FOR AGENDA

EBS/02/172

CONFIDENTIAL

September 17, 2002

To: Members of the Executive Board

From: The Secretary

Subject: **Guatemala—Staff Report for the 2002 Article IV Consultation, Midterm Review Under the Stand-By Arrangement, and Requests for Waiver and Modification of Performance Criteria**

Attached for consideration by the Executive Directors is the staff report for the 2002 Article IV consultation with Guatemala, the midterm review under the Stand-By Arrangement, and Guatemala's requests for waiver and modification of performance criteria, which is tentatively scheduled for discussion on **Wednesday, October 2, 2002**. A draft decision appears on pages 22 and 23. At the time of circulation of this paper to the Board, the Secretary's Department has not received a communication from the authorities of Guatemala indicating whether or not they consent to the Fund's publication of this paper; such communication may be received after the authorities have had an opportunity to read the paper.

Questions may be referred to Mr. Rennhack (ext. 37350) and Mr. Bailén (ext. 34794) in WHD.

Unless the Documents Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the WTO Secretariat on Wednesday, September 25, 2002; and to the European Commission, the European Investment Bank, and the Inter-American Development Bank, following its consideration by the Executive Board.

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INTERNATIONAL MONETARY FUND

GUATEMALA

Staff Report for the 2002 Article IV Consultation, Midterm Review under the Stand-By Arrangement, and Requests for Waiver and Modification of Performance Criteria

Prepared by the Western Hemisphere Department

(In consultation with the Fiscal Affairs, Legal, Monetary and Exchange Affairs, Policy Development and Review, Statistics, and Treasurer's Departments)

Approved by Miguel E. Bonangelino and G. Russell Kincaid

September 16, 2002

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Executive Summary

The authorities have developed a medium-term strategy aimed at fostering faster real economic growth and improving social conditions. Their approach includes maintaining sound macroeconomic policies, increasing social expenditure financed by higher taxes, strengthening the financial system, and improving transparency and governance. Within this framework, in August 2001 congress approved a major tax increase, including an increase in the VAT rate from 10 to 12 percent.

The Fund-supported program for 2002 (approved on April 1) seeks to support real economic growth of 2 percent, while the international reserve cover would remain adequate. The overall public sector deficit would decline from 2.3 percent of GDP in 2001 to 1½ percent of GDP in 2002. Monetary policy would aim at reducing inflation from 9 percent in 2001 to 4–6 percent during 2002. Structural reforms would focus on improving the financial sector, transparency, and governance.

So far in 2002, real economic growth appears to have been slower than expected, while 12-month inflation through July stayed at 9 percent. Through June fiscal policy was on track, while the performance criteria for net domestic assets and net international reserves were not observed, because of an administrative delay in a US$120 million loan disbursement from the IDB. The disbursement is expected to be made in mid-September. The continuous performance criterion on external arrears was breached for a brief period in April. The staff supports the authorities' request for waivers for the non-observance of these criteria, as the deviations have been corrected and have not affected the overall thrust of policies.

For the year as a whole, real GDP might rise by somewhat less than expected. The authorities aim to reduce the ceilings on net domestic assets of the central bank for end-September and end-December with a view to lowering inflation to the target of 4–6 percent. The overall public sector deficit is likely to decline as expected, as tax revenues are performing well while expenditure policy has been strict. The authorities are requesting a modification of the expenditure ceiling for end-September and would like some room for additional social spending. The staff supports these requests.

While the financial sector remains fragile, the four key financial sector reform laws were approved in April. By end-August the superintendency of financial institutions had completed its on-site inspections for the two groups of banks identified in the program, and several banks had already taken corrective action. By end-2002, offshore banks will have to join a regulated financial conglomerate or lose their license. Reforms in governance and transparency are proceeding, although at a slower pace than financial reforms.

The external sector remains vulnerable to volatility in the terms of trade or the business cycle in the United States. The authorities believe that maintaining sound policies is the best way to manage the effect of uncertainty in the external environment.

