **14.5** | **11.9** | **15.2** | **15.0** | **15.3** | **15.7** |
| Public sector | 2.0 | 2.0 | 2.6 | 2.4 | 2.0 | 3.0 | 2.1 | 2.7 |
| Private sector | 10.4 | 9.2 | 11.8 | 9.5 | 13.2 | 12.0 | 13.2 | 13.0 |
| **Combined public sector balance (including central bank losses)** | **-2.2** | **-2.3** | **-0.8** | **-1.7** | **-2.0** | **-0.4** | **-1.7** | **-1.2** |
| Overall balance of the nonfinancial public sector (deficit -) | -1.8 | -1.5 | -0.3 | -1.1 | -1.5 | 0.1 | -1.2 | -0.8 |
| **Nonfinancial public debt (in percent of GDP)** | **16.7** | **17.1** | **15.5** | **...** | **17.1** | **18.0** | **17.8** | **17.8** |
| *Of which:* external | 14.7 | 14.5 | 13.4 | ... | 13.9 | 14.0 | 13.5 | 13.5 |
| **Financing** | **2.2** | **2.3** | **0.8** | **1.7** | **2.0** | **0.4** | **1.7** | **1.2** |
| External financing | 0.8 | 1.1 | 0.1 | 2.3 | 0.8 | 1.0 | 0.4 | 0.3 |
| Domestic financing | 0.7 | -0.6 | 0.7 | -0.6 | 1.2 | -0.6 | 1.3 | 0.9 |
| Privatization/other financing | 0.7 | 1.8 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Memorandum items:** | | | | | | | | |
| Tax revenue in percent of GDP | 9.4 | 9.7 | 10.6 | 10.7 | 10.3 | 10.3 | 10.5 | 11.0 |
| Central government social spending | 5.0 | 5.5 | 5.1 | 5.3 | 5.3 | 5.0 | 5.8 | 6.0 |
| Net oil imports (US$ millions) | 573.3 | 653.6 | 599.4 | … | 731.1 | 909.1 | 1,174.9 | 1,155.3 |

Sources: Bank of Guatemala; Ministry of Finance; and Fund staff estimates and projections.

1/ End-period; a positive change indicates an appreciation.

Table 2. Guatemala: Summary Accounts of the Bank of Guatemala

| | 2001 | 2002 | 2003 Prog. | 2003 Actual | Prel. 2004 | Proj. 2005 | Proj. 2006 |
|---|---|---|---|---|---|---|---|
| Exchange rate (quetzales/U.S. dollars) | 7.9 | 7.6 | 8.0 | 8.0 | 7.7 | ... | ... |
| (Stocks in millions of quetzales) | | | | | | | |
| **Net international reserves** | **18,286** | **17,395** | **20,222** | **22,459** | **26,149** | **29,353** | **30,776** |
| (In millions of U.S. dollars) | 2,301 | 2,278 | 2,528 | 2,799 | 3,380 | 3,655 | 3,723 |
| **Net domestic assets** | **-8,810** | **-7,395** | **-9,346** | **-10,535** | **-13,522** | **-15,760** | **-16,023** |
| Net claims on nonfinancial public sector | -10,156 | -7,307 | -10,030 | -9,453 | -12,112 | -10,905 | -10,905 |
| Central government | -6,328 | -4,902 | -7,384 | -5,885 | -8,214 | -6,762 | -6,762 |
| Rest of nonfinancial public sector | -3,828 | -2,404 | -2,645 | -3,568 | -3,897 | -4,142 | -4,142 |
| Bank of Guatemala losses | 11,013 | 12,028 | 13,135 | 13,000 | 14,187 | 15,275 | 16,308 |
| Net credit to banks | -3,716 | -5,888 | -4,807 | -5,047 | -6,680 | -7,316 | -8,102 |
| *Of which:* reserve | -5,957 | -8,041 | -6,911 | -7,136 | -8,764 | -9,400 | -10,186 |
| Open market operations 1/ | -7,451 | -8,623 | -9,658 | -10,810 | -11,244 | -14,366 | -15,141 |
| Medium- and long- term foreign liabilities | -631 | -525 | -462 | -455 | 0 | 0 | 0 |
| Other assets (net) | 2,130 | 2,919 | 2,476 | 2,230 | 2,326 | 1,552 | 1,816 |
| **Currency issue** | **9,476** | **10,000** | **10,876** | **11,924** | **12,626** | **13,593** | **14,753** |
| (Flows in millions of quetzales) | | | | | | | |
| **Net international reserves** | **3,895** | **-802** | **2,827** | **5,064** | **3,690** | **3,204** | **1,423** |
| (In millions of U.S. dollars) | 438 | -23 | 250 | 521 | 581 | 275 | 68 |
| **Net domestic assets** | **-2,634** | **1,415** | **-1,951** | **-3,139** | **-2,988** | **-2,237** | **-263** |
| Net claims on nonfinancial public sector | -3,584 | 2,849 | -2,723 | -2,146 | -2,659 | 1,207 | 0 |
| Central government | -2,703 | 1,426 | -2,482 | -982 | -2,330 | 1,452 | 0 |
| Rest of nonfinancial public sector | -881 | 1,424 | -241 | -1,164 | -329 | -245 | 0 |
| Bank of Guatemala losses | 1,260 | 1,016 | 1,107 | 972 | 1,186 | 1,088 | 1,033 |
| Net credit to banks | 488 | -2,172 | 1,080 | 841 | -1,633 | -636 | -786 |
| *Of which:* reserve | -953 | -2,084 | 1,130 | 906 | -1,629 | -636 | -786 |
| Open market operations 1/ | -1,361 | -1,171 | -1,035 | -2,187 | -434 | -3,122 | -774 |
| Medium- and long- term foreign liabilities | 75 | 106 | 63 | 70 | 455 | 0 | 0 |
| Other assets (net) | 490 | 789 | -443 | -689 | 96 | -775 | 264 |
| **Currency issue** | **1,262** | **524** | **876** | **1,925** | **702** | **967** | **1,160** |
| (12-month percentage change over the stock of currency issued at the beginning of the period) | | | | | | | |
| **Net domestic assets** | **-32.1** | **14.9** | **-19.5** | **-31.4** | **-25.1** | **-17.7** | **-1.9** |
| Net claims on nonfinancial public sector liabilities | -43.6 | 30.1 | -27.2 | -21.5 | -22.3 | 9.6 | 0.0 |
| Bank of Guatemala losses | 15.3 | 10.7 | 11.1 | 9.7 | 9.9 | 8.6 | 7.6 |
| **Currency issue** | **15.4** | **5.5** | **8.8** | **19.2** | **5.9** | **7.7** | **8.5** |
| **Memorandum item:** | | | | | | | |
| Outstanding open market bills (millions of quetzales) 2/ | 11,015 | 11,159 | 12,206 | 14,509 | 15,906 | 18,339 | 19,113 |

Sources: Bank of Guatemala; and Fund staff estimates.

1/ Includes open market placements with the private sector (financial and nonfinancial).
2/ Open market placements with the private and public sectors.

Table 3. Guatemala: Summary Accounts of Commercial Banks

| | | | | Prel. | Proj. | |
|---|---|---|---|---|---|---|
| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
| Exchange rate (quetzales/U.S. dollar) | 7.9 | 7.6 | 8.0 | 7.7 | ... | ... |
| (Stocks in millions of quetzales ) | | | | | | |
| **Net foreign position** | **-3,853** | **-3,559** | **-3,564** | **-4,277** | **-4,847** | **-5,186** |
| **Net claims on Bank of Guatemala** | **10,556** | **13,224** | **15,106** | **17,441** | **20,806** | **22,269** |
| Legal reserves | 5,968 | 8,041 | 7,136 | 8,764 | 9,400 | 10,186 |
| BOG securities | 6,498 | 6,777 | 9,325 | 9,829 | 12,558 | 13,235 |
| Liabilities to BOG | -2,196 | -2,102 | -2,081 | -2,077 | -2,077 | -2,077 |
| Other | 286 | 508 | 726 | 925 | 925 | 925 |
| **Net domestic assets** | **32,926** | **34,524** | **37,585** | **42,464** | **47,924** | **53,851** |
| Net credit to the NFPS | 918 | 26 | 902 | 1,019 | 994 | 1,290 |
| Net credit to central government | 3,198 | 2,935 | 3,187 | 3,863 | 4,052 | 4,224 |
| Net credit to the rest of NFPS | -2,280 | -2,910 | -2,284 | -2,844 | -3,058 | -2,934 |
| Official capital and reserves | -195 | -238 | -313 | -503 | -503 | -503 |
| Credit to the private sector | 32,864 | 34,860 | 37,389 | 43,448 | 48,323 | 53,400 |
| Other investments | 4,251 | 4,508 | 4,655 | 4,740 | 5,272 | 5,826 |
| Unclassified assets (net) | -4,912 | -4,632 | -5,048 | -6,241 | -6,163 | -6,163 |
| **Medium- and long-term foreign liabilities** | **86** | **66** | **46** | **78** | **78** | **78** |
| **Liabilities to private sector** | **39,543** | **44,123** | **49,081** | **55,550** | **63,805** | **70,855** |
| Demand deposits | 12,305 | 14,554 | 17,580 | 19,765 | 22,826 | 25,402 |
| Time and savings deposits | 20,657 | 23,038 | 25,766 | 29,772 | 34,383 | 38,263 |
| Securities | 3,942 | 3,691 | 2,733 | 2,513 | 2,757 | 3,005 |
| Capital and reserves (private banks) | 2,640 | 2,840 | 3,002 | 3,500 | 3,839 | 4,185 |
| (Flows in millions of quetzales) | | | | | | |
| **Net foreign position** | **298** | **294** | **-5** | **-713** | **-570** | **-340** |
| **Net claims on Bank of Guatemala** | **2,340** | **2,668** | **1,882** | **2,335** | **3,365** | **1,463** |
| Legal reserves | 867 | 2,073 | -906 | 1,629 | 636 | 786 |
| BOG securities | 2,651 | 279 | 2,548 | 504 | 2,729 | 677 |
| Liabilities to BOG | -1,441 | 94 | 21 | 4 | 0 | 0 |
| Other | 263 | 222 | 219 | 199 | 0 | 0 |
| **Net domestic assets** | **1,277** | **1,598** | **3,061** | **4,879** | **5,460** | **5,927** |
| Net credit to the NFPS | 461 | -892 | 876 | 117 | -25 | 296 |
| Net credit to central government | 1,496 | -263 | 251 | 676 | 189 | 172 |
| Net credit to the rest of NFPS | -1,035 | -629 | 625 | -559 | -214 | 123 |
| Official capital and reserves | 63 | -43 | -76 | -189 | 0 | 0 |
| Credit to the private sector | 3,649 | 1,996 | 2,529 | 6,059 | 4,875 | 5,077 |
| Other investment | 266 | 257 | 147 | 86 | 532 | 554 |
| Unclassified assets (net) | -3,163 | 279 | -415 | -1,194 | 78 | 0 |
| **Medium- and long-term foreign liabilities** | **-119** | **-20** | **-20** | **32** | **0** | **0** |
| **Liabilities to private sector** | **4,034** | **4,580** | **4,958** | **6,469** | **8,255** | **7,050** |
| Demand deposits | 1,905 | 2,250 | 3,026 | 2,185 | 3,061 | 2,576 |
| Time and savings deposits | 4,020 | 2,382 | 2,728 | 4,006 | 4,611 | 3,880 |
| Securities | -389 | -251 | -958 | -219 | 244 | 248 |
| Capital and reserves (private banks) | -1,502 | 200 | 162 | 498 | 339 | 346 |

Sources: Bank of Guatemala; and Fund staff estimates and projections.

Table 4. Guatemala: Monetary Survey

| | | | 2003 | | Prel. | Proj. | |
|---|---|---|---|---|---|---|---|
| | 2001 | 2002 | Prog. | Actual | 2004 | 2005 | 2006 |
| Exchange rate (quetzales/U.S. dollars) | 7.9 | 7.6 | 8.0 | 8.0 | 7.7 | ... | ... |
| | | | (Stocks in millions of quetzales) | | | | |
| **Net foreign assets** | **14,433** | **13,836** | **17,013** | **18,895** | **21,872** | **24,506** | **25,590** |
| (In millions of U.S. dollars) | 1,816 | 1,812 | 2,127 | 2,355 | 2,827 | 3,051 | 3,095 |
| **Net domestic assets** | **34,955** | **41,867** | **45,469** | **42,755** | **46,343** | **53,347** | **60,571** |
| Net claims on nonfinancial public sector | -9,238 | -7,281 | -10,668 | -8,550 | -11,092 | -9,910 | -9,615 |
| Central government | -3,130 | -1,967 | -4,554 | -2,698 | -4,351 | -2,710 | -2,538 |
| *Of which* : deposits | -7,741 | -6,658 | -8,318 | -7,405 | -11,035 | -9,583 | -9,583 |
| Rest of nonfinancial public sector | -6,108 | -5,314 | -6,114 | -5,852 | -6,741 | -7,200 | -7,077 |
| Bank of Guatemala losses | 11,013 | 12,028 | 13,135 | 13,000 | 14,187 | 15,275 | 16,308 |
| Credit to private sector | 32,871 | 34,867 | 38,433 | 37,397 | 43,455 | 48,331 | 53,408 |
| Other investments | 4,251 | 4,508 | 4,601 | 4,655 | 4,740 | 5,272 | 5,826 |
| Other assets (net) | -3,942 | -2,256 | -32 | -3,746 | -4,947 | -5,621 | -5,356 |
| **Medium- and long-term foreign liabilities** | **717** | **591** | **528** | **502** | **78** | **78** | **78** |
| **Liabilities to the private sector** | **48,671** | **55,112** | **61,954** | **61,149** | **68,137** | **77,775** | **86,083** |
| Money | 20,532 | 23,284 | 26,394 | 28,189 | 30,960 | 34,988 | 38,724 |
| Quasi-money | 28,139 | 31,828 | 35,560 | 32,959 | 37,177 | 42,787 | 51,094 |
| | | | (Flows in millions of quetzales) | | | | |
| **Net foreign assets** | **4,193** | **-597** | **3,177** | **5,059** | **2,977** | **2,634** | **1,084** |
| (In millions of U.S. dollars) | 490 | -5 | 315 | 543 | 472 | 224 | 44 |
| **Net domestic assets** | **-727** | **6,913** | **3,602** | **888** | **3,588** | **7,004** | **7,224** |
| Net claims on nonfinancial public sector | -3,123 | 1,957 | -3,387 | -1,270 | -2,542 | 1,182 | 296 |
| Central government | -1,207 | 1,163 | -2,587 | -731 | -1,653 | 1,641 | 172 |
| *Of which:* deposits | -2,796 | 1,084 | -1,660 | -748 | -3,630 | 1,452 | 0 |
| Rest of nonfinancial public sector | -1,916 | 794 | -800 | -539 | -889 | -459 | 123 |
| Bank of Guatemala losses | 1,260 | 1,016 | 1,107 | 972 | 1,186 | 1,088 | 1,033 |
| Credit to private sector | 3,649 | 1,996 | 3,566 | 2,529 | 6,059 | 4,875 | 5,077 |
| Other assets (net) | -2,779 | 1,687 | 2,224 | -1,491 | -1,201 | -674 | 264 |
| **Medium- and long-term foreign liabilities** | **-194** | **-126** | **-63** | **-90** | **-423** | **0** | **0** |
| **Liabilities to the private sector** | **3,660** | **6,441** | **6,842** | **6,037** | **6,989** | **9,638** | **8,307** |
| Money | 2,834 | 2,752 | 3,110 | 4,905 | 2,771 | 4,028 | 3,736 |
| Quasi-money | 827 | 3,689 | 3,732 | 1,131 | 4,218 | 5,610 | 8,307 |
| | | | (12-month percentage change over initial stock of liabilities to the private sector) | | | | |
| **Net domestic assets** | **-1.6** | **14.2** | **6.5** | **1.6** | **5.9** | **10.3** | **9.3** |
| Net claims on nonfinancial public sector | -6.9 | 4.0 | -6.1 | -2.3 | -4.2 | 1.7 | 0.4 |
| Credit to private sector | 8.1 | 4.1 | 6.5 | 4.6 | 9.9 | 7.2 | 6.5 |
| **Liabilities to the private sector** | **8.1** | **13.2** | **12.4** | **11.0** | **11.4** | **14.1** | **10.7** |
| Money | 6.3 | 5.7 | 5.6 | 8.9 | 4.5 | 5.9 | 4.8 |
| Quasi-money | 1.8 | 7.6 | 6.8 | 2.1 | 6.9 | 8.2 | 10.7 |
| **Memorandum items:** | | | | | | | |
| | | | (12-month percentage change) | | | | |
| Credit to private sector | 12.5 | 6.1 | 10.2 | 7.3 | 16.2 | 11.2 | 10.5 |
| | | | (In millions of quetzales) | | | | |
| Private financial savings (M3+ nonbank public T-bills) 1/ | 48,961 | 58,121 | ... | 66,439 | 73,909 | 84,271 | 81,898 |

