EXECUTION COMMITTEE

ACT NUMBER 20-2006

Session 20-2006 celebrated in the *Banco de Guatemala* building located at *séptima avenida número veintidós guión cero uno, zona uno* of this city on Friday, May 12, two thousand six, at sixteen hours and thirty minutes.

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

FIRST: Approval of Project for act number 19-2006, corresponding to the session celebrated on May 5, 2006, respectively.
(The project of act 19-2006 circulated.)

SECOND: Market information and monetary variables.

a) Money and Exchange markets.
b) Monetary Variables

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

FOURTH: Other matters.

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

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

Not having any observations, the committee approved act number 19-2006.

SECOND: Information of markets and monetary variables.

The coordinator requested the following information be provided.

a) The Sub-director of the Department of Monetary Stabilization Operations, regarding the Money market informed that during the period from May 8 to 12 of 2006, with partial data to date, registered an attraction of LTD's for Q2,324.8 million and maturity of Q1,760.2 million, which gave a result of net fund raising for Q564.6 million, associated to the operations in bidding (net maturity for Q116.5 million), in the Money Electronic

Banking Table –MEBD- and in the stock exchange (net fund raising of Q696.0 million) and at the window (net maturity for Q14.9 million).

Regarding the interest rates applied in fund raising through LTD's, it was indicated that during the period of May 8 to 12, 2006 for the biddings case, the cut interest rates were of: 4.9998% for 91 days. On the other hand, in the MEBD and in the stock exchange the fund-raising took place for 7 days, at the leading interest rate of the monetary policy of 4.50%.

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 May 8 to 12, 2006 period, with partial data, the minimum was of 4.38%, observed May 12, 2006, and the maximum of 4.6998%, registered on May 11, 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 4.51% for the public titles and of 5.47% for the titles of the financial sector.

On the other hand, it was informed that during the May 8 to 11, 2006 period, regarding Treasury-Bond operations the fund-raising registered was for Q13.5 million and maturity for Q0.1 million.

As to deposits in US dollars convened on May 10, 2006, it was mentioned that no bids were required.

Regarding the Institutional Market for foreign currency the report stated that during the period of May 5 to 11, 2006, the average daily operations for purchase were of US$64.1 million and the sale was of US$70.3 million and that the exchange rates in the referred period remained stable. In effect, on Friday, May 5 they were of Q7.56867 per US$1.00 for purchase and of Q7.58582 per US$1.00 for sale, on Monday, May 8 the rates were Q7.56593 and Q7.58457, on Tuesday, May 9 they were of Q7.56930 and Q7.58337, on Wednesday, May 10 they were Q7.56715 and Q7.58369, and finally, on Thursday, May 11 they were Q7.56969 y Q7.58524.

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 May 8 to 12, 2006, it was commented that the Private Institutional Foreign Currency System –SPID-, the following operations were made: on Thursday, May 11 for

US$0.4 million, at a weighted average exchange rate of Q7.58213 per US$1.00 and on Friday, May 12 of US$0.2 million for Q7.58750. Regarding the Electronic Foreign Currency Negotiation System –SINEDI-, expressed that during the period the *Banco de Guatemala* made the following purchases: on Monday, May 8 for US$17.0 million, at a weighted average exchange rate of Q7.58129 per US$1.00, and on Tuesday, May 9 for US$7.0 million, at Q7.58000, according to the guidelines of the Execution Committee.

On the other hand, they informed that the Future Foreign Currency Market that is operated by the National Stock Exchange, S.A., during the period of May 8 to 12, 2006, did not close operations. As for the closing price in reference up to Friday, May 12, they indicated that for maturity to liquidate in June of 2006 it was of Q7.61000.

b) The Director for the Economic Studies Department informed that on May 11, 2006, the excess of the daily float of the banking system was located at Q3.1 million, with a average position of Q275.7 million.