I. Introduction

1. A mission[1] visited Guatemala City in the period June 17–28 to conduct the discussions for the 2002 Article IV consultation and for the midterm review under the one-year Stand–By Arrangement approved on April 1, 2002.[2]

2. After the Board approved the Stand-By Arrangement, the Chairman noted that fiscal policy and structural measures, especially in the financial sector, will be crucial to restoring macroeconomic stability and placing the economy on a higher growth path. The authorities were urged to avoid further delays in bringing the tax ratio to the target of 12 percent of GDP agreed under the 1996 Peace Accords. Further delays in reaching this target would make it difficult to improve the delivery of social services and raise Guatemala's low social indicators.

3. In the attached letter of September 13, 2002, the authorities note that they have maintained strong macroeconomic policies and that five of the seven quantitative performance criteria for end-June 2002 were observed (Table 1). They have met the two structural benchmarks for completion of the midterm review. The four financial sector reform laws were approved in April 2002. By end-August the on-site inspections were completed for the two groups of banks identified in the program, and undercapitalized banks have been required to increase their capital. They are also requesting waivers for the non-observance of three performance criteria: (i) net domestic assets at end-June 2002; (ii) net international reserves of the central bank at end-June 2002; and (iii) the non-accumulation of external arrears. An administrative delay in securing congressional approval of a US$200 million loan from the IDB postponed the first disbursement of US$120 million, even though the country complied with all of the loan conditions. Congress approved the loan in early September 2002, and the disbursement is expected to take place in mid-September. The end-June targets on net international reserves and net domestic assets would have been met if the disbursement had been received by end-June as planned. In April 2002, Guatemala City incurred external arrears of US$11.5 million, and the government settled the arrears in May 2002. Thus the continuous performance criterion on the non-accumulation of external payments arrears was breached in April–May but is

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[1] The mission consisted of Messrs. Rennhack (Head), Arbulú-Neira, Bailén, Druck, Martin (all WHD) and Luzio (PDR) and met with the minister of finance, the president of the central bank, other senior government officials, and representatives of the private sector and the international donor community.

[2] The arrangement was approved in the amount of SDR 84 million (40 percent of quota). The authorities intend to treat the arrangement as precautionary. Guatemala has no outstanding purchases from the Fund and accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement. Relations with the Fund, the World Bank, and the Inter-American Development Bank are described in Attachments I, II, and III, respectively.

now being observed. On this basis, the authorities are requesting the completion of the midterm review under the program.

4. The Safeguards Assessment of the Bank of Guatemala (BANGUAT) determined that the BANGUAT has taken initial steps to strengthen its safeguards framework. In particular the recent passage of a new central bank law has largely addressed many safeguards issues related to the central bank's external audit and financial reporting framework. However, some significant vulnerabilities remain. To address these vulnerabilities, Fund staff recommended the following priority measures: (i) appoint an audit firm with international central banking experience to conduct the first external audit; (ii) adopt International Accounting Standards as BANGUAT's reporting framework; (iii) adopt a more formal oversight mechanism at the level of the Monetary Board, and (iv) strengthen controls in the areas of international reserves management and data reporting. Staff also proposed measures to improve the Internal Audit Department, establish a mechanism to oversee reserve management guidelines, and ensure appropriate treatment of realized and unrealized gains and losses. The BANGUAT concurred with the assessment's findings and has committed to implementing the proposed recommendations under an agreed timetable.

5. Guatemala's statistical system has significant weaknesses, especially in the data on national accounts, balance of payments, and external debt that complicate surveillance and economic analysis. The authorities are addressing many of these shortcomings through technical assistance from the Fund.

II. Background

6. In the 1990s, real economic growth averaged about 4 percent a year, or about 1¼ percent a year in per capita terms (Table 2). At the same time, public expenditure on education and health as a share of GDP ranked among the lowest in Latin America, reflecting in part the country's low tax revenues (Table 3). As a result, social conditions remained poor, even though some social indicators, such as infant mortality and adult illiteracy, improved (Table 4). In 1998, about one-third of the population lived on less than US$2 per day, and income inequality was extremely high. In 2000, about one-third of adults were illiterate, while 40 percent of the population lacked access to basic health services.