Sources: Bank of Guatemala; and Fund staff estimates.

1/ M3 includes M2 plus securities of the banking system held by the nonbank private sector. Nonbank public T-bills are government securities held by the nonbank private sector.

Table 5. Guatemala: Summary Balance of Payments

(In millions of U.S. dollars)

| | 2001 | 2002 | 2003 | Prel. 2004 | Proj. 2005 | Proj. 2006 |
|---|---|---|---|---|---|---|
| **Current account** | **-1,253** | **-1,234** | **-1,050** | **-1,188** | **-1,294** | **-1,297** |
| Trade balance | -2,747 | -3,485 | -3,661 | -4,382 | -4,727 | -4,851 |
| Exports, f.o.b. | 2,860 | 2,819 | 3,060 | 3,430 | 3,805 | 3,908 |
| Traditional | 950 | 958 | 971 | 1,004 | 1,164 | 1,170 |
| Nontraditional | 1,910 | 1,861 | 2,089 | 2,426 | 2,641 | 2,738 |
| Imports, c.i.f. 1/ | -5,606 | -6,304 | -6,722 | -7,812 | -8,532 | -8,759 |
| *Of which:* oil and lubricants | -754 | -755 | -908 | -1,089 | -1,398 | -1,368 |
| Services | 497 | 275 | 150 | 188 | 197 | 177 |
| Factor services (net) | -84 | -318 | -329 | -319 | -374 | -411 |
| *Of which:* gross interest on public debt | -185 | -185 | -180 | -195 | -236 | -248 |
| Nonfactor (net) | 581 | 592 | 479 | 507 | 571 | 588 |
| Current transfers (net) | 997 | 1,976 | 2,462 | 3,006 | 3,236 | 3,377 |
| **Capital account** | **1,752** | **1,211** | **1,570** | **1,769** | **1,569** | **1,365** |
| Official transfers | 93 | 124 | 134 | 135 | 141 | 150 |
| Public sector | 209 | 54 | 309 | 259 | 180 | 216 |
| Disbursements | 183 | 328 | 178 | 289 | 430 | 479 |
| Amortization | -149 | -167 | -186 | -279 | -222 | -233 |
| Bonds (net) | 175 | -108 | 267 | 248 | -29 | -30 |
| Private sector | 1,450 | 1,033 | 1,128 | 1,375 | 1,248 | 999 |
| FDI 2/ | 456 | 110 | 131 | 155 | 193 | 247 |
| Medium and long-term debt flows | 214 | 274 | 267 | 284 | 355 | 336 |
| Short-term debt flows | 44 | 70 | 42 | 109 | 72 | 23 |
| Portfolio flows and errors and omissions 3/ | 737 | 579 | 688 | 827 | 628 | 394 |
| **Overall balance** | **499** | **-23** | **521** | **581** | **275** | **68** |
| (Annual percentage growth) | | | | | | |
| **Value** | | | | | | |
| Exports, f.o.b. | -7.3 | -1.4 | 8.6 | 12.1 | 10.9 | 2.7 |
| Imports, c.i.f. | 8.4 | 12.4 | 6.6 | 16.2 | 9.2 | 2.7 |
| (In percent of GDP) | | | | | | |
| **Current account** | **-6.0** | **-5.3** | **-4.2** | **-4.4** | **-4.4** | **-4.2** |
| Trade balance | -13.1 | -15.0 | -14.8 | -16.3 | -16.2 | -15.7 |
| Exports, f.o.b. | 13.6 | 12.1 | 12.4 | 12.8 | 13.0 | 12.7 |
| Imports, c.i.f. | -26.6 | -27.0 | -27.2 | -29.1 | -29.2 | -28.4 |
| Services | 2.4 | 1.2 | 0.6 | 0.7 | 0.7 | 0.6 |
| *Of which:* interest on public debt | -0.9 | -0.8 | -0.7 | -0.7 | -0.8 | -0.8 |
| Current transfers (net) | 4.7 | 8.5 | 10.0 | 11.2 | 11.1 | 10.9 |
| *Of which:* remittances | 2.8 | 6.5 | 8.2 | 9.4 | 9.4 | 9.3 |
| **Capital account** | **8.3** | **5.2** | **6.3** | **6.6** | **5.4** | **4.4** |
| Official transfers | 0.4 | 0.5 | 0.5 | 0.5 | 0.5 | 0.5 |
| Public sector | 1.0 | 0.2 | 1.2 | 1.0 | 0.6 | 0.7 |
| Private sector | 6.9 | 4.4 | 4.6 | 5.1 | 4.3 | 3.2 |
| FDI 2/ | 2.2 | 0.5 | 0.5 | 0.6 | 0.7 | 0.8 |
| Medium and long-term debt flows | 1.0 | 1.2 | 1.1 | 1.1 | 1.2 | 1.1 |
| Short-term debt flows | 0.2 | 0.3 | 0.2 | 0.4 | 0.2 | 0.1 |
| Portfolio flows and errors and omissions 3/ | 3.5 | 2.5 | 2.8 | 3.1 | 2.2 | 1.3 |
| **Overall balance** | **2.4** | **-0.1** | **2.1** | **2.2** | **0.9** | **0.2** |
| **Memorandum items:** | | | | | | |
| Net international reserves (in months of next year imports of goods and services) 4/ | 4.0 | 3.7 | 4.0 | 4.4 | 4.6 | 4.5 |
| Stock of NIR (in millions of U.S. dollars) | 2,301 | 2,278 | 2,799 | 3,380 | 3,655 | 3,722 |
| Export deflator (percentage change) 5/ | -5.6 | -1.6 | 6.9 | 17.3 | 5.7 | -2.2 |
| Import deflator (percentage change) 5/ | -3.4 | 1.8 | 11.1 | 13.0 | 5.6 | -1.1 |

Sources: Central Bank of Guatemala; Ministry of Finance; and Fund staff estimates and projections.

1/ Variations in 2000 and 2001 partly reflect changes in import registration system implemented in July 2000 and upgraded in June 2001.

2/ Includes privatization-related flows equivalent to 0.8 percent in 2000 and 1.7 percent in 2001.

3/ May include unreported FDI flows.

4/ Excludes claims on Nicaragua amounting to US$75.7 million in 2000 official data.

5/ For goods only.

Table 6. Guatemala: Operations of the Combined Public Sector

(In percent of GDP)

| | | | | 2003 | | Prel. | Proj. | |
|---|---|---|---|---|---|---|---|---|
| | 2000 | 2001 | 2002 | Prog. | Actual | 2004 | 2005 | 2006 |
| **I. Central Government Operations** | | | | | | | | |
| **Total revenue 1/** | **10.4** | **11.1** | **11.6** | **11.5** | **11.3** | **11.0** | **11.2** | **11.6** |
| Tax revenue | 9.4 | 9.7 | 10.6 | 10.7 | 10.3 | 10.3 | 10.5 | 11.0 |
| Direct taxes | 2.5 | 2.5 | 3.0 | 2.9 | 2.9 | 2.7 | 2.7 | 2.8 |
| Indirect taxes | 6.9 | 7.1 | 7.6 | 7.8 | 7.4 | 7.5 | 7.8 | 8.2 |
| Nontax revenue and transfers | 0.9 | 1.4 | 1.0 | 0.8 | 0.9 | 0.7 | 0.6 | 0.6 |
| **Total expenditures 1/ 2/** | **12.4** | **13.3** | **12.2** | **13.1** | **13.4** | **11.4** | **13.0** | **13.1** |
| Current expenditures | 8.6 | 9.2 | 8.6 | 9.2 | 9.3 | 8.2 | 8.8 | 8.8 |
| Wages and salaries | 3.5 | 3.6 | 3.5 | 3.4 | 3.5 | 3.2 | 3.2 | 3.2 |
| Goods and services | 1.3 | 1.5 | 1.2 | 1.3 | 1.3 | 1.0 | 1.4 | 1.3 |
| Interest | 1.2 | 1.4 | 1.2 | 1.3 | 1.2 | 1.2 | 1.5 | 1.7 |
| Transfers | 2.6 | 2.7 | 2.6 | 3.2 | 3.4 | 2.8 | 2.7 | 2.7 |
| Capital expenditure | 3.7 | 4.1 | 3.6 | 3.9 | 4.1 | 3.2 | 4.2 | 4.3 |
| *Of which* | | | | | | | | |
| Fixed capital formation | 1.5 | 1.6 | 0.9 | 1.0 | 1.0 | 0.8 | 1.3 | 1.5 |
| Military demobilization | 0.0 | 0.0 | 0.0 | 0.2 | 0.1 | 0.2 | 0.0 | 0.0 |
| Net lending | 0.0 | 0.2 | 0.3 | 0.1 | 0.0 | 0.1 | 0.2 | 0.2 |
| **Current account balance (deficit -)** | **1.6** | **1.5** | **2.7** | **2.1** | **1.7** | **2.7** | **2.3** | **2.7** |
| **Overall balance (deficit -)** 3/ | **-2.4** | **-2.4** | **-0.3** | **-1.6** | **-2.3** | **-0.4** | **-1.8** | **-1.5** |
| **Financing** | **2.4** | **2.4** | **0.3** | **1.6** | **2.3** | **0.4** | **1.8** | **1.5** |
| External (net) | 0.9 | 1.3 | 0.2 | 2.4 | 0.9 | 1.1 | 0.5 | 0.3 |
| Domestic (net) | 1.5 | 1.1 | 0.1 | -0.8 | 1.3 | -0.7 | 1.4 | 1.2 |
| **II. Combined Public Sector Operations** | | | | | | | | |
| **Combined public sector balance** | **-2.2** | **-2.3** | **-0.8** | **-1.7** | **-2.0** | **-0.4** | **-1.7** | **-1.2** |
| Nonfinancial public sector | -1.8 | -1.5 | -0.3 | -1.1 | -1.5 | 0.1 | -1.2 | -0.8 |
| Central government | -2.4 | -2.4 | -0.3 | -1.6 | -2.3 | -0.4 | -1.8 | -1.5 |
| Rest of the nonfinancial public sector | 0.6 | 0.9 | 0.1 | 0.4 | 0.8 | 0.6 | 0.6 | 0.7 |
| Bank of Guatemala | -0.4 | -0.8 | -0.6 | -0.6 | -0.5 | -0.6 | -0.5 | -0.4 |
| **Combined public sector financing** | **2.2** | **2.3** | **0.8** | **1.7** | **2.0** | **0.4** | **1.7** | **1.2** |
| External (net) | 0.8 | 1.1 | 0.1 | 2.3 | 0.8 | 1.0 | 0.4 | 0.3 |
| Foreign loans (net) | 0.4 | 0.1 | 0.6 | 0.0 | -0.3 | 0.1 | 0.5 | 0.1 |
| Bonded debt | 0.4 | 0.9 | -0.5 | 2.3 | 1.1 | 0.9 | -0.1 | 0.2 |
| Domestic (net) | 0.7 | -0.6 | 0.7 | -0.6 | 1.2 | -0.6 | 1.3 | 0.9 |
| Banking system | 1.0 | -1.0 | 1.4 | -0.6 | -0.1 | -1.5 | 0.9 | 0.4 |
| Bonded debt | -0.5 | 0.0 | -0.3 | 0.1 | 1.2 | 1.1 | 0.6 | ... |
| Change in floating debt | 0.2 | 0.4 | -0.4 | -0.1 | 0.2 | -0.2 | -0.2 | ... |
| Privatization | 0.7 | 1.8 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | ... |
| **Memorandum items:** | | | | | | | | |
| Central government social spending 1/ | 5.0 | 5.5 | 5.1 | 5.3 | 5.3 | 5.0 | 5.8 | 6.0 |

Sources: Ministry of Finance; Bank of Guatemala; and Fund staff estimates and projections.

1/ In 2005, projected revenue and expenditure (including social expenditure) exceed the approved 2005 budget.

2/ In 2004, expenditure excludes three items amounting to 0.6 percent of GDP which are included in official figures: (1) capitalization of the Fund for the Protection of Depositors has been excluded; (2) reduction of arrears has been classified below the line; and (3) payments intended for ex-members of the Civilian Auxiliary Patrols (ex-PACs), which remain in a trust fund account classified under central government deposits in the Bank of Guatemala balance sheet, have been excluded.

