EXECUTION COMMITTEE

ACT NUMBER 2-2006

Session 2-2006 celebrated in the *Banco de Guatemala* building on Friday, January thirteenth, two thousand six, at fifteen hours and thirty minutes.

The coordinator, with the corresponding quorum, for the consideration of the Execution Committee submitted the project for the order of the day.

FIRST: Approval of Project for acts number 1-2005, corresponding to the session celebrated on January 61, 2006.
(The project of the act circulated.)

SECOND: Market information and monetary variables.

a) Money and Exchange markets.
b) Monetary Variables

THIRD: Balance of Inflation risks

FOURTH: Analysis of the monetary situation and definition of the guidelines of execution for the Monetary, Exchange and Credit Policy for the following week.

FIFTH: Other matters.
Not having more observations, the committee approves the order of the day.

FIRST: The coordinator has put to consideration the corresponding project act.
Not having any observations, the committee approved acts number 1-2006.

SECOND: Information of markets and monetary variables.

The coordinator requested that the corresponding information be presented.

a) The Director of the Department of Monetary Stabilization Operations, regarding the Money market informed that during the period from January 9 to 13 of 2006, with partial numbers to date, registered an attraction of LTD's for Q3,507.3 million and maturity of Q2,675.8 million, which gave a net result of fund raising for Q831.5 million, associated to the operations in bidding (net attraction for Q17.5 million), in the Money Electronic Banking Table –MEBD- and in the stock exchange (net fund raising of Q885.0 million) and at the window (net maturity for Q71.0 million).

Regarding the interest rates applied in fund raising through LTD's, it was indicated that during the period of January 9 to 13, 2006 for the biddings case, the cut interest rates were of: 5.00% for 91 days, 6.25% for 364 days. On the other hand, in the MEBD and in the stock exchange the fund-raising took place for 7 days, at the leading interest rate of the monetary policy of 4.25%.

As for the weighted average interest rates of total operations of repurchase agreements made in the stock exchange of the country, it was indicated that, during the January 9 to 13, 2006 period, with partial data, the minimum was of 4.31%, observed January 10, 2006, and the maximum of 4.62%, registered on January 12, 2006. It also pointed out that the amounts negotiated were higher with public titles and that the average weighted interest rates during said period were of 4.47% for public titles and of 5.31% for the financial sector titles.

On the other hand, it was informed that during the January 9 to 12, 2006 period, regarding Treasury Bond operations the fund-raising registered was for Q52.5 million and maturity for Q20.5 million and US$5.8 million.

Regarding the Institutional Market for foreign currency the report stated that during the period of January 6 to 12, 2006, the average daily operations for purchase were of US$63.4 million and the sale was of US$61.9 million as the exchange rates showed a tendency toward the low. In effect, on Friday, January 6 they were of Q7.63653 per US$1.00 for purchase and of Q7.66406 per US$1.00 for sale, on Monday, January 9 the rates were Q7.62889 and Q7.65893, on Tuesday, January 10 they were Q7.63423 and Q7.65442, Wednesday, January 11 they were Q7.62944 y Q7.64870, and finally, on Thursday, January 12 they were Q7.62735 y Q7.64351.

In the operations of the electronic systems of negotiations of foreign currency administered by the *Bolsa de Valores Nacional, S.A.* (National Stock Exchange, S.A.), for the period of January 6 to 12, 2006, commented that the Private Institutional Foreign

Currency System –SPID-, the operations took place s follows: on Tuesday, January 10, there was an operation for US$2.0 million, at a weighted average exchange rate of Q7.61500 per US$1.00 and on Thursday, January 12 for US$1.00 at Q7.64100 per US$1.00. Regarding the Electronic Foreign Currency Negotiation System –SINEDI-, they declared that during the period no operations were closed and only the *Banco de Guatemala* received daily, a bid for the purchase of US$10.0 million, with the following prices: January 6 and 9 of Q7.58900, on January 10 of Q7.59477, on January 11 of Q7.60146 and on January 12 of Q7.60498, according to the guidelines of the Execution Committee.

On the other hand, they informed that the Future Foreign Currency Market that is operated by the National Stock Exchange, S.A., during the period of January 9 to 13, 2006, did not close operations. As for the closing price in reference up to Friday, January 13, they indicated that for maturity to liquidate in March of 2006 the price was Q7.66000, and for the maturity to liquidate in June of 2006 it was of Q7.66000.

b) The director for the Economic Studies Department informed that on January 12, 2006, the excess of the daily float of the banking system was located in a position of Q764.1 million, with an average position of Q520.5 million.

The highlights during the period of January 5 to 12, 2006, the main demonetizing factors were the increase in balance the long term deposits constituted in the *Banco de Guatemala* for Q687.7 million, the banking float balance for Q212.8 million and the deposits for the Central Government in the *Banco de Guatemala* for Q62.8 million; while the main monetizing factors were the decrease in the balance of the deposits of the rest of the public sector in the Central Bank for Q148.7 million and the increase in the Net International Reserve –RIN- balance for the equivalent of Q754.4 million.