7. In 2000 and 2001, the administration gradually developed a medium-term poverty reduction strategy (PRS)—which was presented at a Consultative Group meeting in early 2002—based on steps to promote faster economic growth and to improve social conditions. The PRS set specific goals for 2005, including raising real economic growth above 4 percent a year, reducing the index of extreme poverty by 3 percentage points and improving many indices of the quality of education, health, and rural development. The policies focused on:

- *Sound macroeconomic policies.* The authorities wanted to maintain a low overall public sector deficit, supported by a prudent monetary policy, throughout the government's term to avoid political cycles in the stance of demand policies, which have added to uncertainty and deterred investment. In the most recent political transition, the fiscal deficit rose sharply and monetary policy eased ahead of the November 1999 elections, which forced the current government to spend its first year restoring sound policies.

- *Increased social spending financed with higher tax revenues.* The 1996 Peace Accords called for an increase in tax revenues from 8 percent of GDP in 1996 to 12 percent of GDP by 2000. These additional domestic resources—together with donor support—were to finance a pick up in public spending on social programs and basic infrastructure from 4 percent of GDP in 1996 to 8 percent of GDP by 2000. Through 2000, tax revenues and social spending had increased somewhat but stayed below the objectives set out in the accords. In August 2001, congress adopted several revenue measures, including an increase in the VAT rate from 10 percent to 12 percent and an increase in the presumptive income tax rate on commercial and agricultural corporations,[3] with a view to raising tax revenues to 9¾ percent of GDP in 2001 and to 10¾ percent of GDP in 2002. Based on these actions, the international donor community agreed to continue to provide financial support, on the condition that the authorities raise tax revenues to 12 percent of GDP by 2004.

- *Strengthen the financial system.* In 2000, the authorities agreed to participate in the FSAP process out of a concern for the health of the financial system. The FSSA report found that the financial system was quite fragile, partly because of the existence of a sizable unregulated offshore banking sector, and recommended comprehensive financial sector reform (Box 1). In 2001, the authorities moved quickly to intervene three small banks, secured congressional approval of an anti-money laundering law in October 2001 and began to draft four financial sector reform laws.

- *Improve transparency and governance.* Guatemala ranks poorly on many indicators of governance, especially in the areas of rule of law, control of corruption, and political stability (Table 5). Concerns about governance add to uncertainty, deter investment, and undermine support for higher taxes, because many citizens question the quality of public spending.

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[3] The other measures included increases in excise taxes on fuel oil and import duties on used cars. Congress also approved reforms to the tax and penal codes with a view to strengthening tax administration.

Box 1. Financial Sector Stability Assessment—Main Conclusions

The FSSA report concluded that the financial system in Guatemala was quite fragile. At the time the report was prepared (2000–01), the financial system was experiencing an increase in nonperforming loans, insufficient provisioning, and a deterioration in capital adequacy. Moreover, there was concern that the sizable unregulated offshore sector may have been concealing problem loans and losses. Specifically:

- several structural weaknesses in prudential regulation and in supervisory practices led to poor compliance with the Basel Core Principles (BCPs);
- the legal and judicial framework for bank restructuring and resolution was inadequate, with a weak system for early resolution of bank difficulties, inappropriate use of lender of last resort facilities, and government deposits and cumbersome procedures for bank intervention;
- the institutional and legal framework for monetary and financial policies had several deficiencies, as the role of the Monetary Board gave rise to excessive political influence and potential conflicts of interest; and
- the payments system contained several risks, in particular because the central bank implicitly guaranteed the settlement of clearinghouse balances.

The report recommended a comprehensive reform strategy that started with an overhaul of the legal framework for financial supervision, banking, and the central bank. The authorities agreed with the conclusions of the report and without delay began to develop four new financial sector laws with the technical assistance of the Fund, the World Bank, and the IDB. The superintendency of financial institutions was to conduct on-site inspections of all banks and require shareholders of undercapitalized banks to inject more capital.

8. **Macroeconomic performance remained uneven in 2000–01**, mainly because of inconsistent policy implementation. In 2000, the government cut the overall public sector deficit to 2 percent of GDP, from 3 percent of GDP in 1999. However, sharp increases in public spending in early 2001 boosted the overall deficit of the combined public sector to 2.3 percent of GDP in 2001, in spite of the tax increase. During 2000, the central bank adopted a tight monetary policy to help reverse the demand stimulus of 1999 but then eased the stance of monetary policy during 2001. Open market interest rates declined from 18 percent at end-2000 to 10 percent at end-2001, considerably more than the fall in U.S. interest rates, and the growth in currency issue picked up to 15 percent during the year. Real GDP growth slowed to 2.1 percent in 2001, reflecting a continuing decline in the terms of trade as well as the recession in the United States. Inflation declined to 5 percent during 2000 but then rose to 9 percent during 2001, as policies were not tight enough to limit the price impact of the VAT increase.