3/ Includes statistical discrepancy.

Table 7. Guatemala: Financial Soundness Indicators: Core and Encouraged Sets 1/

(In percent)

| | | End-December | | | | |
|---|---|---|---|---|---|---|
| | | 2000 | 2001 | 2002 | 2003 | 2004 |
| **Core Set** | | | | | | |
| Deposit-taking institutions (banks) | | | | | | |
| Capital adequacy | Statutory capital to risk-weighted assets | 13.9 | 14.1 | 14.9 | 15.6 | 14.5 |
| Asset quality | Nonperforming loans to total gross loans | 9.6 | 8.1 | 7.9 | 6.5 | 5.8 |
| | Nonperforming loans net of provisions to capital | 41.3 | 34.2 | 26.7 | 20.5 | 22.5 |
| | Sectoral distribution of loans to total loans | | | | | |
| | Consumption | ... | 36.0 | 41.0 | 41.1 | 45.0 |
| | Agriculture | ... | 9.1 | 7.8 | 8.9 | 8.0 |
| | Mining | ... | 0.0 | 0.2 | 0.0 | 0.0 |
| | Industry | ... | 10.1 | 10.9 | 11.2 | 10.1 |
| | Electricity, gas, and water | ... | 1.4 | 1.3 | 1.5 | 2.6 |
| | Construction | ... | 7.4 | 6.4 | 6.2 | 7.2 |
| | Commerce | ... | 27.8 | 25.6 | 23.4 | 21.0 |
| | Transport and warehousing | ... | 1.7 | 0.7 | 0.7 | 0.7 |
| | Financial and real estate services | ... | 3.7 | 3.6 | 3.9 | 3.2 |
| | Community services, personal, and others | ... | 2.7 | 2.6 | 3.1 | 2.2 |
| | Total | ... | 100.0 | 100.0 | 100.0 | 100.0 |
| | Large exposures to capital | ... | ... | ... | 69.4 | 65.4 |
| Earnings and profitability | Return on assets | 1.1 | 1.1 | 0.8 | 1.1 | 1.4 |
| | Return on equity | 12.0 | 11.6 | 8.5 | 12.2 | 15.3 |
| | Interest margin to gross income | 35.0 | 32.0 | 35.4 | 34.6 | 37.7 |
| | Noninterest expenses to gross income | 53.2 | 55.3 | 60.7 | 64.2 | 63.9 |
| Liquidity | Liquid assets to total assets (liquid asset ratio) | 25.7 | 29.9 | 31.3 | 28.0 | 29.1 |
| | Liquid assets to short-term liabilities | 29.1 | 33.6 | 35.2 | 31.6 | 32.9 |
| Sensitivity to market risk | Net open position in foreign exchange to regulatory capital | 11.5 | 37.8 | 36.3 | 44.6 | 33.1 |
| **Encouraged Set** | | | | | | |
| Deposit-taking institutions (banks) | Capital to assets | 8.5 | 8.3 | 8.9 | 9.0 | 8.9 |
| | Geographical distribution of loans to total loans | | | | | |
| | Guatemala | ... | 83.0 | 85.0 | 84.0 | 80.3 |
| | El Progreso | ... | 6.1 | 6.6 | 4.0 | 1.5 |
| | Escuintla | ... | 1.3 | 1.2 | 1.8 | 2.5 |
| | Izabal | ... | 1.0 | 0.9 | 1.3 | 1.0 |
| | Alta Verapaz | ... | 1.2 | 0.8 | 0.7 | 1.0 |
| | Quetzaltenango | ... | 0.8 | 0.6 | 0.5 | 0.9 |
| | Huehuetenango | ... | 1.0 | 0.5 | 0.5 | 9.0 |
| | Sacatepequez | ... | 0.4 | 0.4 | 0.3 | 0.5 |
| | Other | ... | 5.2 | 3.8 | 6.5 | 11.4 |
| | Trading income to total income | 74.9 | 69.4 | 68.7 | 60.0 | 63.5 |
| | Personnel expenses to noninterest expenses | 37.9 | 36.3 | 35.9 | 24.9 | 26.7 |
| | Spread between reference lending and deposit rates 2/ | ... | ... | ... | 9.6 | 8.9 |
| | Spread between highest and lowest interbank rate | ... | ... | ... | ... | ... |
| | Customer deposits to total (non-interbank) loans | 1.4 | 1.4 | 1.5 | 1.3 | 1.3 |
| | Foreign currency-denominated loans to total loans (percent) | 18.4 | 21.1 | 24.1 | 27.7 | 28.3 |
| | Foreign currency-denominated liabilities to total liabilities (percent) | 11.3 | 14.1 | 15.9 | 19.6 | 21.0 |

Source: Superintendency of Banks.

1/ Indicators for the onshore banking system only.
2/ Based on central bank repo operations.

Table 8. Guatemala: Summary of the Structure and Performance of the Financial Sector 1/

| | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|---|---|
| Number of banks 2/ | 34 | 34 | 32 | 31 | 31 | 29 | 28 |
| Majority state-owned (in percent of total assets) | 6.5 | 8.8 | 8.5 | 3.4 | 2.5 | 3.3 | 3.3 |
| Majority foreign-owned (in percent of total assets) | 0.3 | 0.5 | 0.6 | 0.5 | 0.4 | 0.4 | 0.5 |
| Foreign branches (as a percent of total assets) | 2.9 | 3.0 | 3.5 | 4.0 | 3.7 | 2.8 | 1.6 |
| Number of banks accounting for at least | | | | | | | |
| 25 percent of total assets | 3 | 3 | 3 | 1 | 1 | 1 | 1 |
| 75 percent of total assets | 15 | 14 | 14 | 9 | 9 | 9 | 8 |
| Total assets of banks (in percent of nominal GDP) | 29.1 | 29.0 | 33.9 | 35.2 | 38.5 | 34.6 | 35.6 |
| Credit to private sector (in percent of nominal GDP) | 21.3 | 22.3 | 22.2 | 22.5 | 20.2 | 17.4 | 18.7 |
| Contingent and off-balance sheet accounts | | | | | | | |
| (in percent of total assets) | 16.6 | 13.2 | 15.1 | 11.8 | 10.8 | 11.3 | 13.8 |
| *Of which* | | | | | | | |
| Foreign currency denominated ) | | | | | | | |
| (in percent of total assets | 4.5 | 2.9 | 2.7 | 2.3 | 3.2 | 3.4 | 5.3 |
| Average pretax return on total assets (in percent) | 1.0 | 1.4 | 1.1 | 1.0 | 0.9 | 1.3 | 2.4 |
| Average financial spread 3/ | 10.8 | 9.3 | 9.1 | 9.1 | 9.1 | 9.6 | 8.9 |
| Interest rate spread in interbank market (in percent) | 6.6 | 10.1 | 10.1 | 10.1 | 8.3 | 6.3 | 6.3 |
| Foreign currency sovereign debt rating 4/ | | | | | | | |
| Moody's | Ba2 | Ba2 | Ba2 | Ba2 | Ba2 | Ba2 | Ba2 |
| S&P | ... | ... | ... | BB | BB | BB- | BB- |

Sources: Superintendency of Banks; Bank of Guatemala; and Fund staff estimates.

1/ The Guatemalan financial system consists of the central bank, one majority state-owned bank, 27 commercial banks, including two branches of foreign banks and one majority foreign-owned bank, and 18 nonbank financial intermediaries. In addition, there are credit unions, leasing, and factoring companies, and credit card companies.

2/ Includes 3 domestic private banks in the process of liquidation.

3/ Spread between lending and deposit interest rates calculated from the income statement and the balance sheet data of commercial banks.

4/ Moody's rated Guatemala for the first time in July 1997 for long-term currency bonds placed in the Euromarket.

Table 9. Guatemala: Quantitative Performance Criteria under the 2003 Stand-By Arrangement

| | Jun. | Sep. | Dec. |
|---|---|---|---|
| (In millions of quetzales) | | | |
| **Deficit of the combined public sector** 1/ | | | |
| Program ceiling | 1,630 | 2,730 | 3,347 |
| Actual | 959 | 2,014 | 3,970 |
| Adjusted ceiling | 1,630 | 2,189 | 2,147 |
| Margin (+), shortfall (-) | 672 | 175 | -1,823 |
| **Central government expenditure** 1/ | | | |
| Program ceiling | 12,110 | 18,710 | 25,679 |
| Actual | 11,632 | 18,448 | 26,334 |
| Adjusted ceiling | 12,110 | 18,110 | 24,479 |
| Margin (+), shortfall (-) | 478 | -338 | -1,855 |
| **Central government social expenditure (indicative target)** | | | |
| Program floor | 5,440 | 8,150 | 10,425 |
| Actual | 4,871 | 7,722 | 10,502 |
| Adjusted floor | 5,440 | 8,150 | 10,502 |
| Margin (+), shortfall (-) | -569 | -428 | 77 |
| **Net domestic assets of the central bank** 1/ | | | |
| Program ceiling | -12,670 | -12,180 | -9,346 |
| Actual | -9,844 | -12,889 | -10,469 |
| Adjusted ceiling | -9,467 | -10,298 | -7,460 |
| Margin (+), shortfall (-) | 377 | 2,591 | 3,009 |
| (In millions of U.S. dollars) | | | |
| **Net international reserves of the central bank** 1/ | | | |
| Program floor | 2,730 | 2,640 | 2,528 |
| Actual | 2,452 | 2,867 | 2,799 |
| Adjusted floor | 2,330 | 2,405 | 2,293 |
| Margin (+), shortfall (-) | 122 | 462 | 271 |
| **Contracting of nonconcessional external debt** | | | |
| Maturity: less than one year | | | |
| Program ceiling (outstanding stock) | 9 | 11 | 15 |
| Actual | 31 | 28 | 28 |
| Margin (+), shortfall (-) | -22 | -17 | -13 |
| Maturity: more than one year | | | |
| Program ceiling (cumulative flow) | 705 | 1,095 | 1,344 |
| Actual | 10 | 310 | 310 |
| Margin (+), shortfall (-) | 696 | 786 | 1,035 |

Sources: Bank of Guatemala, Ministry of Finance; and Fund staff estimates.

1/ The November 2003 mission agreed ad referendum to waive the applicability of some of the end-December adjustors.

Table 10. Structural Performance Criteria and Benchmarks Under the 2003 Stand-By Arrangement

| | Program | Final Status |
|---|---|---|
| **I. Structural Performance Criteria** | | |
| No use of CHN to assist or absorb private banks | Continuous | Observed |
| Secure congressional approval of a law exempting transfers of bank assets from VAT | By midterm review | Not approved |
| Non accumulation of external payments arrears | Continuous | Observed |
| **II. Structural Benchmarks** | | |
| Submission to congress of draft law on combating the financing of terrorism | By midterm review | Done |
| Submission to congress of draft law on fiscal transparency | By midterm review | Not done |
| Approval by the Monetary Board of payment system reform | During 2003 | Done |
| Complete onsite inspection of offshore banks | By midterm review | Completed |
| Conduct viability analysis of CHN | By midterm review | Not done |
| Adopt corrective actions on onshore banks as the result of on-site inspections | Ongoing | Ongoing |
| Strengthen the framework for resolution of problem banks | By midterm review | Ongoing |

Table 11. Guatemala: Key Elements of the Authorities' Policy Framework

| Reforms | Sector | Responsible Power | Status | Comment |
|---|---|---|---|---|
| **I. Immediate Measures (Next 6 Months)** | | | | |
| Strengthening of tax administration (SAT) 1/ | Fiscal (revenue) | Executive | Ongoing | Program to strengthen tax administration (including recommendations from FAD) already yielding additional revenue. |
| Revenue package in 2005 | Fiscal (revenue) | Executive/Congress | Pending | The government is pursuing a strategy to mobilize support for measures. Potential for adverse court rulings. |
| Strengthen expenditure control | Fiscal (expenditure) | Executive | Ongoing | In addition to measures already being put in place by the authorities, a January ROSC mission also provided TA. |
| Implement a strategic plan for CHN | Financial | Executive/Congress | Pending | A plan has been developed and is being initiated in 2005. |
| Complete bank resolution framework; register financial conglomerates; bring offshore banks into the regulatory framework | Financial | Superintendency of Banks/Monetary Board | Ongoing | Mostly done; the authorities have substantial ownership of the financial sector reform program. |
| Cover the 2003 central bank losses in the 2005 budget | Monetary/Fiscal | Executive/Congress | Ongoing | Approved with the 2005 budget; the government is expected to issue bond in second or third quarter of 2005. |
| Initiate comprehensive review and evaluation of pension funds | Fiscal (expenditure) | Executive | Pending | Financial assessment expected to be initiated in mid-2005. |
| **II. Near-Term Measures (Next 1-2 Years)** | | | | |
| Increase social spending | Fiscal (expenditure) | Executive/Congress | Pending | A sustained increase would require additional resources. |
| Revise the Organic Budget law and enact a fiscal transparency law | Fiscal (expenditure) | Executive/Congress | Pending | The government places a high priority on improving the transparency of government operations. The transparency law is ready for presentation to congress. |
| Reduce the excessive amount of related party lending by banks | Financial | Superintendency of Banks/Monetary Board | Pending | To be considered by the Monetary Board. |
| Require general provisions of banks | Financial | Superintendency of Banks/Monetary Board | Pending | To be considered by the Monetary Board. |
| Implement program to control corruption | Governance | Executive | Ongoing | The government is pursuing an assertive and high profile campaign against corruption. New ethics code issued for civil service and sanctions tightened. |
| Improve the quality and coverage of BOP, national accounts, and fiscal statistics | Statistics | Executive | Initiated | The authorities have begun to deal with long standing problems with the quality of statistics. |
| Further expand the integrated budgetary control system (SIAF) to include the Social Security Institute and 100 municipalities | Fiscal (expenditure) | Executive | Pending | Transparency is a government priority. |

1/ See Appendix II for details.