The highlights during the period of May 4 to 11, 2006 the main demonetizing factors were the increase in the balance in the long term deposits constituted in the *Banco de Guatemala* for Q719.0 million and the deposits of the Central Government in the *Banco de Guatemala* for Q277.6 million; while the main monetizing factors were the decrease in the banking float balance for Q714.6 million and the deposits of the rest of the public sector in the Central Bank for Q108.7 million; and, the increase in balance of the Net International Reserve –RIN- balance for the equivalent of Q128.8 million.

Regarding the indicative variables of the Monetary, Exchange Rate and Credit Policy they indicated that with the projection to April 2006, for December 2006 the total expected inflation estimated with a model of ordinary squared minimums is of 7.55% and with a softened exponential model of 7.32%; the simple average of both models is located at 7.44%, which is found within the margin of tolerance (6.0% +/- 1 percentage point), which suggests the monetary policy remain invariable; and, for December 2007 the total expected inflation, estimated with an ordinary squared minimum model, is of 7.75% and with a softened exponential model of 6.22%; the simple average of both models is at 6.99%, which is over the expected policy goal (5.0% +/- 1 percentage point), which suggests a restrictive monetary policy.

Regarding the expected subjacent inflation for 2006, with data up to April 2006, estimated with an integrated auto-regression model of mobile averages ARIMA was of 6.89%, whereas the estimated with a softened exponential model was of 6.46%; the simple average of both models is of 6.68%, which is within the margin of tolerance for the policy goal (6.0% +/- 1 percentage point), which suggests the monetary policy remain invariable; and, for December 2007 the estimated inflation with an integrated autoregressive model of mobile averages ARIMA, was of 7.01%, whereas the estimated softened exponential model was of 5.99%.; the simple average of both models is of 6.50%, which is located over the policy goal (5.0% +/- 1 percentage point), which suggests a restrictive monetary policy.

As to the parameter rate, up to May 4, 2006, the lower limit was 1.92%, and the upper limit is 9.82%; while the simple average between the repurchase agreements of 8 to 15 days (4.75%) and the weighted average of the monetary stabilization operations of up to 91 days (4.73%) was situated at 4.74%, which is located within the tolerance margin estimated for the parameter rate, situation that suggests the monetary policy remain invariable. When referring to the parity liable rate, they declared that up to May 4, 2006, the lower limit was 6.35% and the upper limit was 7.93%, and the weighted average rate of long term deposits of the banking system was of 6.99%, which maintains itself within the fluctuation range of the parity liable rate, which advises an invariable monetary policy.

As to monetary issue observed to May 11, 2006, they indicated that it presents a deviation of Q514.5 million regarding the upper limit programmed runner for said variable, which would indicate that there is space available to restrict the monetary policy.

As to the total payment means, to May 4, 2006, it exhibited an inter-annual growth rate of 15.5%, which is under the tolerance margin estimated range for said variable on that same date (16.0% to 18.0%), which advises relaxing the monetary policy. Also, up to said date, the banking credit of the private sector registered an inter-annual growth rate of 25.9%, which is within the range estimated for May 4, 2006 (24.1% to 26.1%), which suggests an invariable monetary policy.

As to inflation expectations of private analysts, they indicated that according to the poll made in April 2006, for December 2006 an inflationary rhythm of 7.54% is expected, which is above the goal for monetary policy (6.0% +/- 1 percentage point), an aspect which suggests restricting monetary policy; and, for December 2007, the inflation projection is located at 6.88%, which is over the monetary policy goal (5.0% +/- 1 percentage point), which suggests restricting the monetary policy.

Also it was indicated that the new implied inflation expectations, for April 2006 showed an inflationary rhythm of 6.44%, which is within a tolerance margin of the monetary policy for 2006 (6.0% +/- 1 percentage point), which suggests an invariable monetary policy.