9. **In these two years, the external sector became more vulnerable**. While the quetzal depreciated vis-à-vis the U.S. dollar by about 2 percent, the currency appreciated in

real effective terms by 7½ percent in 2000–01 (Table 6, Figure 1). The government granted minimum wage increases of 10 percent in 2000 and 16 percent in 2001, which led to a significant increase in labor costs in U.S. dollar terms in industries such as maquila, that link their wages to the minimum wage. The external current account deficit amounted to 5.9 percent of GDP in 2001, compared with 5.5 percent of GDP in 2000,[4] reflecting in part declining world commodity prices, and the deficit was financed largely by private capital inflows not related to foreign direct investment. However, by end-2001, net international reserves rose to the equivalent of about 130 percent of base money and 175 percent of short-term public debt on a remaining maturity basis.

10. **For 2002, the authorities developed a program that incorporated their policies into a consistent framework.** Their policies aim at supporting real economic growth of somewhat more than 2 percent, in view of the outlook in late 2001 (when the program was designed) for a difficult external environment. Net international reserves would decline by US$210 million to US$2.1 billion by end-2002,[5] but would continue to provide adequate cover for imports and short-term debt on a remaining maturity basis, while the external current account deficit would narrow slightly in relation to GDP. The overall public sector deficit is targeted to decline to 1½ percent of GDP, as central government revenues will benefit from the full-year effect of the increase in the VAT rate as well as a virtual freeze on nominal spending in 2002. Monetary policy, together with the stronger fiscal policy, aims to limit the growth in currency issue to 7½ percent during the year to offset the price impact of the VAT rate increase and lower inflation to 4–6 percent during 2002. The central bank would allow the exchange rate to reflect market forces, limiting its foreign exchange intervention to market smoothing. With privatization virtually complete, structural measures are to focus on strengthening the financial system and improving governance and transparency.

11. The program involves less fiscal adjustment, somewhat faster broad money growth, and a larger current account adjustment than had been envisaged in the March 2002 staff report. These differences in the estimated outturn for 2001 reflect weaknesses in statistical reporting, and do not alter the prospects for achieving the original program targets. In the previous staff report, real GDP was estimated to rise by 1.8 percent in 2001, the overall public sector deficit for 2001 was projected at 3.0 percent of GDP, and the growth in bank liabilities to the private sector was expected to be 15.8 percent. The changes resulting from the more recent information on the outturn for 2001 reflect the long lags in compiling complete information. The most recent estimate of the external current account deficit of