Table 12. Guatemala: Medium-Term Projections

| | 1999 | 2000 | 2001 | 2002 | 2003 | Prel. 2004 | Projected 2005 | 2006 | 2007 | 2008 | 2009 | 2010 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | | (In percent ) | | | | | | | |
| Real GDP growth | 3.8 | 3.6 | 2.3 | 2.2 | 2.1 | 2.7 | 3.2 | 3.2 | 3.5 | 3.5 | 3.5 | 3.5 |
| Real per capita income growth 1/ | 1.1 | 0.9 | -0.4 | -0.4 | -0.5 | 0.1 | 0.6 | 0.6 | 0.9 | 0.9 | 0.9 | 0.9 |
| Consumer prices (end of period) | 4.9 | 5.1 | 8.9 | 6.3 | 5.9 | 9.2 | 6.0 | 5.0 | 5.0 | 4.5 | 4.5 | 4.0 |
| | | | | | (In percent of GDP) | | | | | | | |
| **Savings and investment** | | | | | | | | | | | | |
| Gross investment | 17.4 | 17.8 | 17.1 | 19.8 | 19.4 | 19.4 | 19.7 | 19.9 | 20.1 | 20.3 | 20.4 | 20.4 |
| Public | 5.5 | 4.2 | 4.3 | 3.4 | 4.1 | 3.4 | 3.8 | 4.0 | 4.1 | 4.3 | 4.3 | 4.3 |
| Private | 11.9 | 13.7 | 12.8 | 16.3 | 15.4 | 16.0 | 15.9 | 16.0 | 16.0 | 16.0 | 16.1 | 16.1 |
| Savings | 11.8 | 12.4 | 11.1 | 14.5 | 15.2 | 15.0 | 15.3 | 15.7 | 16.1 | 16.5 | 16.6 | 16.7 |
| Public | 2.5 | 2.0 | 2.0 | 2.6 | 2.0 | 3.0 | 2.1 | 2.7 | 2.9 | 3.1 | 3.1 | 3.1 |
| Private | 9.3 | 10.4 | 9.2 | 11.8 | 13.2 | 12.0 | 13.2 | 13.0 | 13.1 | 13.3 | 13.5 | 13.6 |
| **Combined public sector** | | | | | | | | | | | | |
| **Overall balance** | **-3.0** | **-2.2** | **-2.3** | **-0.8** | **-2.0** | **-0.4** | **-1.7** | **-1.2** | **-1.2** | **-1.2** | **-1.2** | **-1.2** |
| Financing | 3.0 | 2.2 | 2.3 | 0.8 | 2.0 | 0.4 | 1.7 | 1.2 | 1.2 | 1.2 | 1.2 | 1.2 |
| External (net) | 1.7 | 0.8 | 1.1 | 0.1 | 0.8 | 1.0 | 0.4 | 0.3 | 0.5 | 0.4 | 0.4 | 0.4 |
| Domestic (net) | 0.7 | 0.7 | -0.6 | 0.7 | 1.2 | -0.6 | 1.3 | 1.0 | 0.7 | 0.7 | 0.8 | 0.8 |
| Privatization/other | 0.6 | 0.7 | 1.8 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| **Central government** | | | | | | | | | | | | |
| Revenues | 10.5 | 10.4 | 11.1 | 11.6 | 11.3 | 11.0 | 11.2 | 11.6 | 12.1 | 12.6 | 12.6 | 12.6 |
| *Of which* | | | | | | | | | | | | |
| Tax revenues | 9.3 | 9.4 | 9.7 | 10.6 | 10.3 | 10.3 | 10.5 | 11.0 | 11.5 | 12.0 | 12.0 | 12.0 |
| Expenditures | 13.3 | 12.4 | 13.3 | 12.2 | 13.4 | 11.4 | 13.0 | 13.1 | 13.6 | 14.1 | 14.1 | 14.1 |
| *Of which* | | | | | | | | | | | | |
| Social and other peace related | 5.3 | 5.0 | 5.5 | 5.1 | 5.3 | 5.0 | 5.8 | 6.0 | 6.3 | 6.9 | 7.2 | 7.2 |
| Interest payments | 1.3 | 1.2 | 1.4 | 1.2 | 1.2 | 1.2 | 1.5 | 1.7 | 1.7 | 1.6 | 1.6 | 1.6 |
| **External sector** | | | | | | | | | | | | |
| Current account | -5.5 | -5.4 | -6.0 | -5.3 | -4.2 | -4.4 | -4.4 | -4.2 | -4.1 | -3.9 | -3.8 | -3.7 |
| *Of which* | | | | | | | | | | | | |
| Exports, f.o.b. | 15.2 | 16.0 | 13.6 | 12.1 | 12.4 | 12.8 | 13.0 | 12.7 | 12.5 | 12.5 | 12.5 | 12.6 |
| Imports, c.i.f. | -24.9 | -26.8 | -26.6 | -27.0 | -27.2 | -29.1 | -29.2 | -28.4 | -28.0 | -27.7 | -27.6 | -27.4 |
| Capital account | 4.9 | 9.2 | 8.3 | 5.2 | 6.3 | 6.6 | 5.4 | 4.4 | 4.7 | 4.4 | 4.6 | 3.9 |
| Official capital and transfers | 2.0 | 1.2 | 1.4 | 0.8 | 1.8 | 1.5 | 1.1 | 1.2 | 1.1 | 0.8 | 0.9 | 0.2 |
| Private sector | 2.8 | 8.0 | 6.9 | 4.4 | 4.6 | 5.1 | 4.3 | 3.2 | 3.6 | 3.6 | 3.7 | 3.8 |
| *Of which* | | | | | | | | | | | | |
| Foreign direct investment | 0.8 | 1.2 | 2.2 | 0.5 | 0.5 | 0.6 | 0.7 | 0.8 | 0.9 | 1.0 | 1.1 | 1.2 |
| **Total NFPS debt** | **17.2** | **16.7** | **17.1** | **15.5** | **17.1** | **18.0** | **17.8** | **17.8** | **17.4** | **16.6** | **16.0** | **14.8** |
| External 2/ | 14.9 | 14.7 | 14.5 | 13.4 | 13.9 | 14.0 | 13.5 | 13.5 | 13.4 | 13.0 | 12.7 | 11.8 |
| Domestic | 2.3 | 2.0 | 2.6 | 2.1 | 3.2 | 4.0 | 4.3 | 4.3 | 4.0 | 3.6 | 3.3 | 3.0 |
| **Memorandum item** | | | | | | | | | | | | |
| **Net international reserves** | | | | | | | | | | | | |
| Net international reserves (in months of next year imports of goods and services) | 2.3 | 3.6 | 4.0 | 3.7 | 4.0 | 4.4 | 4.6 | 4.5 | 4.5 | 4.5 | 4.5 | 4.4 |

Sources: Fund staff estimates and projections.

1/ In 2003-09, the annual population growth is assumed to remain at 2.6 percent.

2/ Excludes debt owed by state-owned enterpise Corfina, which is under dispute. In 2003, this amounted to US$531.5 million, or 2.2 percent of GDP.

Table 13. Guatemala: Indicators of Vulnerability

| | | | | | Prel. | Proj. | |
|---|---|---|---|---|---|---|---|
| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 |
| **External indicators** | | | | | | | |
| Merchandise exports (12-month percentage change) | 10.9 | -7.3 | -1.4 | 8.6 | 12.1 | 10.9 | 2.7 |
| Merchandise imports (12-month percentage change) | 13.4 | 8.4 | 12.4 | 6.6 | 16.2 | 9.2 | 2.7 |
| Terms of trade (12-month percentage change) 1/ | 1.7 | -1.0 | -2.5 | -4.4 | 1.0 | -0.5 | -0.3 |
| Current account balance (in percent of GDP) | -5.4 | -6.0 | -5.3 | -4.2 | -4.4 | -4.4 | -4.2 |
| Capital account balance (in percent of GDP) | 9.2 | 8.3 | 5.2 | 6.3 | 6.6 | 5.4 | 4.4 |
| Net international reserves 2/ | | | | | | | |
| In millions of U.S. dollars | 1,802 | 2,301 | 2,278 | 2,799 | 3,380 | 3,655 | 3,722 |
| In percent of M2 | 42.4 | 44.7 | 39.3 | 41.5 | 44.5 | 42.5 | 39.3 |
| In percent of base money | 120.4 | 129.8 | 108.7 | 126.2 | 135.5 | 135.6 | 126.7 |
| In percent of base money and central bank certificates | 70.0 | 73.0 | 66.2 | 70.4 | 77.4 | 77.5 | 74.2 |
| In percent of short-term external debt on a remaining maturity basis 3/ | 62.1 | 83.3 | 76.3 | 171.8 | 185.8 | 193.3 | 194.5 |
| In percent of net short-term foreign-currency liabilities of comm. banks | 387.0 | 313.7 | 254.1 | 223.6 | 193.9 | n.a. | n.a. |
| In months of next year's imports of goods and nonfactor services | 3.6 | 4.0 | 3.7 | 4.0 | 4.4 | 4.6 | 4.5 |
| Commercial banks foreign assets (in millions of U.S. dollars) | 105.5 | 184.1 | 251.1 | 316.6 | 322.8 | 251.6 | 209.1 |
| Commercial banks foreign liabilities (in millions of U.S. dollars) | 643.0 | 669.0 | 717.1 | 760.7 | 869.7 | 869.7 | 869.7 |
| Real effective exchange rate, percentage change, 12-month period 4/ | -2.0 | 2.5 | 6.9 | 1.7 | 3.7 | n.a. | n.a. |
| Real effective exchange rate, percentage change, eop | 1.9 | 3.2 | 8.3 | -1.9 | 7.5 | n.a. | n.a. |
| **Public indebtness indicators** | | | | | | | |
| Total public sector debt (in percent of GDP) | 17.4 | 17.6 | 15.8 | 17.4 | 18.0 | 17.4 | 17.0 |
| Domestic public sector debt (in percent of GDP) 5/ | 2.0 | 2.6 | 2.1 | 3.2 | 4.0 | 3.9 | 3.5 |
| External public sector debt (in percent of GDP) 6/ | 15.3 | 14.9 | 13.7 | 14.2 | 14.0 | 13.5 | 13.5 |
| (Public sector) external interest payments in percent of exports of goods and nonfactor services | 4.6 | 3.1 | 5.0 | 4.7 | 4.2 | 4.6 | 4.7 |
| (Public sector) external amortization payments in percent of exports of goods and services | 14.5 | 15.2 | 8.3 | 6.6 | 7.8 | 4.9 | 5.0 |
| Public sector and financial sector external debt (in percent of GDP) | n.a. | n.a. | 18.9 | 20.5 | 21.3 | 20.4 | 19.8 |

Sources: Bank of Guatemala; and Fund staff estimates and projections.

1/ Includes trade in goods and nonfactor services.

2/ Excludes claims on Nicaragua amounting to US$145.7 million up to 1999, and US$72.5 million in 2000, which are included in official data.

3/ Includes staff estimates of private external debt. Assumes all foreign liabilities of banking system are short term.

4/ Reflects change in the 12-month average. Negative indicates a real depreciation.

5/ Includes central government and public enterprises; excludes Bank of Guatemala domestic liabilites (around 4.5 percent of GDP in 2002). Data before 2002 are not available.

6/ Includes Bank of Guatemala's external liabilities. Excludes debt owed by state-owned enterprise Corfina, the resolution of which is currently underway. In 2003, this amounted to US$531.5 million or 2.2 percent of GDP (including capitalized interest of US$400 million).

**Error! No sequence specified.}**

Table 14. Guatemala: External Debt Sustainability Framework, 1998-2010

(In percent of GDP, unless otherwise indicated)