They mentioned that the Monetary Conditions Index –ICM-, to May 4, 2006, was -2.66 percentage points which is within the fluctuation margin estimated for said variable on that date (-3.71 to -2.11 percentage points), which advises that the monetary policy should remain invariable.

To conclude this report, regarding the orientation of the indicative variables; it was reported that regarding the previous week, the "total inflation projection for 2006" went from suggesting that the monetary policy remain invariable to suggesting that the monetary policy be restricted and the variable "banking credit to the private sector" went from suggesting that the monetary policy be restrictive to remaining invariable. As a result, six variables suggest that the monetary policy be restrictive (the total inflation projection for 2006 and for 2007, the subjacent inflation projection for 2007, the monetary issue, and the inflation expectations of the private analysts for 2006 and for 2007); six variables advise the monetary policy remain invariable (the subjacent inflation projection for 2006, the parameter rate, parity liable rate, the banking credit to the private sector, the implied inflation expectations and the Monetary Conditions Index); and, one variable suggests the monetary policy relax (the payment means).

On the other hand, the information of the Consumer Price Index to April 2006 based on the report by the National Statistics Institute (INE) was presented (the monthly inflation was of 0.82%, higher by 0.34 percentage points to that of March 2006 and higher by 0.19 percentage points to that observed in April 2005; the inflationary rhythm was located at 7.48%, higher by 0.20 percentage points to the registered in March 2006 (7.28%) and lower by 1.40 percentage points to the observed in April 2005 (8.88%); the subjacent inflation registered a rhythm of 7.30%, higher by 0.07 percentage points to the observed in March 2006 (7.23%) and lower by 0.69 percentage points to that of April 2005 (7.99%)); as well as the estimations of the imported and domestic components of the total inflation (of the

7.48% inflationary rhythm to April 2006, 2.93 percentage points are attributable to the imported inflation, of which, at the same time, 2.21 percentage points correspond to the indirect imported inflation (second round effect); therefore, of the inflationary rhythm, 4.55 percentage points correspond to domestic inflation).

Finally, it was indicated that regarding the behavior of the nominal exchange rate, the center of the expected runner for the week of May 8 to 12, 2006 was of Q7.621 per US$1.00 and the observed level (calculated as the average of the exchange rates for purchase and sale in the institutional foreign currency market for the period between May 8 and 10) was of Q7.576 per US$1.00, which allows inferring that the observed value of the nominal exchange rate is found within the expected fluctuation band, but close to the lower limit, therefore in this light inflationary or deflationary pressures are not foreseen.

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

a) Analysis of the monetary situation

The technical departments presented some advances of the second running of the semi-structural model to the Committee. The purpose of the mentioned presentation was to obtain feedback from the Committee in order to have the necessary fine-tuning so that the inflationary prognosis in the mid-term would be empirically and theoretically consistent, and therefore give the final results to the Monetary Board in the next meeting in which a decision must be made regarding the leading interest rate of the monetary policy. On this matter, a member of the Committee suggested that among the results of the run of the model, a breach of product prognosis should be included (difference between observed product and the potential product), added to the implications of these on the growth of the economic activity.

Based on the information received, the Committee began a discussion on the analysis that must be presented to the Monetary Board in its session on Wednesday, May 24, 2006 when, according to the approved calendar, the Board will make a decision regarding the level of the leading interest rate of the Monetary Policy. For the effect, in the heart of the Committee the factors that suggest a raise to the referred interest rate as well as those that advise it remain invariable were analyzed; so that they are taken into account in the inflation risks balance that the technical departments will present to the Committee in the next meeting.

