

## **EXECUTION COMMITTEE**

### **ACT NUMBER 61-2005**

Session 61-2005 celebrated in the *Banco de Guatemala* building on Monday, November twenty-eighth, two thousand five, at nine hours.

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

**ONLY POINT:** Presentation of the Prognosis and Political Analysis of the Monetary Policy System.

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

**ONLY POINT:** Evaluation of the participation of the *Banco de Guatemala* in the exchange market with an exchange rate showing a tendency toward appreciation.

The Committee was convened with the purpose of being shown a presentation of the Equipment of Prognosis of the Economic Area relative to the Prognosis and Analysis of the Monetary Policy System that, with the purpose of accommodating the operative procedures and analysis of said policy to the requirements of the regimen of explicit goals of inflation, the design is being finished with the technical assistance of the International Monetary Fund –FMI-. In the presentation, it was indicated that the main tool of the prognosis system is a semi-structural macroeconomic model, which would generate the prognosis of inflation at mid-term (between one and a half to two years). Said model is made up of short term forecasts that generate the initial conditions for the simulation of it; also, it is complemented by other elements, such as satellite models for exogenous variables (federal fund interest rate, world economic growth, oil prices and others) and the knowledge and experience of the personnel of the Central Bank. With these provisions, the model generates a forecast base and alternate scenarios that allow an evaluation of inflation risks and effectuate monetary policy recommendations.

Regarding the semi-structural macroeconomic model, it was pointed out that the same is made up of eleven principal equations (domestic added demand, external added

demand, total demand, added offer, monetary policy rule, uncovered parity interest rate, yield curve, short-term Fisher equation, long-term Fisher equation, inflation expectations and exchange rate expectations). The main use of said model will be to generate conditional forecasts of inflation for periods of six to eight trimesters.

On the other hand, it was emphasized that this prognosis system was designed to be operated every trimester, with non-seasonal data. This obeys two reasons: the theoretical and practical. The theoretic reason is that the data with higher frequency contains short-term information that is not relevant for monetary policy decision making; on the other hand, the practical reason refers to, according to the experience of the consulters of the technical mission of the IMF, the exercise of prognosis that will take between six and eight weeks to fulfill, therefore it would be impossible that it would be made with greater frequency, for example, monthly. It was also mentioned that the consulters of the IMF recommended the adoption of trimesterly activities programs to develop each exercise of prognosis; such a program includes work sessions between the departments' members of the Prognosis of the Economic Area Team, sessions of the cited group with the Economic Manager and sessions with the Execution Committee in which the latter is made aware of the advances and the results of the work by the Prognosis Team.

Last, it was indicated that, given the progress to date, the Prognosis and Analysis System of the Monetary Policy for Guatemala would be ready so that, through a gradual process and continuous refinement, it would begin to be implemented as of January, 2006. For said reason, the Execution Committee required the technical departments that in the proposal document to the Monetary, Exchange and Credit Policy for 2006 it include a special area in which it explains the theoretical aspects of the transmission mechanism of the monetary policy, as well as, the details referred to by the Inflation Prognosis System. The session ends at ten hours and one minute, all who attended sign in agreement.