| | Actual | | | | | | | | Projected | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | | | 2004 p/ | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | | |
| | | | | | | | | | **I. Baseline Projections** | | | | | | | | Debt-stabilizing non-interest current account 1/ |
| **External debt 2/** | **22.9** | **27.2** | **28.5** | **28.4** | **27.5** | **28.6** | | | **29.2** | **28.9** | **29.2** | **29.4** | **29.2** | **29.1** | **28.3** | | **-2.2** |
| Change in external debt | 2.0 | 4.3 | 1.3 | -0.1 | -0.8 | 1.1 | | | 0.5 | -0.2 | 0.2 | 0.2 | -0.2 | -0.1 | -0.8 | | |
| Identified external debt-creating flows (4+8+9) | 0.4 | 5.0 | -2.4 | -2.1 | -0.4 | 0.5 | | | 0.2 | 0.9 | 1.4 | 0.8 | 0.5 | 0.4 | 0.3 | | |
| Current account deficit, excluding interest payments | 4.0 | 4.0 | 3.6 | 4.3 | 3.9 | 2.9 | | | 3.1 | 2.8 | 2.4 | 2.3 | 2.0 | 1.9 | 1.8 | | |
| Deficit in balance of goods and services | 8.2 | 8.5 | 8.8 | 10.3 | 12.4 | 12.9 | | | 14.4 | 14.1 | 13.7 | 13.4 | 13.1 | 12.9 | 12.6 | | |
| Exports | 18.0 | 18.8 | 20.0 | 18.6 | 17.0 | 16.6 | | | 17.1 | 17.6 | 17.1 | 16.9 | 17.0 | 17.1 | 17.1 | | |
| Imports | 26.2 | 27.2 | 28.9 | 28.8 | 29.4 | 29.5 | | | 31.6 | 31.8 | 30.8 | 30.4 | 30.1 | 29.9 | 29.8 | | |
| Net non-debt creating capital inflows (negative) | -3.4 | -1.7 | -6.5 | -5.7 | -3.0 | -3.3 | | | -3.5 | -2.7 | -1.9 | -2.2 | -2.4 | -2.4 | -2.5 | | |
| Automatic debt dynamics 3/ | -0.2 | 2.7 | 0.5 | -0.7 | -1.4 | 0.9 | | | 0.6 | 0.8 | 0.9 | 0.8 | 0.9 | 1.0 | 1.0 | | |
| Contribution from nominal interest rate | 1.4 | 1.6 | 1.8 | 1.7 | 1.4 | 1.4 | | | 1.4 | 1.6 | 1.8 | 1.8 | 1.9 | 1.9 | 1.9 | | |
| Contribution from real GDP growth | -1.0 | -0.9 | -0.9 | -0.6 | -0.6 | -0.5 | | | -0.7 | -0.9 | -0.9 | -1.0 | -1.0 | -1.0 | -1.0 | | |
| Contribution from price and exchange rate changes 4/ | -0.6 | 2.0 | -0.4 | -1.8 | -2.2 | ... | | | ... | ... | ... | ... | ... | ... | ... | | |
| Residual, incl. change in gross foreign assets (2-3) 4/ | 1.6 | -0.7 | 3.7 | 1.9 | -0.4 | 0.6 | | | 0.4 | -1.1 | -1.2 | -0.6 | -0.8 | -0.6 | -1.1 | | |
| External debt-to-exports ratio (in percent) | 127.2 | 144.8 | 142.3 | 152.8 | 161.7 | 172.4 | | | 170.1 | 164.1 | 170.4 | 173.8 | 171.8 | 170.5 | 164.8 | | |
| **Gross external financing need (in billions of U.S. dollars) 6/** | **3.1** | **3.4** | **3.9** | **4.7** | **4.1** | **4.1** | | | **4.5** | **4.9** | **5.2** | **5.5** | **5.6** | **5.9** | **6.2** | | |
| In percent of GDP | 16.4 | 18.8 | 20.3 | 22.1 | 17.6 | 16.4 | | | 16.8 | 16.8 | 16.7 | 16.9 | 16.2 | 16.1 | 15.9 | | |
| **Key Macroeconomic Assumptions** | | | | | | | 10-Year Historical Average | 10-Year Standard Deviation | | | | | | | | For debt stabilization | Projected Average |
| Real GDP growth (in percent) | 5.0 | 3.8 | 3.6 | 2.3 | 2.2 | 2.1 | 3.5 | 1.1 | 2.7 | 3.2 | 3.2 | 3.5 | 3.5 | 3.5 | 3.5 | 3.5 | 3.3 |
| GDP deflator in U.S .dollars (change in percent) | 2.8 | -8.1 | 1.6 | 6.6 | 8.3 | 3.9 | 4.5 | 5.2 | 5.8 | 5.2 | 2.6 | 2.0 | 2.3 | 2.4 | 2.5 | 2.5 | 3.3 |
| Nominal external interest rate (in percent) | 7.0 | 6.6 | 7.1 | 6.5 | 5.4 | 5.4 | 6.4 | 0.7 | 5.2 | 6.0 | 6.5 | 6.5 | 6.9 | 7.0 | 7.0 | 7.0 | 6.4 |
| Growth of exports (U.S. dollar terms, in percent) | 8.8 | -0.6 | 12.4 | 1.1 | 1.5 | 3.6 | 7.6 | 8.1 | 12.2 | 11.7 | 2.8 | 4.4 | 6.3 | 6.3 | 6.5 | | 7.2 |
| Growth of imports (U.S. dollar terms, in percent) | 20.1 | -0.9 | 11.7 | 9.0 | 13.0 | 6.5 | 9.7 | 8.0 | 16.2 | 9.2 | 2.7 | 4.1 | 5.0 | 5.4 | 5.4 | | 6.9 |
| Current account balance, excluding interest payments | -4.0 | -4.0 | -3.6 | -4.3 | -3.9 | -2.9 | -3.3 | 1.0 | -3.1 | -2.8 | -2.4 | -2.3 | -2.0 | -1.9 | -1.8 | | -2.3 |
| Net non-debt creating capital inflows | 3.4 | 1.7 | 6.5 | 5.7 | 3.0 | 3.3 | 3.4 | 1.6 | 3.5 | 2.7 | 1.9 | 2.2 | 2.4 | 2.4 | 2.5 | | 2.5 |
| | | | | | | | | | **II. Stress Tests for External Debt Ratio** | | | | | | | | Debt-stabilizing non-interest current account 1/ |
| **A. Alternative Scenarios** | | | | | | | | | | | | | | | | | |
| A1. Key variables are at their historical averages in 2005-09 7/ | | | | | | | | | 29.6 | 29.4 | 28.5 | 28.0 | 27.4 | 27.0 | 26.2 | | -2.9 |
| **B. Bound Tests** | | | | | | | | | | | | | | | | | |
| B1. Nominal interest rate is at 200 basis points higher than the projected 2005 level | | | | | | | | | 29.2 | 29.5 | 30.2 | 30.4 | 30.2 | 30.1 | 29.3 | | -2.2 |
| B2. Real GDP growth is at historical average minus two standard deviations in 2005 and 2006 | | | | | | | | | 29.2 | 29.4 | 30.1 | 30.3 | 30.0 | 29.8 | 28.8 | | -2.3 |
| B3. Change in U.S. dollar GDP deflator is at historical average minus two standard deviations in 2005 and 2006 | | | | | | | | | 29.2 | 32.0 | 34.7 | 34.5 | 33.7 | 33.2 | 31.7 | | -2.8 |
| B4. Non-interest current account is at historical average minus two standard deviations in 2005 and 2006 | | | | | | | | | 29.2 | 31.4 | 34.5 | 34.8 | 34.6 | 34.5 | 33.8 | | -2.0 |
| B5. Combination of 1-4 using one standard deviation shocks | | | | | | | | | 29.2 | 32.7 | 36.5 | 36.8 | 36.5 | 36.5 | 35.6 | | -2.5 |
| B6. One-time 30 percent nominal depreciation in 2005 | | | | | | | | | 29.2 | 39.8 | 39.1 | 38.5 | 37.3 | 36.3 | 34.3 | | -3.2 |

p/ Preliminary

1/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and both non-interest current account and nondebt inflows in percent of GDP) remain at their levels of the last projection year.

2/ Includes public and private sector external debt. Excludes debt owed by state-owned enterprise Corfina (amounting to US$531.5 million in 2003) which is under dispute

3/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in U.S. dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

4/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).

5/ For projection, line includes price and exchange rate changes.

6/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

7/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

**Error! No sequence specified.}**

Table 15. Guatemala: Nonfinancial Public Sector Debt Sustainability Framework, 1999-2010 1/
(In percent of GDP, unless otherwise indicated)

| | Actual | | | | | | | | Projections | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | | | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | |
| | | | | | | | | | **I. Baseline Projections** | | | | | | Debt-stabilizing primary balance 1/ |
| **Public sector debt 2/** | **17.2** | **16.7** | **17.1** | **15.5** | **17.1** | **18.0** | | | **17.8** | **17.8** | **17.4** | **16.6** | **16.0** | **14.8** | 0.6 |
| *Of which:* foreign-currency denominated | 14.9 | 15.0 | 14.7 | 13.4 | 14.2 | 14.1 | | | 13.5 | 13.5 | 13.4 | 13.0 | 12.7 | 11.8 | |
| Change in public sector debt | 5.7 | -0.4 | 0.3 | -1.6 | 1.6 | 0.9 | | | -0.2 | 0.0 | -0.4 | -0.8 | -0.6 | -1.2 | |
| Identified debt-creating flows (4+7+12) | 2.4 | -0.3 | -0.3 | -1.5 | 1.6 | -0.6 | | | 0.2 | 0.0 | 0.1 | 0.1 | 0.2 | 0.3 | |
| Primary deficit | 1.5 | 0.8 | 0.8 | -0.6 | 1.0 | -0.8 | | | 0.4 | -0.2 | -0.2 | -0.1 | -0.1 | 0.1 | |
| Revenue and grants | 10.5 | 10.4 | 11.1 | 11.5 | 11.3 | 11.0 | | | 11.2 | 11.7 | 12.2 | 12.7 | 12.6 | 12.5 | |
| Primary (noninterest) expenditure | 12.0 | 11.2 | 11.9 | 11.0 | 12.3 | 10.2 | | | 11.5 | 11.5 | 12.1 | 12.5 | 12.5 | 12.6 | |
| Automatic debt dynamics 3/ | 1.5 | -0.5 | 0.3 | -0.9 | 0.6 | -0.2 | | | -0.1 | 0.2 | 0.2 | 0.2 | 0.3 | 0.2 | |
| Contribution from interest rate/growth differential 4/ | 0.3 | -0.5 | -0.1 | -0.4 | 0.0 | -0.2 | | | -0.1 | 0.2 | 0.2 | 0.2 | 0.3 | 0.2 | |
| *Of which:* contribution from real interest rate | 0.7 | 0.1 | 0.2 | 0.0 | 0.4 | 0.3 | | | 0.4 | 0.8 | 0.8 | 0.8 | 0.8 | 0.7 | |
| *Of which:* contribution from real GDP growth | -0.4 | -0.6 | -0.4 | -0.3 | -0.3 | -0.4 | | | -0.5 | -0.5 | -0.6 | -0.6 | -0.5 | -0.5 | |
| Contribution from exchange rate depreciation 5/ | 1.1 | 0.0 | 0.5 | -0.6 | 0.5 | ... | | | ... | ... | ... | ... | ... | ... | |
| Other identified debt-creating flows | -0.6 | -0.7 | -1.5 | 0.0 | 0.0 | 0.4 | | | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| Privatization receipts (negative) | -0.6 | -0.7 | -1.5 | 0.0 | 0.0 | 0.0 | | | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| Recognition of implicit or contingent liabilities | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | | | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| Other (specify, e.g., bank recapitalization) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.4 | | | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| Residual, including asset changes (2-3) 6/ | 3.3 | -0.1 | 0.7 | -0.1 | 0.1 | 1.6 | | | -0.5 | 0.0 | -0.5 | -0.9 | -0.8 | -1.5 | |
| Public sector debt-to-revenue ratio 2/ | 163.7 | 161.0 | 153.8 | 134.2 | 152.0 | 164.3 | | | 159.5 | 152.2 | 142.2 | 131.0 | 127.2 | 118.7 | |
| **Gross financing need 7/** | **5.9** | **5.8** | **7.0** | **2.7** | **3.6** | **1.4** | | | **2.6** | **2.1** | **2.5** | **2.0** | **2.0** | **1.2** | |
| In billions of U.S. dollars | 1.1 | 1.1 | 1.5 | 0.6 | 0.9 | 0.4 | | | 0.8 | 0.6 | 0.8 | 0.7 | 0.7 | 0.5 | |
| **Key Macroeconomic and Fiscal Assumptions** | | | | | | | 8-Year Historical Average | 8-Year Standard Deviation | | | | | | | Projected Average |
| Real GDP growth (in percent) | 3.8 | 3.6 | 2.3 | 2.2 | 2.1 | 2.7 | 3.4 | 1.1 | 3.2 | 3.2 | 3.5 | 3.5 | 3.5 | 3.5 | 3.0 |
| Average nominal interest rate on public debt (in percent) 8/ | 12.3 | 7.7 | 9.2 | 8.1 | 8.0 | 7.7 | 9.1 | 2.1 | 9.0 | 10.5 | 10.2 | 10.2 | 10.3 | 9.9 | 8.6 |
| Average real interest rate (nominal rate minus change in GDP deflator, in percent | 7.3 | 0.9 | 1.6 | -0.1 | 2.6 | 1.8 | 1.8 | 2.8 | 2.6 | 4.8 | 5.2 | 5.1 | 5.5 | 5.2 | 3.7 |
| Nominal appreciation (increase in U.S. dollar value of local currency, in percent) | -11.4 | -0.1 | -3.5 | 4.2 | -4.0 | ... | -3.9 | 5.4 | ... | ... | ... | ... | ... | ... | ... |
| Inflation rate (GDP deflator, in percent) | 5.0 | 6.8 | 7.6 | 8.1 | 5.5 | 6.0 | 7.3 | 1.6 | 6.4 | 5.6 | 5.0 | 5.1 | 4.8 | 4.7 | 5.2 |
| Growth of real primary spending (deflated by GDP deflator, in percent) | 15.6 | -3.3 | 8.7 | -5.7 | 14.1 | -14.8 | 10.0 | 10.7 | 17.0 | 3.1 | 8.5 | 7.5 | 3.2 | 0.0 | 5.7 |
| Primary deficit | 1.5 | 0.8 | 0.8 | -0.6 | 1.0 | -0.8 | 0.7 | 0.7 | 0.4 | -0.2 | -0.2 | -0.1 | -0.1 | 0.1 | 0.0 |
| | | | | | | | | | **II. Stress Tests for Public Debt Ratio** | | | | | | Debt-stabilizing primary balance 1/ |
| **A. Alternative Scenarios** | | | | | | | | | | | | | | | |
| A1. Key variables are at their historical averages in 2004-08 10/ | | | | | | | | | 17.9 | 18.3 | 18.1 | 17.6 | 17.2 | 16.0 | 0.0 |
| **B. Bound Tests** | | | | | | | | | | | | | | | |
| B1. Real interest rate is at historical average plus two standard deviations in 2004 and 2005 | | | | | | | | | 18.6 | 19.1 | 18.8 | 18.0 | 17.5 | 16.3 | 0.6 |
| B2. Real GDP growth is at historical average minus two standard deviations in 2004 and 2005 | | | | | | | | | 18.4 | 19.3 | 19.5 | 19.2 | 19.2 | 18.6 | 0.7 |
| B3. Primary balance is at historical average minus two standard deviations in 2004 and 2005 | | | | | | | | | 19.5 | 21.9 | 21.6 | 21.0 | 20.6 | 19.5 | 0.7 |
| B4. Combination of 1-3 using one standard deviation shocks | | | | | | | | | 19.3 | 21.1 | 20.8 | 20.1 | 19.6 | 18.5 | 0.7 |
| B5. One-ime 30 percent real depreciation in 2004 10/ | | | | | | | | | 29.0 | 29.6 | 29.6 | 29.3 | 29.2 | 28.4 | 1.1 |
| B6. 10 percent of GDP increase in other debt-creating flows in 2004 | | | | | | | | | 27.8 | 28.3 | 28.3 | 27.8 | 27.7 | 26.9 | 1.0 |