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

i) The behavior of the international price of oil is to rise, which continues to be the main inflationary risk in the country, given that for 2006 said price is expected to remain high. According to the last quote on the future price of oil, it increased to US$77.13 per barrel at the end of 2006, level which contrasts with the prevailing quote on April 21 (date in which the Committee discussed the level of the leading interest rate) that was of US$75.54 per barrel.

ii) The inflationary rhythm (total as well as subjacent) stopped the deceleration in February, presenting a change in tendency toward the rise as of March.

iii) The projections of the inflationary rhythms (total and subjacent) for December 2006 and 2007, based on the econometric methods, increased the regarding the projections made in March of the current year. It is worth indicating that for the first time in the year, the projection of the total inflation for December 2006 (7.44%) is located over the inflation goal determined in the monetary policy (6.0% +/- 1 percentage point).

iv) The number of the indicative variables that advise restricting the monetary policy, regarding the information presented in the April 21, 2006 session, increased from five to six, due to the fact that the total inflation projection for 2006 went from suggesting an invariable monetary policy to a restrictive one.

On the other hand, regarding the factors that advise the leading interest rate of the monetary policy remain invariable, only the result of the inflation expectations survey of the private panel of analysts made in April (that incorporates information observed to March) reflecting a decrease of 0.20 percentage points in the projection of the inflationary rhythm for December 2006, when going from 7.74% in March to 7.54% in April, was identified.

The Committee took note that the monetizing and demonetizing factors foreseen for the week of May 12 to 18, 2006 indicate an increase in the creation of primary liquidity for Q2, 659.9 million, fundamentally due to the maturity of LTD's. Also, a decrease in the demand for monetary issue for Q187.6 million is foreseen and a daily banking liquidity position for Q329.7 million. Also, monetary issue is deviated in Q697.1 million above the central programmed point for said variable, therefore the excess of aggregate liquidity estimated for the referred period is located at Q3,874.3 million; if these factors are given, the Committee considered that it would be necessary to make the issue offer compatible with the demand programmed, that the LTD's that expire during the period (Q2,974.7 million, according to registries to May 11, 2006) have to be relocated; and, also, have additional fund raising for around Q899.7 million.

Regarding the determination of quotas for the biddings in the following week, the information provided by the daily monetization flow was taken into account, estimated for the following week and on the other hand, the adopted measures of the previous week regarding the reduction of quotas and the number of weekly biddings; as well as alternating the bidding terms. Based on the above, the Committee agreed that the fund-raising quota for the 182 and 364 day terms to be convened on Monday, May 15, 2006 to be established at Q30.0 million and Q60.0 million, respectively.

Regarding the convening to bidding of LTD's in US dollars, the Committee took into account the foreseen maturity of Treasury Bonds expressed in US dollars, and considered that for the week of May 15 to 19, 2006, it is not necessary to convene biddings of LTD's in the mentioned currency.

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

Based on the discussed, the Committee agreed that for the week of May 15 to 19, 2006, continue with the execution guidelines of the monetary policy observed during the present week; in other words, and continue with operations in the MEBD and in the stock exchange, for fund-raising as well as giving liquidity to the market. The fund-raising operations were made for 7 day terms without quotas, at a leading interest rate of 4.50%, and the bids of liquidity offer in 7 day terms, at a leading interest rate of 7.65%, whose guarantee of said operations will be constituted only by receiving public titles. It is worth indicating that the Committee reiterated the importance of participating in both venues; in other words, keeping simultaneous liquidity giving bids and the retiring of liquidity, considering said participation constitutes a signal of willingness by the Central Bank to moderate the volatility in the short term interest rate.

The Committee taking into account the agreed in matters of coordination with the fiscal policy for the participation in the money market, agreed to convene a bid for the term deposit on Wednesday, May 15 for the terms of 182 and 364 days, with a fund-raising quota for Q30.0 million and Q60.0 million, respectively. The interest rates will be determined according to the conditions of the market, reflected in the bids received.

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

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

As for the participation of the *Banco de Guatemala* in the exchange market, the Committee agreed that while they wait for the presentation of the Participation Regulation in the exchange market submitted for approval to the Monetary Board in the Monetary Policy Report to March 2006, to continue participating through the electronic negotiating system of foreign currency, according to the established for the effect.

FOURTH: Other matters.

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