Regarding the indicative variables of the Monetary, Exchange and Credit Policy they indicated that with the projection to October for December of 2006 the total inflation estimated with a model of ordinary squared minimums is of 7.54% and with a softened exponential model of 7.34%; the simple average of both models is located at 7.44%, which is above the policy goal (6.0%), which suggests a restrictive monetary policy.

Regarding the expected subjacent inflation for 2006, with data up to December 2005, estimated with an integrated auto-regression model of mobile averages ARIMA was of 7.24%, whereas the estimated with a softened exponential model it was of 6.33%; the simple average of both models is of 6.79%, which is above the policy goal (6.0%), which suggests a restrictive monetary policy.

As to the parameter rate, up to January 5, 2006, the lower limit was 1.45%, and the upper limit is 9.35%, while the simple average between the repurchase agreements of 8 to 15 days (5.74%) and the weighted average rate of open market operations –OMA- of up to 91 days (4.57%) was situated at 5.16%, which is located within the estimated for the parameter rate, situation that suggests an invariable monetary policy. When referring to the parity passive rate, they declared that up to January 5, 2006, the lower limit was 5.85% and the upper limit was 7.43%, and the weighted average rate of long term deposits of the banking system was of 6.93%, which maintains itself within the fluctuation range of the parity passive rate, which advises an invariable monetary policy.

As to monetary issue observed to January 12, 2006, they indicated that it presents a deviation of Q472.8 million according to the upper limit programmed for said variable, which would indicate that there is space available to restrict the monetary policy.

As to the total payment means, to January 5, 2006, it exhibited an inter-annual growth rate of 14.4%, which is within the estimated range for said variable on that same date (14.1% to 16.1%), which advises the monetary policy to remain invariable. Also, up to said date, the banking credit to the private sector registered an inter-annual growth rate of 21.6%, which is above the upper limit of the estimated range for January 5, 2006 (22.0% to 24.0%), which suggests relaxing the monetary policy.

As to inflation expectations of private analysts, they indicated that according to the poll made in December of 2005, for December of 2006 an inflationary rhythm of 8.78% is expected, which is above the goal for monetary policy (6.0%), an aspect which suggests restricting monetary policy. Also it was indicated that the new implied inflation expectations, for December, 2005 showed an inflationary rhythm of 5.55%, which is within the goal range for 2005 (4% to 6%), which suggests an invariable monetary policy.

They mentioned that the Monetary Conditions Index –ICM-, to January 5, 2006, was -3.14 percentage points which is within the range estimated for said variable on that date (-3.71 to -2.11 percentage points), which advises that monetary policy should remain invariable.

To conclude this report, regarding the orientation of the indicative variables; it was reported that regarding last week, the “parameter rate” and “banking credit to the private sector” variables went from suggesting that the monetary policy be restrictive to suggest it remain invariable and to relax it. Also adding to the number of variables the indicative variable “implied inflation expectations”, whose orientation is to maintain the referred policy invariable, which decreased the variables to four that suggest restricting the monetary policy (the total inflation projection, the subjacent inflation projection, the inflation expectations of private analysts and monetary issue); there was an increase to five variables that suggest the monetary policy remain invariable (parity passive rate, Monetary Conditions Indexes, implied inflation expectations, the total payment means and parameter rate); and one suggests to relax it (the banking credit to the private sector).

On the other hand, the information of the Consumer Price Index to December, 2005, reported by the National Statistics Institute –INE- (the monthly inflation was of -0.04%, lower by 0.08 percentage points to that of November, 2005; the inflationary rhythm was at 8.57%, lower by 0.68 percentage points to that of November, 2005 and lower by 0.66 points than the observed in December, 2004; the subjacent inflation registered a rhythm of 7.74%, lower by 0.29 percentage points to that of November, 2005 (8.03%) and lower than that of December 2004 (8.41%)); as well as the estimations of the imported and domestic inflation components (of 8.57% of the inflationary rhythm to December, 2005, 2.21 percentage points are attributable to the imported inflation, where at the same time, 1.36 percentage points corresponded to the indirect imported inflation (second-round effect); therefore, the inflationary rhythm, 6.36 percentage points correspond to domestic inflation).

THIRD: Preliminary Inflation Risks Balance.