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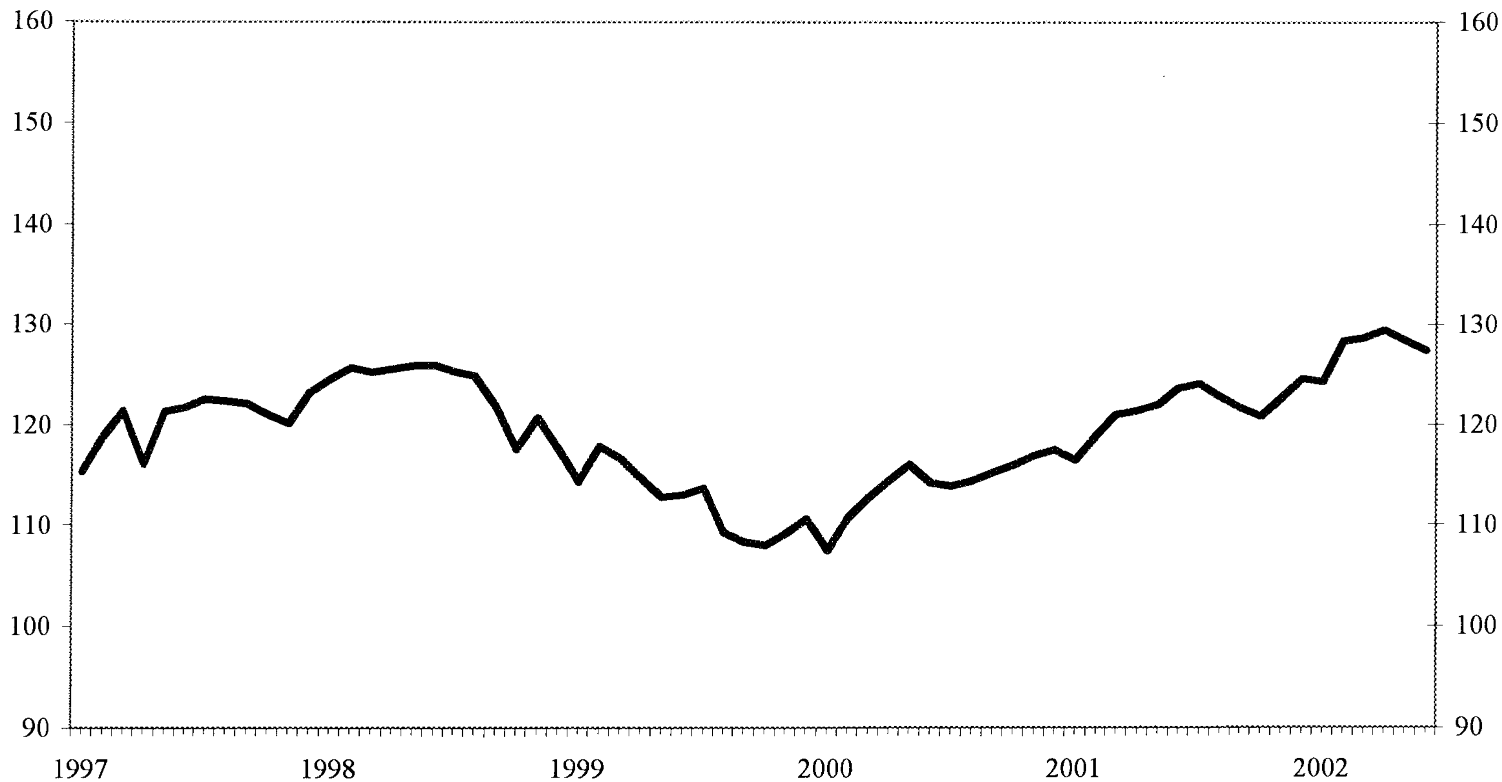
[4] The increase in the estimated external current account deficit in 2001, compared with the program, largely reflects a revision of imports to include duty-free imports, which were made by the government.

[5] The government planned to retire short-term debt, using the proceeds of the US$325 million bond issued in late 2001.

Figure 1. Guatemala: Real Effective Exchange Rate 1/2/
(1995=100)



Source: Information Notice System.
1/ An increase (decrease) means appreciation (depreciation)
2/ Measure real effective exchange rate in a multilateral (trade weighted) sense.

5.9 percent of GDP in 2001 differs substantially from the estimate of 4.5 percent of GDP presented in the previous staff report. This revision reflects fundamental improvements in the data reporting systems. In May 2001, the central bank modified its import recording system to integrate the electronic customs reporting system from the customs and tax agencies. The staff estimates that this change raised the estimate of merchandise imports by 0.8 percent of GDP in 2001. Starting in January 2002, the data on workers' remittances have been improved significantly to include transfers made through commercial banks. The authorities have not revised the import or remittance data for earlier years, which makes it very difficult to assess trends in the external current account deficit.

12. **So far in 2002**, the monthly indicator of economic activity rose by 1 percent in the first five months of the year, while 12-month inflation declined to about 7½ percent through August.

13. **The overall public sector registered a small surplus through June**, compared with a small deficit anticipated under the program (Table 7). Central government tax revenues rose by 25 percent year on year, as a result of the measures adopted in 2001. The performance criterion on the ceiling on total central government expenditure was observed, as expenditure fell by 3.1 percent in nominal terms (about 12 percent in real terms) year on year. Most of the expenditure cuts took place in nonpriority areas (defense expenditure fell by almost 30 percent year on year), while social expenditure was 0.4 percent of GDP above the program floor, with higher spending largely in education and health. As a result, the central government registered a surplus of 0.4 percent of GDP, as programmed. Central bank operating losses turned out lower than expected, as interest rates on open market securities fell by 200 basis points between end-2001 and June 2002. Public enterprises registered a smaller than expected surplus, because of reduced interest income on their holdings of central bank securities.