1/ Assumes that key variables (real GDP growth, real interest rate, and primary balance) remain at the level in percent of GDP/growth rate of the last projection year.
2/ Includes nonfinancial public sector debt.
3/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; $\pi$ = growth rate of GDP deflator; g = real GDP growth rate; $\alpha$ = share of foreign-currency denominated debt; and $\varepsilon$ = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).
4/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi (1+g)$ and the real growth contribution as -g.
5/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.
6/ For projections, this line includes exchange rate changes.
7/ Defined as public sector deficit, plus amortization of medium- and long-term public sector debt, plus short-term debt at end of previous period.
8/ Derived as nominal interest expenditure divided by previous period debt stock.
9/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.
10/ Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Table 16. Guatemala: Millennium Development Goals

| | 1990 | 1995 | 2001 | 2002 | 2015 Target |
|---|---|---|---|---|---|
| 1. Eradicate extreme poverty and hunger | | | | | |
| Population below $1 a day (%) | .. | .. | 16 | .. | Halve 1990 $1 a day poverty rate |
| Poverty gap at $1 a day (%) | .. | .. | 4.6 | .. | |
| Percentage share of income or consumption held by poorest 20% | .. | .. | 2.6 | .. | |
| Prevalence of child malnutrition (% of children under 5) | .. | 26.6 | 24.2 | .. | Halve 1990 malnutrition rate |
| Population below minimum level of dietary energy consumption (%) | 16 | 21 | 25 | .. | |
| 2. Achieve universal primary education | | | | | |
| Net primary enrollment ratio (% of relevant age group) | .. | 72.5 | 85 | .. | Net enrollment to 100 |
| Percentage of cohort reaching grade 5 (%) | .. | 49.6 | 55.8 | .. | |
| Youth literacy rate (% ages 15-24) | 73.4 | 76.5 | 79.6 | 80.1 | |
| 3. Promote gender equality | | | | | |
| Ratio of girls to boys in primary and secondary education (%) | .. | 88.4 | 92.5 | .. | Education ratio to 100 |
| Ratio of young literate females to males (% ages 15-24) | 82.3 | 83.9 | 85.3 | 85.6 | |
| Share of women employed in the nonagricultural sector (%) | 36.8 | .. | 37.5 | 39.2 | |
| Proportion of seats held by women in national parliament (%) | .. | 8 | .. | .. | |
| 4. Reduce child mortality | | | | | |
| Under 5 mortality rate (per 1,000) | 82 | 64 | 59 | 49 | Reduce 1990 under 5 mortality by two-thirds |
| Infant mortality rate (per 1,000 live births) | 60 | 49 | 44 | 36 | |
| Immunization, measles (% of children under 12 months) | 68 | 83 | 91 | 92 | |
| 5. Improve maternal health | | | | | |
| Maternal mortality ratio (modeled estimate, per 100,000 live births) | .. | .. | 240 | .. | Reduce 1990 maternal mortality by three-fourths |
| Births attended by skilled health staff (% of total) | .. | 34.3 | 40.6 | .. | |
| 6. Combat HIV/AIDS, malaria and other diseases | | | | | |
| Prevalence of HIV, female (% ages 15-24) | .. | .. | 0.8 | .. | Halt, and begin to reverse, AIDS, etc. |
| Contraceptive prevalence rate (% of women ages 15-49) | .. | 31.9 | 38.2 | .. | |
| Number of children orphaned by HIV/AIDS | .. | .. | 32,000 | .. | Halt, and begin to reverse, AIDS, etc. |
| Incidence of tuberculosis (per 100,000 people) | .. | .. | 82 | 77.2 | |
| Tuberculosis cases detected under DOTS (%) | .. | 44 | 39 | 45 | |
| 7. Ensure environmental sustainability | | | | | |
| Forest area (% of total land area) | 31.2 | .. | 26.3 | .. | |
| Nationally protected areas (% of total land area) | .. | 16.8 | 16.8 | 20 | |
| GDP per unit of energy use (PPP $ per kg oil equivalent) | 5.5 | 6.3 | 6.4 | .. | |
| CO2 emissions (metric tons per capita) | 0.6 | 0.7 | 0.9 | .. | |
| Access to an improved water source (% of population) | 76 | .. | 92 | .. | |
| Access to improved sanitation (% of population) | 70 | .. | 81 | .. | |
| Access to secure tenure (% of population) | .. | .. | .. | .. | |
| 8. Develop a Global Partnership for Development | | | | | |
| Youth unemployment rate (% of total labor force ages 15-24) | .. | .. | .. | .. | |
| Fixed line and mobile telephones (per 1,000 people) | 21.3 | 31.7 | 162.8 | 202 | |
| Personal computers (per 1,000 people) | .. | 3 | 12.8 | 14.4 | |
| General indicators | | | | | |
| Population (million) | 8.7 | 10.0 | 11.9 | 12.0 | |
| Gross national income (U.S. dollar billion) | 8.5 | 14.5 | 21.5 | 23.6 | |
| GNI per capita (U.S. dollars) | 977 | 1,448 | 1,810 | 1,965 | |
| Adult literacy rate (percent of people ages 15 and over) | 61 | 64.9 | 69.2 | 69.9 | |
| Total fertility rate (births per woman) | 5.3 | 5.1 | 4.6 | 4.3 | |
| Life expectancy at birth (years) | 61.4 | 63.6 | 65.0 | 65.5 | |
| Aid (percent of GNI) | 2.7 | 1.4 | 1.1 | 1.1 | |
| Gross investment (% of GDP) | 13.6 | 15.1 | 17.1 | 19.8 | |
| Trade (% of GDP) | 33.5 | 37.2 | 40.2 | 39.1 | |

Source: *World Development Indicators database, April 2004, and IMF staff estimates*

Note: In some cases the data are for earlier or later years than those stated.

Goal 1 targets: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day. Halve, between 1990 and 2015, the proportion of people who suffer from hunger.

Goal 2 target: Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling.

Goal 3 target: Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education no later than 2015.

Goal 4 target: Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate.

Goal 5 target: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.

Goal 6 targets: Have halted by 2015, and begun to reverse, the spread of HIV/AIDS. Have halted by 2015, and begun to reverse, the incidence of malaria and other major proportion of people without sustainable access to safe drinking water. By 2020, to have achieved a significant improvement in the lives of at least 100 million slum dwellers.

Goal 8 targets: Develop further an open, rule-based, predictable, non-discriminatory trading and financial system. Address the Special Needs of the Least Developed Countries. Address the Special Needs of landlocked countries and small island developing states. Deal comprehensively with the debt problems of developing countries through national and international measures in order to make debt sustainable in the long term. In cooperation with developing countries, develop and implement strategies for decent and productive work for youth. In cooperation with pharmaceutical companies, provide access to affordable, essential drugs in developing countries. In cooperation with the private sector, make available the benefits of new technologies, especially information and communications.

# GUATEMALA—FUND RELATIONS
(As of March 31, 2005)

**I. Membership Status:** Joined: December 28, 1945, Article VIII

| II. General Resources Account: | SDR Million | Percentage of Quota |
|---|---|---|
| Quota | 210.20 | 100.00 |
| Fund holdings of currency | 210.21 | 100.00 |

| III. SDR Department | SDR Million | Percentage of Allocation |
|---|---|---|
| Net cumulative allocation | 27.68 | 100.0 |
| Holdings | 5.01 | 18.11 |

**IV. Outstanding Purchases and Loans:** None

**V. Financial Arrangements:**

| Type | Approval Date | Expiration Date | Amount Approved (SDR Million) | Amount Drawn (SDR Million) |
|---|---|---|---|---|
| Stand-By | 06/18/03 | 03/15/04 | 84.00 | 0.00 |
| Stand-By | 04/01/02 | 03/31/03 | 84.00 | 0.00 |
| Stand-By | 12/18/92 | 03/17/94 | 54.00 | 0.00 |

**VI. Projected Obligations to the Fund** (SDR million; based on existing use of resources and present holdings of SDRs):

| | Forthcoming | | | | |
|---|---|---|---|---|---|
| | 2005 | 2006 | 2007 | 2008 | 2009 |
| Charges/interest | 0.42 | 0.56 | 0.56 | 0.56 | 0.56 |
| **Total** | **0.42** | **0.56** | **0.56** | **0.56** | **0.56** |

**VII. Safeguards Assessment**

Under the Fund's safeguards assessment policy, Bank of Guatemala (BANGUAT) was subject to an assessment with respect to the Stand-By Arrangement, which was approved on April 1, 2002 (Country Report No: 02/80). The assessment, which was completed on August 09, 2002, identified certain weaknesses and made appropriate recommendations.

## VIII. Exchange Rate Arrangements

Since March 1994, Guatemala has had an arrangement based on an interbank foreign exchange market in which authorized financial institutions buy and sell foreign exchange at market-determined rates. Financial institutions authorized to operate in the foreign exchange market include commercial banks, finance companies, and exchange houses. The exchange regime is classified as "Managed floating with no pre-announced path for the exchange rate." As of March 29, 2005 the reference exchange rate was Q 7.61 per U.S. dollar.

## IX. Last Article IV Consultation

The last Article IV consultation was concluded by the Executive Board on October 3, 2002. Staff proposed that Guatemala remain on a 24-month consultation cycle.

## X. FSAP Participation

An FSAP was conducted on July 3–7, 2000 and on September 11–23, 2000, and the Financial System Stability Assessment was discussed by the Executive Board on May 14, 2001 at the time of the 2001 Article IV consultation.

## XI. Technical Assistance

In June 2000 an STA mission assisted the authorities in developing a new CPI. In October and December 2000, a joint World Bank-IMF mission visited Guatemala to help prepare draft legislation on central bank, banking sector, and banking supervision. In December 2000 and June 2002 MAE missions provided assistance on payments system issues. In February 2001, MAE provided assistance on bank restructuring. FAD provided assistance in May 2001 on tax policy and tax administration; in February 2002 on expenditure management; in August 2003 and March 2004 on tax policy; and in April and November 2004 on tax administration. A STA mission on balance of payments statistics took place in March 2004. A STA mission visited Guatemala City in March 2004 to assist in completing General Data Dissemination System metadata for the financial and external sectors. MFD missions on inflation targeting visited Guatemala in September 2004 and March 2005. FAD missions on expenditure management and on tax administration visited Guatemala in January-February 2005.

## XII. Resident Representative

Mr. Erik Offerdal opened the Resident Representative office in August 2003.

## KEY STAFF RECOMMENDATIONS FOR TAX ADMINISTRATION REFORM

Fund staff (FAD) has worked closely with the authorities over the past year to design a comprehensive plan to strengthen tax administration and tax enforcement in Guatemala. The staff's main recommendations in this area have been:

**Taxpayer segmentation (early 2005)**

1. The purpose of taxpayer segmentation is to focus tax control on specific taxpayers, based on their tax significance. The criterion for selecting large taxpayers would include total sales and the amount of tax paid. The Superintendency for Tax Administration (SAT) should:

- Create a "Large Taxpayers Coordination" (CGC) unit, responsible for monitoring the country's 300 largest taxpayers; the existing Special Taxpayer Coordination (CCE) unit would administer the subsequent 2,700 largest taxpayers.

- "Account officers" should be appointed within the CGC and the CCE units to manage taxpayer files. The account officers would be responsible for advising taxpayers and taking action against those who do not file on time or are delinquent.

**Incentives to file electronically (early 2005)**

2. Banks not complying with SAT Resolutions 610-2002 and 263-2002 should be penalized. The purpose is to encourage the electronic filing of returns to prevent errors, create reliable databases, and facilitate effective cross-checks of data. The SAT should:

- Require all taxpayers managed by CGCs and CCEs to file and pay electronically.

- Suspend banks that accept paper returns for taxes owed in excess of Q 10,000. These banks would no longer be authorized to receive tax returns and payments.

**Electronic recording of large taxpayers' purchases and sales (*AsisteLibros*) (early 2005)**

3. The purpose of electronic recording is to identify large taxpayers' suppliers, in order to verify compliance with their tax obligations. The SAT should:

- Require large taxpayers to use SAT's AsisteLibros software.

**Control of late filing and delinquent taxpayers (early 2005)**

4. The purpose is to immediately penalize noncompliance with deadlines by requiring delinquent taxpayers to make payments based on previous returns. The SAT should:

- Require delinquent taxpayers to make a partial payment based on previous returns, in accordance with Articles 106, 107, and 109 of the Tax Code.

- Allow taxpayers to file returns without paying in full the amount reported as due but while immediately taking collection action to recover the resulting debt.

**Customs control (mid-2005)**

5. To combat smuggling, the waybills of air and sea carriers should be electronically linked to customs declarations, to assure consistency of the declared data. The SAT should:

- Begin using the electronic air and sea waybill (done in April 2005).

- Establish a new electronic customs declaration (declaración única de aduanas, DUA) for operations carried out on or after June 1, 2005.

**Legal changes to improve the tax administration (late 2005)**

- **VAT withholding**. Withholding helps curb evasion and generates immediate revenue. Legislation should establish withholding systems with a rate of 3 percent for: (a) imports, (b) large taxpayers' purchases, (c) large exporters' purchases, and (d) credit card operations.

- **Simplified system for small taxpayers**. A new VAT system for small taxpayers should include monthly payments, eliminate the requirement of filing returns, and prohibit the issuance of invoices that generate tax credits.

- **Means of payment for large transactions**. Legislation should promote the use of banks for commercial transactions in order to detect false VAT credits. The SAT should require that invoices amounting to Q 10,000 or more be paid using bank means of payment (checks, electronic transfers, credit and debit cards, etc.). Invoices over Q 10,000 *not* paid using bank means would not generate tax credits for the VAT and would not be accepted as a deductible expense on income tax returns.

- **Third-party information**. Third-party information is essential for ascertaining the real economic circumstances of taxpayers and determining their true ability to pay taxes. The powers envisaged in Article 30 of the Tax Code (currently suspended) should be reinstated to enable the SAT to obtain information from third parties.

- **Seizure of vehicles**. Legislation should authorize SAT to seize vehicles found to be transporting contraband.

- **Suspended taxpayers**. Some taxpayers apply for registration for the sole purpose of issuing invoices to document nonexistent transactions to generate false credits for VAT or false expenditure on income tax returns. Legislation should authorize the SAT to introduce a "suspended taxpayers" category for taxpayers with no tax activity during a one-year period or who have failed to answer summonses. Suspended taxpayers would not be eligible for automatic renewal of the their tax registration and would not be allowed to print invoices to grant tax credits for VAT or to document expenditure on income tax returns. Some applications from suspended taxpayers should be denied (such as, authorization to print invoices, tax refunds request, importers and customs agents licenses request, change of vehicle license plates authorization, approval of books of accounts, authorization of branches, issuance of government supplier certificates).

- **Invoicing control**. Legislation should establish specific controls to detect the use of false invoices, which reduces the base of the VAT and the income tax. The SAT should have the power to determine the data requirements as well as the procedures to control the printing of tax invoices and other fiscal documents.

## GUATEMALA—RELATIONS WITH THE WORLD BANK

(As of January 31, 2005)

1. IBRD assistance to Guatemala intensified considerably after the signing of the Peace Accords agreements, particularly during the last Country Assistance Strategy (CAS) implementation period (1998 to 2001). Eleven new projects were approved during this period and assistance expanded in the areas of poverty reduction, policy analysis, civil society engagements, decentralization, with a special focus on gender and indigenous issues. In order to set forth Bank assistance plans during the interim period (2002–2004), a CAS Progress Report was presented to the Board of Directors on May 31, 2002. The update to the strategy does not differ significantly from the previous CAS, and highlights the importance of Bank support of the reforms in the financial sector.

2. As of January 31, 2005 the IBRD portfolio in Guatemala contained 12 projects for a total commitment of US$526 million, of which US$251 million remains undisbursed. The portfolio is relatively new (the average implementation period is approximately 3.5 years), as all projects have become effective after December 1998. The last project approved by the Bank's Board was the Second Main and Rural Roads Project (US$47 million) supports the government's initiative to build and repair rural, secondary, and main roads and bridges, providing some 500,000 local people in an impoverished and isolated part of the country better and quicker access to markets, schools, health clinics, and other key facilities. The project recently was recently declared effective and began full implementation in November 2004.