The Economic Manager, with the purpose of counting on information to sustain the decision to be adopted by the Monetary Board in its session celebrated on Wednesday, January 25, 2006, regarding the elevation or to maintain the leading interest rate of the monetary policy, referred to the partial inflation risks balance with data to December 2005, prepared by the technical department, emphasizing on the following aspects:

As to outer conditions, it was indicated that the behavior of international oil prices observed an increase regarding the observed in the session of the Execution Committee on December 16, 2005, therefore said variable will continue being the main inflationary risk in Guatemala in 2006, even though in lower magnitude than in 2005. It was indicated that the external inflationary impact will continue to be a risk whereas the compound interest of inflation of the main commercial partners of Guatemala continues to be high. In effect, it was declared that the inflationary rhythm of the United States of America (country with the highest relative weight within the index) accelerated when surpassing 2.75% in 2004 to 3.37% in 2005. In that sense, it was indicated that the compound inflationary rhythm of the main commercial partners of the country –weighted by the commercial structure of Guatemala with each one of them-, to December, 2005 was located at 4.08%, higher to that of December, 2004 (3.97%), therefore through this, to December, 2005, the imported inflation risks had not improved. However, a deceleration is foreseen for the referred index in 2006 to 3.80%, which would indicate that even though an inflationary risk persists, this would be moderating this year.

Regarding some of the macroeconomic variables of the United States of America, according to the projection by Global Insight, the federal funds objective interest rate in the first trimester is expected to reach at least 4.50%, pointing out that this is associated with a slight deceleration in the economic activity of said country in 2006 from 3.70% to 3.60%, with which the analysts foresee that greater adjustments in the interest rate over 4.50% could have a noxious effect in the added demand. Also, another factor mentioned was that the international analysts project greater inflation for the referred country in the first trimester of 2006 (from 3.50% to 3.70%), which associated to a lower growth rate can induce greater unemployment rates.

As to internal conditions, it was indicated that between January 1 and 13 of this year, in the private sector the level of monetary stabilization of operations has been situated below the programmed by about Q309.1 million. On the other hand, the behavior of the deposits by the Central Government in the *Banco de Guatemala* at the beginning of the year were slightly above the programmed, situation that reverts itself in the following five days when it was below the programmed level, and that was then compensated on January 12, due to the increase associated by the disbursement of the loan contracted by the

Government of the Republic mediated by the *Ministerio de Finanazas Públicas* (Equivalent to the Department of the Treasury), with the World Bank for US$99.7 million.

As to the indicative variable, it was indicated that to the date the restrictive bias of the variables reported that suggest that the monetary policy be restricted decreased regarding the observed on December 16, 2005 from six to four (the projection of total inflation, the projection of subjacent inflation, the expectations of inflation by private analysts and monetary issue), one variable suggested relaxing the monetary policy (the banking credit to the private sector) and the variables that suggest the monetary policy remain invariable increased form three to four (the parity passive rate, the parameter rate, the total payment means and the Monetary Conditions Index).

The econometric projections prepared by the technical departments, using data observed to December, 2005, estimate average inflation of both methods for December 2006 and December 2007 above the fixed goal (6% for 2006 and 5.0% for 2007) when located at 7.44% and 7.16%, respectively. Also, it was indicated that the inflation expectations for December 2006, are located at 8.78%.

FOURTH: Analysis of the monetary situation and definition of the guidelines of Monetary, Exchange and Credit Policy execution for the following week.

a) Analysis of the monetary situation

The Committee took note that the monetizing and demonetizing factors previewed for the week of January 13 to 19, 2006 indicate an increase in the creation of primary liquidity for Q3, 088.8 million, fundamentally due to the maturity of LTD's. Also, an increase is foreseen for the demand for monetary issue for Q113.5 million and a daily position of banking liquidity for January 19, 2006 for Q. 678.9 million. Also, that the monetary issue is deviated in Q655.4 million above the central programmed point for said variable, therefore the excess of added liquidity for the referred period is located at Q4, 536.6 million; if these factors are given, the Committee considered that it would be necessary to make the issue offer compatible with the demand programmed, that the LTD's that expire during the period (Q3,202.2 million, according to registries to January 5, 2006) have to be relocated; and also, make additional fundraising for around Q1,334.4 million.

Regarding the determination of quotas for biddings in the following week, the information provided for estimated daily flow of monetization for the following week and as an established rule for the effect. Also, the Committee was informed that the frame of the coordination of the placements with the representatives of the *Ministerio de Finanazas Públicas* (Equivalent to the Department of the Treasury), suggested that the pertinence of maintaining fund raising LTD's at terms greater than one year be reviewed. In that sense, with the end of maintaining an adequate coordination with the money market, the Committee agreed that the Central Bank not offer LTD's for periods longer than one year. Based on the above, the Committee agreed that for the following week the fund raising quota for the 91 and 364 day terms to be convened on Monday would be, established at Q75.0 million and Q60.0 million, respectively, for each term; and for the 182 day term to be convened Friday would be Q60.0 million.

Regarding the convening of bids for LTD's in US$ dollars, the Committee took note that for the following week there was important maturity of Treasury Bonds expressed in US dollars with residents, reason why it was agreed that for the week of January 16 to 20, 2006, bidding for LTD's in said currency was convened.