14. **The central bank's net domestic assets contracted as expected through end-June,** except for the effect of the delay in the disbursement of the IDB loan (Table 8). The central bank began to tighten credit policy in July and August, leading to an increase in open market interest rates of about 100 basis points and a slowdown in the 12-month growth of currency issue to 11.3 percent by end-August, compared with 12.2 percent at end-June.

15. **The central bank let the exchange rate reflect market forces**, with only limited foreign exchange intervention. In the first semester the quetzal appreciated in nominal terms by 1¼ percent. Together with the continued high inflation, this led to a real effective currency appreciation of 4½ percent in this period. Minimum wages were raised by 9.6 percent at the beginning of 2002, which—together with the nominal currency appreciation—pushed up minimum wages in U.S. dollar terms.

16. **The financial sector remains fragile**, as problem loans rose to 14 percent of total loans in May 2002 (Table 9). The three banks intervened in 2001 remain in liquidation, because this process is being handled under the previous financial sector laws. At the same

time, the onshore banking system became more dollarized, following the change in May 2001 that allowed residents to hold assets and liabilities in foreign currency in the banking system.[6] This legal change most likely led to a transfer of U.S. dollar deposits and some loans from the unregulated offshore sector to the onshore sector. Initially, the growth in M2 surged to over 20 percent year on year in late 2001 and early 2002, as recorded foreign currency deposits expanded quickly. By June 2002, foreign currency deposits reached US$335 million (6 percent of M2), but the growth in M2 had slowed to 11 percent year on year, suggesting that the stock adjustment was coming to an end (Table 10). By contrast the growth in credit to the private sector remained steady at about 13 percent a year, even though recorded credit to the private sector in foreign currency rose to US$805 million (about 17 percent of total credit to the private sector) by June 2002. With the higher deposits and lower central bank interest rates, banks reduced their deposit interest rates in local currency from 7.7 percent at end-2001 to 7 percent in June 2002, while local currency lending interest rates declined from 17.9 percent to 16.9 percent.

17. **With regard to the external sector**, preliminary information suggests that the trade deficit widened in the first five months of 2002 (Table 11). Total exports in U.S. dollar terms (including net maquila exports) fell by 5 percent year on year, driven largely by a decline in non-traditional exports and no growth in net maquila exports related to the weakness in the economy of the United States. Reported imports in U.S. dollar terms increased by 16.6 percent in this period, reflecting improvements in the customs reporting system. However, reported workers' remittances rose by 96 percent in the first half of the year, mainly due to better reporting of these inflows. As a result, the measured external current account deficit most likely narrowed in the first half of 2002. In the first half of the year, net international reserves declined by about US$65 million, reflecting in part the government's repayment of US$145 million of short-term external debt.

18. **To improve governance and public accountability**, congress approved the law on the office of the comptroller general in mid-May. The government has submitted to congress draft laws strengthening the existing laws on probity to govern purchases and procurement of the central administration so as to introduce greater transparency and efficiency in such areas. The authorities are preparing a draft law to require the government to include an estimate of the cost of special tax privileges in its annual budget.

19. **The authorities are planning to participate in the HIPC relief for Honduras and Nicaragua**. Spain helped cover the costs of the relief to Nicaragua, and the authorities are looking for a similar mechanism to minimize the costs of the relief to Honduras.

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[6] U.S. dollar deposits are subject to a reserve requirement of 14.6 percent, the same as the rate applied to local currency deposits.

III. POLICY DISCUSSIONS

20. **The policy discussions focused on the authorities' progress in implementing their medium-term strategy.** So far this year, the tax measures adopted in 2001 are raising revenues as envisaged, which is helping to reduce the overall public sector deficit while allowing for moderate growth in social spending as expected. The four new financial sector laws created the legal framework that will enable the authorities to begin to tackle the weaknesses identified by the FSSA report. At the same time, continued high inflation was viewed as a threat to external competitiveness and medium-term growth prospects. The authorities noted that it would be a challenge to reduce inflation to the targeted range by the end of the year, but emphasized the importance of adjusting policies to try to achieve the target. As a result, they intend to rely on a tighter credit policy to slow the growth in currency issue to lower inflation. The authorities added that fiscal policy in 2002 has been helping to limit inflationary pressures, with the significant increase in revenues and tight control over expenditure. The slow growth in the monthly index of economic activity through May suggested that real GDP might rise by somewhat less than 2 percent this year. Nonetheless, output in the telecommunications and electricity and water sectors is projected to rise by 6 percent, as recently privatized firms expanded their investment, and it was agreed to maintain the program projection for real growth.