3. **Future Assistance**: In coordination with the new authorities, the World Bank will develop a new CAS which is expected to be completed during the first half of 2005. The central component of the Bank's support for Guatemala would be a programmatic series of quick-disbursing operations to support the Berger Administration's program, *Vamos Guatemala!* focusing especially on supporting the policy and institutional development aspects of the government's strategy for accelerating broad-based growth and improving governance as key components of the effort to reduce poverty and improve social conditions. These operations will be accompanied by selective investment lending in key areas such as Education, Public Sector Management, Health and Nutrition, Judicial Systems and Land Property Rights.

## Guatemala: Relations with the World Bank

### I. Active IBRD Portfolio

| IBRD Operations by Sector (US$ millions, as of January 31, 2005) | Disbursed | Undisbursed |
|---|---|---|
| Transportation | 49.4 | 64.0 |
| Private Sector Development | 2.2 | 18.1 |
| Law and Public Administration | 66.0 | 55.9 |
| Land Management | 23.0 | 0.0 |
| Financial Sector | 100.8 | 54.2 |
| Environment and Rural Development | 15.6 | 14.4 |
| Education | 17.6 | 44.5 |
| **TOTAL** | **274.7** | **251.2** |
| Plus: Disbursements from closed projects | 687.6 | |
| Less: Repaid principal [1] | 476.5 | |
| **Current Debt outstanding** | **477.5** | |

| IBRD Flows (US$ millions) [2] | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|---|
| Gross disbursements | 51.4 | 46.3 | 82.9 | 45.0 | 79.2 | 2.4 |
| Principal Repayments (-) | 13.2 | 11.6 | 13.4 | 17.9 | 29.2 | 1.9 |
| **Total Net Disbursements** | **38.2** | **34.7** | **69.5** | **27.1** | **50.0** | **0.5** |
| Interests and Fees (-) | 20.8 | 22.3 | 22.1 | 18.6 | 16.9 | 0.8 |
| **Total Net Cash Flows** | **17.4** | **12.4** | **47.4** | **8.5** | **33.1** | **-0.3** |
| **Debt Outstanding (end of year)** | **295.7** | **329.5** | **399.8** | **427.6** | **477.7** | **477.5** |

1/ Including exchange rate adjustments (-US$8.3 million)

2/ Figures for 2005 reflect flows until January 31, 2005.

Source: World Bank Country Management Unit

## GUATEMALA—RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK
(As of February 2005)

### A. Recent Projects and Objectives

1. The Bank's country strategy with Guatemala parallels the new 2004–2007 political cycle in the country, which began when President Berger took office.

2. The IDB strategy with Guatemala has the central objective of poverty reduction. To achieve it, the program for the period 2004–2007 has established two interrelated strategic objectives: (i) to improve the conditions for efficient production and incorporate excluded sectors into the productive process; and (ii) to strengthen human capital with equity. Also, the strategy includes improvements in the country's institutions in support of better governance as a cross-cutting issue, which is a necessity for progress in both areas. The Bank seeks to support the government's strategy, whose focus is the promotion of opportunities for higher economic growth and job creation with broad participation by all sectors, which will reduce poverty levels in a setting of macroeconomic stability.

3. In 2003 the Bank approved loans to finance the national census (US$25 million), investments in rural water and sanitation (US$50 million) and a project for electricity interconnection with Mexico (US$37.5 million). In 2004 the Bank approved only one loan to support social public expenditure reform (US$100 million). Also in the pipeline are projects in the areas of citizen security, rural electricity. environment and indigenous population. The Bank is supporting the authorities to define a strategy to reduce poverty. In addition, the Bank has been supporting nonfinancial activities including the coordination of the Consultative Group meetings in Guatemala and several sectoral studies (growth, governance, etc).

### B. IDB Loan Disbursements 1998 – 2004

(In millions of U.S. dollars)

| | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 |
|---|---|---|---|---|---|---|
| **Disbursements** | **169.6** | **65.7** | **96.5** | **195.1** | **53.4** | **118.3** |
| Amortization | 46.4 | 42.3 | 35.1 | 39.5 | 51.9 | 72.5 |
| Interest and charges | 42.1 | 49.0 | 41.8 | 57.1 | 54.0 | 46.5 |
| **Net flows** | **81.1** | **-25.6** | **19.6** | **98.5** | **-52.5** | **0.3** |

**C. IDB Schedule of Loan Disbursements 2005– 2007 1/**

(In millions of U.S. dollars)

| | 2005 | 2006 | 2007 |
|---|---|---|---|
| **Disbursements** | **82.3** | **160.0** | **180.0** |
| | | | |
| Amortization | 64.0 | 68.6 | 71.6 |
| Interest and charges | 53.9 | 67.7 | 66.9 |
| | | | |
| **Net flows** | **-35.6** | **23.7** | **41.5** |

1/ Includes loans that are anticipated but not yet approved.

**D. IDB Portfolio in Guatemala as of February 2005**

(In millions of U.S. dollars)

| **Sector** | **Approved** | **Undisbursed** |
|---|---|---|
| Quality of public expenditure | 100 | 100 |
| Social sectors | 325 | 120 |
| Community development | 205 | 61 |
| Environment | 64 | 11 |
| Health | 55 | 48 |
| Physical infrastructure | 269 | 179 |
| Agriculture | 33 | 21 |
| Reform loans | 38 | 6 |
| Infrastructure and investment | 8 | 0 |
| Justice | 25 | 4 |
| Trade | 5 | 2 |
| Technology development | 11 | 10 |
| **Total** | **776** | **436** |

## GUATEMALA STATISTICAL ISSUES

1. The authorities have made efforts to improve the macroeconomic statistics and are very cooperative in providing data to the Fund. However, important deficiencies remain in the areas of government finance, balance of payments, money and banking, and national accounts and price statistics. As noted below, the authorities are beginning to address problems with assistance from STA. Guatemala became a participant in the General Data Dissemination System (GDDS) in 2004.

2. A data ROSC mission visited Guatemala City during October 14-28 2004. The mission identified shortcomings mainly in national accounts and balance of payments. Main recommendations were: (i) announce publication by early 2005 of the national accounts for 2001 that will serve as a benchmark in the preparation of a new series consistent with 1993 SNA; (ii) expand the coverage of the fiscal statistics to include social security agencies, local governments, and nonfinancial public enterprises; (iii) widen the coverage of the monetary statistics to include offshore banks and credit and savings cooperatives; (iv) prepare sectoral breakdowns of depository corporations in accordance with the *MFSM* methodology; (v) implement the conversion of balance of payments statistics according to *BPM5* recommendations; and (vi) expand balance of payments data sources by implementing new ITRS forms and conducting surveys.

**National accounts statistics**

3. The national accounts are compiled by the Bank of Guatemala (BG) based on the *1953 U.N. System of National Accounts (1953 SNA)* with 1958 as the base year. The conceptual framework, methodology and base year of national accounts are seriously outdated. Commendably, however, the BG is working intensely to implement the 1993 SNA and produce a higher-quality series with 2001 as base year, with results expected shortly. Paucity of source data is the key factor hindering the accuracy and reliability of the national accounts. In particular, compilation of the traditional national accounts series relies on administrative source data, with virtually no data obtained from surveys; therefore, the coverage of national accounts is limited. GDP is compiled by the production approach at constant (1958) prices only and by the expenditure approach at current and constant prices. Data are published annually with preliminary estimates available with a lag of about three months. Processes for assessment and validation of source, intermediate, and output data are weak. STA provided technical assistance in August 1997 with follow-up missions in national accounts in January 1998 and March 1999, and a June 2000 mission for the CPI.

4. The National Institute of Statistics (NIS) introduced a new CPI based on weights from a household expenditure survey conducted in 1998/1999, and publication of the new CPI began in February 2001. However, there are some weaknesses in the compilation of the CPI related to the treatment of missing prices, changes in product quality, and the inclusion of new products. The data ROSC mission concluded that the independence of the NSI might be seen as hindered by its lack of financial autonomy and a governing body comprising

representatives from ministries and industry associations. The head of the NIS is a member of the NIS Board, but lacks the right to vote, which may undermine accountability. Fines for nonreporting and misreporting are low, with no mechanism to preserve their real value, which could complicate efforts to improve source data by the members of the National Statistical System. Resources at the NIS are insufficient, including for compiling the CPI, and the contribution of the NIS to the compilation of the national accounts is minimal. In addition, a producer price index, basic input for compiling national accounts estimates in real terms, is not compiled.

**Monetary statistics**

5. Data on the BG, commercial banks, and other financial institutions are being compiled on a monthly basis and sent regularly to the Fund for publication in the IFS. However, data on offshore banks is not yet included. In 1998 a technical assistance mission recommended to the BG measures to improve the data compilation of the financial system, including: (i) compilation of monetary statistics for savings and credit cooperatives; (ii) revision of the money and credit aggregates; (iii) classification of domestic institutional units into central and local governments, no financial public enterprises, and the financial corporations sub sector (central bank, depository corporations, and other financial corporations), which will improve the coherence of monetary data with data from the balance of payments, fiscal sector, and national accounts; and (iv) breakdown between residents and nonresidents in the monetary accounts. A September 2001 monetary and financial statistics mission advised BG to establish a work plan to undertake all of these recommendations. As of end-2004, commercial banks were still unable to provide adequately sectorized data (financial assets and liabilities not broken-down by counterpart sector). An August 2004 mission assisted the BG in developing an integrated monetary database to be used internally by the BG, as well as by the WHD and STA.

**Government finance statistics**

6. There are problems in reconciling the government public sector balance as measured from above the line from that as measured from the financing flows (below the line). While progress has been made in adopting the new accounting framework for the budget, insufficient work has been conducted to improve statistics of the social security and public enterprises. In fact overall public sector data are not compiled on a regular basis by the ministry of finance.

**Balance of payments**

7. The overall conceptual framework used to compile the balance of payments is in broad conformity with the guidelines in *BPM4*, but plans are underway for a full transition to *BPM5*. The BG compiles annual balance of payments and quarterly balance of payments based on the *BPM5* are prepared for IMF publication (*IFS* and *BOPSY*). As surveys are not conducted, data sources are insufficient and not fully dependable for compilation. Data

collection is largely based on the International Reporting Transactions Reporting System (ITRS) managed by banks.

8. The data ROSC mission found shortcomings similar to those identified by the TA mission of March 2004. Following these missions, BG is in the process of hiring an external expert to support the implementation of recommendations. Main recommendations were: (i) implement and publish the planned conversion of balance of payments statistics according to *BPM5* recommendations; (ii) expand data sources by implementing new foreign exchange transactions forms (ITRS) and conducting surveys commencing with direct investment enterprises; (iii) and modify as planned the new ITRS forms following BPM5 classification and sectorization to ensure identification of transactions involving financial assets and liabilities and the residency status of transactors.

## GUATEMALA: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE
(As of April 18, 2005)

| | Date of latest observation | Date received | Frequency of Data[6] | Frequency of Reporting[6] | Frequency of publication[6] |
|---|---|---|---|---|---|
| Exchange Rates | 4/15/05 | 4/18/05 | D | D | D |
| International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1] | 4/15/05 | 4/18/05 | D | D | D |
| Reserve/Base Money | 3/31/05 | 4/1/05 | D | D | D |
| Broad Money | 2/25/05 | 3/15/05 | M | M | M |
| Central Bank Balance Sheet | 4/15/05 | 4/18/05 | D | D | D |
| Consolidated Balance Sheet of the Banking System | 2/25/05 | 3/15/05 | M | M | M |
| Interest Rates[2] | 4/7/05 | 4/15/05 | D | D | D |
| Consumer Price Index | 3/05 | 4/15/05 | M | M | M |
| Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4] | 3/05 (Financing) | 4/15/05 | M | M | M |
| Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government | 4/05 | 4/15/05 | M | M | M |
| Stocks of Central Government and Central Government-Guaranteed Debt[5] | 12/31/04 | 1/15/05 | M | M | M |
| External Current Account Balance | 12/04 | 3/28/05 | Q | I | Q |
| Exports and Imports of Goods and Services | 12/04 | 3/28/05 | Q | I | Q |
| GDP/GNP | 2003 | 3/31/04 | A | A | A |
| Gross External Debt | 12/31/04 | 2/15/05 | M | M | M |

[1]Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).

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# IMF Executive Board Concludes 2005 Article IV Consultation with Guatemala

On May 16, 2005, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Guatemala.[1]

**Background**

Guatemala has pursued macroeconomic stabilization successfully since the 1996 Peace Accords, although the goals of the Accords remain to be fully realized. Fiscal discipline has anchored the policy framework; international reserves have risen; and the banking system has been strengthened. Following three years of sluggish economic growth, activity improved somewhat in 2004, with real GDP rising by 2¾ percent, but consumer price inflation drifted upward to over 9 percent. Guatemala continues to suffer from widespread poverty; and, according to a 2002 World Bank survey, perceptions of corruption and weak integrity of some public institutions pose additional challenges.

The government that took office last year has adopted the Peace Accords as the platform for its policy agenda. The Accords embody a broad national consensus on economic, social, and security priorities. Reflecting this, the government's economic program rests on three main pillars: macroeconomic stability; financial sector restructuring; and structural reforms to boost growth and reduce poverty.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

A key objective of the program is to keep the fiscal deficit below 2 percent of GDP. Within this framework, the government is seeking to mobilize additional fiscal resources to finance a significant increase in public investment and social spending.

Monetary policy is being geared to reducing inflation to the 4–6 percent range. The exchange system is flexible, but the central bank has intervened in the foreign exchange over the past year to contain the appreciation of the quetzal against the U.S. dollar. In January 2005 a rules-based mechanism for interventions was introduced.

The Guatemalan banking system has been strengthened in recent years. Prudential norms have been tightened and the offshore banks have been brought into the regulatory framework.

The government's structural reform program, *Vamos Guatemala*, is focused on promoting competitiveness, economic growth, and social progress. Steps have been taken to foster a business climate characterized by transparency, the rule of law, and good governance; a Commissioner for Competitiveness has been appointed; and implementation of Dominican Republic-Central American Free Trade Agreement (CAFTA-DR) is expected to help underpin the recovery. Social spending will be increased, with a redoubling of the development effort in municipalities with the highest incidence of poverty.

**Executive Board Assessment**

Executive Directors commended the Guatemalan authorities' efforts to maintain macroeconomic stability and pursue structural reforms. The public debt has been kept low, international reserves have been strengthened, and the financial system has been made more robust. At the same time, economic growth has been sluggish, poverty remains widespread, and the momentum in strengthening the tax effort has weakened, with consequent declines in social spending. More generally, the economic and social objectives of the 1996 Peace Accords remain to be achieved.