Based on the information received and taking into account the preliminary balance of the inflation risks presented by the technical corps of the Bank, the Committee began the discussion on the analysis that must be presented by the Monetary Board in its session of Wednesday, January 25, 2006 when, according to the calendar programmed, the Board will take a determination as to the level of the leading interest rate of the monetary policy. For the effect, the factors that advise an elevation of the leading interest rate for the monetary policy were presented, as well as those that advise to keep it invariable.

As to the factors that advise elevating the leading interest rate; the following were mentioned:

i) Notwithstanding that, according to the analysis made by international experts, in 2006 there are no abrupt hikes expected in the international price of oil; the behavior of said price is still the main inflationary risk in Guatemala.

ii) The operations of monetary stabilization, to date, are located below the foreseen level in the monetary program.

iii) According to the econometric projections made by the technical departments, the expected inflation for 2006, subjacent as well as total, are located above the goal foreseen for the present year.

On their part, regarding the factors that advise maintaining the leading interest rate invariable are the following:

i) The inflationary rhythm, total as well as subjacent, observed in December were reduced regarding the previous month.

ii) The econometric projection of the total inflationary rhythm as well as the subjacent decreased regarding the previous month. Also, the inflation expectations of the panel of private analysts obtained in the December survey are less than the obtained in the November survey.

iii) The number of indicative variables that advise restricting the monetary policy were reduced from six to four regarding the observed on December 16 (last date the leading interest rate was adjusted). Notwithstanding, some members of the Committee indicated that this change must be made cautiously, due to the form in which the expected trajectory of the inter-annual growth rate of payment means and credit to the private sector were calculated; also, they pointed out that due to the fact that in 2005 the central point of the inflation goal was 5%, so much so that for 2006 the punctual goal of inflation is of 6%, the indicative variables “Parameter Rate” and “Monetary Conditions Index” can be given an artificial sense that the monetary policy is now far from the zone where it suggests greater restriction.

Taking into account the above, the heart of the Committee continued to agree that it is necessary to continue analyzing the mentioned factors, and requested the technical departments continue investigating on the indicated aspects, as well as those that would surface, on the one hand, on the information that complements the definitive balance of inflation risks and, on the other hand, the initial conditions of the semi-structural model, in order that in the next session the Committee aligns conclusions that will be submitted to consideration in the Monetary Board on January 25, 2005.

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

Based on the monetary situation analysis, the Execution Committee agreed that for the week of January 16 to 20, 2006, they would maintain the execution guidelines for the monetary policy observed during the present week; in other words, continue to operate in MEBD and in the Stock exchange, in raising funds as well as in giving liquidity to the market. The raising funds operations will be 7 day terms without quota, at an interest rate of 4.25%, whereas, the offer position of liquidity at 7 day terms, with an initial interest rate of 7.65%, whose guarantee of said operations will be constituted by receiving public titles, only. It is worth mentioning that the Committee stressed the importance of participating in both venues; in other words, maintaining simultaneous positions of giving liquidity to the market and liquidity withdrawal, considering said participation constitutes a sign of disposition of the Central Bank to moderate the volatility of the short term interest rate.

The Committee, taking into consideration the agreed with the fiscal policy to participate in the money market, agreed that the calling for biddings for term deposits would take place on Mondays and Fridays; so Monday for 91 and 364 day terms, with a raising funds quota of Q75.0 million and Q60.0 million, respectively, for each term; and Friday for 182 day term, with raising funds quotas for Q60.0 million. The interest rates would be determined according to the market conditions, reflected in the positions received, considering the established yield curve by the technical department.

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

On the other hand, the Committee agreed to summon biddings for term deposits in US dollars –DP in US$-, on Wednesday January 18, 2005, the 91 and 364 day terms, for an amount of up to US$30.0 million. The bids received can be awarded taking as a reference the interest rates of the Treasury Letters of the United States of America in similar terms, without excluding the possibility that, if the bids received deserve better rates, a session with the Committee will be convened to decide its awarding. Also, it awarded the General Manager of the *Banco de Guatemala* with the authority, so that, as of the bids on January 18, 2006; he can award the amounts requested on the 91 and 364 day bids, the reference interest rate indicated, as long as they are within the established quota.

The Committee agreed to continue accepting the constitution of term deposits in United States dollars directly at a window, from public entities, in current terms of (91 days and 364 days) and that the interest rate applied would be the resulting weighted average from the last awarded bidding for long term deposits in said currency.

As for the participation of the *Banco de Guatemala* in the Exchange market, the Committee agreed that it should continue participating in the SINEDI through participation rules established in session 55-2005 dated October 27, 2005.

FIFTH: Other matters.

Not having any other matter to see, the session ends at seventeen hours, all who attended sign in agreement.