Against this background, Directors welcomed the authorities' renewed commitment to achieving the objectives of the Peace Accords. The government has set forth a comprehensive and ambitious reform agenda in the *Vamos Guatemala* plan. Directors considered that, to realize the growth dividends of the reform agenda, fiscal reform measures should be supported by prudent monetary policy to control inflation, while structural reforms should aim at increasing competitiveness and enhancing the investment climate. They welcomed the envisaged efforts to fight corruption and improve the transparency of government operations, which will help build trust in public institutions and partnership with the private sector, and solidify public acceptance and support for the reform agenda. Directors encouraged the authorities to continue their commendable efforts to promote a public dialogue and to garner the necessary ownership and consensus for faster implementation of the government's reform program.

Directors regretted the decline in the tax revenue-to-GDP ratio since 2002, which has set back the achievement of the Peace Accord goal of raising tax revenue to 12 percent of GDP. Additional revenues are needed to finance well-targeted social programs and pressing investment needs that are crucial for achieving the country's development priorities. Directors supported the ongoing work to strengthen tax administration, and welcomed the progress already evident in this area. However, they noted that strengthening tax revenues on a lasting basis will require congressional action on tax policy as well as some key tax administration measures. Directors underlined the importance of moving forward expeditiously with specification of measures aimed at strengthening revenues and improving the quality of the tax system, including by broadening the tax base and eliminating exemptions. They supported the government's active participation in efforts to strengthen cooperation on tax issues at the regional level.

Directors noted that Guatemala continues to face serious problems of poverty and income distribution, with most of its social indicators falling below the averages for Latin America. They accordingly welcomed plans to increase spending on social sectors from 2005, with a view to improving the quality of human capital, bolstering productivity growth, and alleviating social inequalities. Directors also called attention to the importance of improving the quality of public spending and strengthening public expenditure management. Key steps planned by the authorities include extending coverage of the Integrated Financial Management System to lower levels of government, and initiating a review of the long-term financial viability of the pension system.

Directors encouraged the central bank to focus on the goal of achieving low inflation. They agreed that the authorities should strengthen their flexible exchange rate regime, which remains appropriate for Guatemala. They recommended that foreign exchange market intervention be limited to smoothing excessive short-term volatility. Directors took note of the authorities' desire to prevent an abrupt appreciation of the quetzal, and welcomed the authorities' intention to pursue a broadly symmetrical intervention policy, also dampening excessive depreciation, as needed. At the same time, Directors considered that a strengthening of external competitiveness would be best achieved by actions to raise productivity, reduce infrastructure bottlenecks, and maintain a prudent fiscal policy. They supported the ongoing work aimed at adopting inflation targeting as the framework for monetary policy. Directors looked forward to further analysis of the implications of the sizable flows of private capital and remittances for monetary and exchange rate policies.

Directors welcomed the emphasis in the authorities' program on policies to increase growth, improve competitiveness, and foster a good business climate. This will require more open and competitive markets, the rule of law, and good governance. Directors were particularly encouraged by Guatemala's early ratification of the free trade agreement with the United States (CAFTA-DR), which will help Guatemala secure broad and stable market access to its main trading partner and provide an anchor for the implementation of growth-oriented institutional reforms. Such reforms should help attract new private investment and strengthen the position of the traded goods sector as Guatemala faces growing international competition, including from the recent expiry of quotas on world trade in textiles.

Directors were encouraged by the significant progress on financial sector reforms since the last consultation, in particular the steps taken to bring the offshore banks into the regulatory framework. They encouraged the authorities to address remaining vulnerabilities, including through steps to reduce bank lending to related parties, build general provisions, and deal with the persistent losses of the state mortgage bank (CHN), in line with the Financial Sector Assessment Program recommendations. Directors urged the authorities to persevere with implementation of anti-money laundering legislation and to update combatting-the-financing of terrorism legislation. The authorities were also encouraged to monitor closely any risks stemming from dollarization in the banking system.

Directors welcomed the steps taken by the authorities to strengthen macroeconomic statistics, including Guatemala's recent accession to the General Data Dissemination System. Further work is needed to address weaknesses in the national accounts, the balance of payments, and the data on non-budgetary fiscal transactions.

Directors considered that Guatemala's medium-term economic outlook is favorable under strong policies, albeit not without risks. The combination of low public debt, a strengthened banking system, a flexible exchange rate regime, and adequate international reserves provides considerable room for maneuver in dealing with adverse shocks.

***Public Information Notices (PINs)*** form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Guatemala: Selected Economic and Financial Indicators

| | 2001 | 2002 | 2003 | Prel. 2004 | Proj. 2005 |
|---|---|---|---|---|---|
| **Real economy (percentage change)** | | | | | |
| Real GDP | 2.3 | 2.2 | 2.1 | 2.7 | 3.2 |
| Consumer prices (end of period) | 8.9 | 6.3 | 5.9 | 9.2 | 6.0 |
| **Public finances (percent of GDP)** | | | | | |
| Consolidated public sector deficit | -2.3 | -0.8 | -2.0 | -0.4 | -1.7 |
| Nonfinancial public sector debt (end of period) | 17.1 | 15.5 | 17.1 | 18.0 | 17.8 |
| **Money and credit (end-year, percentage change)** | | | | | |
| Credit to the private sector | 12.5 | 6.1 | 7.3 | 16.2 | 11.2 |
| Liabilities to the private sector | 8.1 | 13.2 | 11.0 | 11.4 | 14.1 |
| **Interest rates (domestic currency time deposits)** | 11.3 | 9.6 | 6.7 | 6.9 | ... |
| **External sector** | | | | | |
| External current account balance (percent of GDP) | -6.0 | -5.3 | -4.2 | -4.4 | -4.4 |
| Change in net international reserves (millions of U.S. dollars, increase -) | -499 | 23 | -521 | -581 | -275 |
| Gross international reserves (in months of next year imports of goods and services) | 4.0 | 3.7 | 4.0 | 4.4 | 4.6 |
| Terms of trade (percentage change) | -1.0 | -2.5 | -4.4 | 1.0 | -0.5 |
| Real effective exchange rate (end of period) 1/ | 3.2 | 8.3 | -1.9 | 7.5 | ... |

Sources: Bank of Guatemala; Ministry of Finance; and IMF Staff estimates and projections.

1/ End-period; a positive change indicates an appreciation.

**Statement by Moises Schwartz, Executive Director for Guatemala and Gerardo Peraza, Senior Advisor to Executive Director May 16, 2005**

On behalf of our Guatemalan authorities, we thank management and staff for the continued support and advice to the country. Guatemala maintains a close dialogue with staff and benefits from intensive technical cooperation in several key areas of the government agenda. The authorities broadly agree with the staff's appraisal.

Immediately after taking office in early 2004, the authorities made a priority to restore credibility in public institutions, fiscal discipline and consequently market confidence. They re-launched the 1996 Peace Accords and made them the cornerstone of the government's policy framework. In May 2004, the government launched a comprehensive plan to strengthen tax administration and tax enforcement. A month later, despite facing a fragmented congress, the government secured the passage of a tax reform to revert the impact of court rulings that threatened to erode the tax base. The authorities are determined to raise revenue collection as envisaged in the Accords to increase significantly the spending on health, education, and justice and to put Guatemala on track to achieve the Millennium Development Goals. The authorities have also made the fight against corruption and promotion of transparency central themes in their policy agenda.

In 2005, the government seeks to maintain the momentum of the recovery by preserving the macroeconomic stability—underpinned by fiscal consolidation, lowering inflation, improving the business climate, and structural reforms focused on strengthening competitiveness and maximizing the potential benefits of trade agreements. Clearly, the economy is still vulnerable to external shocks but the authorities are confident that the envisaged measures will make the country more resilient to those shocks while strengthening its competitiveness.

Thus, 2004 marked a clear turnaround in economic performance. Real per capita GDP stabilized after three years of consecutive decline. Real output growth accelerated to 2.7 percent despite the negative impact of higher oil prices and a sharp contraction in government spending. Fostered by a stronger foreign demand and increased domestic confidence, this recovery reflected mainly buoyant goods exports and a sharp rebound in private investment. Rising family remittances also supported a solid growth in private consumption and imports. Net international reserves climbed to US$3.5 billion (US$2.9 billion in 2003), about 5.1 months of imports or 5.2 times the external service on short-term public debt. Inflation closed at 9.2 percent (5.8 percent in 2003) owing largely to high international oil prices, a build up of excess liquidity since mid-2003, and uncertainty related to the delays in the fiscal budget process. Thanks to a prudent policy mix of gradual monetary tightening, and austere fiscal stance, the government eliminated excess liquidity balances by the end of the year. Since then, inflation has started to fall reaching 8.9 percent by end-April 2005.

The budget deficit was reduced sharply in 2004 to 0.3 percent of GDP, from 2.3 percent in 2003. This reduction reflected those actions to revert the impact of court-ordered tax reductions and strict spending policies without affecting social spending allocations. The June 2004 tax package included a temporary tax to support the peace agreement (IETAAP)[1] and excises on alcoholic beverages, established a 5 percent turnover tax as an alternative to the corporate income tax, and introduced a minimum tax provision in the corporate income tax that will remain in effect after the IETAAP is phased out by 2007. The fiscal target for 2005 of 1.8 percent of GDP takes into account a sharp rebound in public investment, and an increase in social spending by about ½ percent of GDP. To mobilize the necessary resources the authorities will seek approval by Congress of a set of structurally sound revenue measures that will raise tax collections to 12 percent. On the tax administration front, the Superintendency of Tax Administration (SAT) has drawn up a detailed strategic plan which incorporates 106 points of action identified with technical advice from FAD.

The authorities share staff's views of the potential benefit of advancing the timetable for their reforms. However, they would like to reiterate that the pace of implementation is constrained by the need to build support for key elements of their agenda, particularly those related to revenue mobilization. In this context, the authorities have designed a well-focused strategy, including a public education and consultation campaign, to link achievement of the Millennium Development Goals and the Peace Accords objectives to the mobilization of additional fiscal resources. The funding requirement and the accompanying measures that will be identified in this process will be sent to Congress as soon as consensus is reached on their implementation. The corresponding revenue measures will be calibrated to take account of the resources being generated under the tax administration plan.

At 18 percent of GDP in 2004, Guatemala's public debt is one of the lowest in the region. Since taking office, the government has adopted a number of measures to guarantee that the debt outlook continues to be robust. The authorities have lengthened the maturity structure of its domestic and external debt and have begun to reduce the foreign currency component of its domestic debt. In September 2004, a US$330 million 30-year Eurobond was placed at a spread of 300 bps, the lowest spread and longest maturity of any Guatemalan sovereign debt placement. By late-April 2005, the government had almost completed its financing requirement for the year mostly through local placements of bonds in domestic currency in maturities of 5 and 10 years at 9 percent for the longest maturity. The placement reflected not only favorable global liquidity conditions but also renewed confidence in government market-oriented policies.

Like other emerging economies suffering from global imbalances, Guatemala is facing sizeable inflows of private capital and remittances that together with higher oil prices have made more challenging the management of monetary and exchange rate policies. The authorities plan to maintain their policy mix together with central bank intervention in the foreign exchange market to prevent excessive appreciation of the quetzal. Since last year, the

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[1] In essence a presumptive minimum corporate income tax.

central bank has increased its placement of open market paper and raised its benchmark interest rate on several occasions—more recently in February 2005—to minimize the second round effects derived from the high oil prices. The public sector has indeed provided an important supporting role by maintaining larger than anticipated deposits at the central bank. In addition, the central bank will continue intervening in the foreign exchange market only to prevent excessive exchange volatility through the nondiscretionary rule introduced early this year. The decline in inflation so far this year supports the view that the policy mix is adequate and that in the absence of new shocks inflation will converge to the upper limit of the central bank's target range of 4-6 percent. The Bank of Guatemala will continue its efforts to adopt inflation targeting as the framework for its policy, and it is thankful for the valuable technical assistance received from the Fund's MFD department.

On financial sector issues, the authorities remain committed to the implementation of the plan launched in 2001 (in line with the recommendations in the FSSA) to strengthen the financial system and ensure that it provides the basis for sound macroeconomic management and support economic growth. A new legal and regulatory framework approved in 2002 has strengthened supervision of the system and helped improve the performance and solvency of banks. On average, Guatemalan banks remain well capitalized with NPL at record low and stronger net open position. Looking forward, the authorities will focus on remaining vulnerabilities such as: (i) addressing the persistent losses of the CHN; (ii) assessing the need to tighten related party lending and the introduction of general provisions; (iii) recapitalizing the central bank; and (iv) the payment system. In addition, given the importance of cross-border lending and financial integration in Central America, Guatemala will seek convergence of banking regulations and prudential norms in the region and welcomes Fund's current work on this area.

The government is also committed to recapitalize and reinforce the central bank. The approved budget for 2005 included a bond at market interest that will cover the central bank losses for 2003 (about 0.5 percent of GDP). In addition, during the second half of the 2005, the government will re-submit to Congress a request to approve the issuance of a long-term zero-coupon bond equivalent to the stock of central bank losses that had been accumulated up to end-2001. On the central bank's lender-of-last resort facility, the government introduced in March 2005 new regulations to complement and clarify the framework contained in the 2002 Organic Law of the central bank.

The authorities will implement a program of structural reforms to strengthen Guatemala's competitive position and make the economy more resilient to shock. In 2004, the government appointed a Commissioner for Competitiveness to promote exports and investment, focusing on issues of infrastructure, administrative and regulatory impediments and other institutional factors to enhance the investment climate. The government has been pursuing deeper economic integration with Central America, and will seek harmonization of fiscal incentives among the Central American countries as the region tries to attract FDI in the context of CAFTA-DR. Guatemala will also benefit from the extension of the EU's Generalized System of Preferences (GSP).

The authorities are determined to address the structural obstacles that still hamper economic growth and social progress in Guatemala, and will foster a business climate characterized by transparency, good governance and the rule of law. In addition to the measures described in paragraph 13 of the staff report, the authorities are seeking to adopt a judicial framework that is fully consistent with the Inter-American Convention Against Corruption. A number of initiatives are already under way to prevent corruption practices, such as the revision of the civil service law, stricter norms for contracts with states, and reforms to the penal code with more severe sanctions for bribery and illicit enrichment.

Finally, the authorities have launched a program (Vamos Guatemala) focused on growth and competitiveness with a special emphasis on social progress. They have restructured the budget to ensure that public spending is targeted to the priorities of the program. Under the social component (Guate Solidaria) for instance, the government will promote economic development by focusing in municipalities with the highest incidence of poverty. These objectives are designed to foster participatory socioeconomic development by focusing on education, health, housing, and justice. This program has been initiated in 41 municipalities with vulnerable population and unsatisfactory nutritional standards. Key components of the program are based on partnership with the private sector, and the government is enlisting support from the multilateral development agencies, including sector loans from the IDB and the World Bank.