21. **The authorities and the staff agreed that more work was required to achieve the objectives of the medium-term strategy,** especially to make a significant improvement in social conditions. The overall public sector deficit would need to fall to about 1 percent of GDP in 2003 and beyond to underpin macroeconomic stability, which is consistent with the medium-term framework of the program. This deficit could be fully financed by multilateral and official creditors and would keep total public debt at about 25 percent of GDP. This conservative stance would give fiscal policy room for maneuver in the event of terms of trade shocks or natural disasters and provide a cushion in the event the government had to assume contingent liabilities arising from difficulties in the financial system or the social security system. Within this overall fiscal stance, tax policy would need to aim at raising revenues further to support additional social spending and public investment. It would be crucial to follow through with strengthening financial supervision and regulation in line with the new legal framework and considerable work remained to improve governance and transparency. The staff noted that the external sector remained highly vulnerable, especially if economic difficulties elsewhere in the region intensified. The authorities shared this concern and felt that the situation reinforced the need for prudent policies.

A. Fiscal Policy

22. **In 2002, the tax increases, together with tight expenditure control, are expected to reduce the overall public sector deficit to 1.5 percent of GDP** (with a central government deficit of 1.3 percent of GDP), as envisaged in the program. External financing would amount to 0.4 percent of GDP, reflecting net disbursements mainly from the IDB

and the World Bank, while privatization proceeds would amount to 0.3 percent of GDP. Net domestic financing would cover the remainder of the deficit.

23. **Based on the strong revenue performance in the first half of 2002**, the government's tax collections are projected to reach the target of 10¾ percent of GDP. The authorities will continue to monitor revenue and stand ready to consider additional tax measures if revenue collections were to fall significantly below the program target. In this event, the staff suggested broadening the income tax base as recommended in 2001 by the FAD tax policy mission.

24. **The ministry of finance's control over spending has been enhanced** by the presidential decree issued in February 2002, which set quarterly limits for expenditure by each ministry, froze civil service wage rates, and prohibited supplemental appropriations. In addition, the expenditure reporting of several public agencies has been substantially improved. These agencies had been following the historical practice of underreporting their actual spending to the ministry of finance during the first ten months of the year. In the past, in November and December, these agencies would report their cumulative underreported spending in the first ten months as well as their actual spending in the last two months of the year. On this basis, the annual expenditures for past years were correct and consistent with spending authorized by congress. However, the Fund-supported program sets a quarterly ceiling on total actual spending by the central government, and the past practice is inconsistent with the program. This problem was uncovered during congressional testimony in early July 2002. The minister of finance moved quickly to correct the information on central government expenditure for April and May that had already been sent to the Fund staff as part of the system for program monitoring, and to put in place a system to gather the correct information for June and beyond.[7] The authorities have assured the staff that the information on expenditure through June 2002 is accurate and consistent with the program definitions. In this context, the authorities are requesting a modification of the ceiling on central government expenditure for end-September 2002, while leaving the ceiling for end-December 2002 unchanged, because the original program ceiling for end-September was based on an incorrect pattern of seasonality.

25. **This expenditure control will allow the government to keep total nominal expenditure under the program ceiling**. Compared to the program, the wage bill is projected to rise slightly in relation to GDP, based on new positions in the ministries of education and internal security, while capital expenditure is expected to fall in relation to GDP, reflecting a slower pace of implementation of some projects caused in part by the

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[7] This provision of inaccurate data does not constitute a breach of Article VIII, Section 5, because this information was not in relation to the data needed to determine the observance of the end-June performance criterion on central government expenditure. The applicability of Article VIII, Section 5 will be discussed further in a Board paper being prepared that is entitled "Strengthening the Effectiveness of Article VIII, Section 5."

limited availability of counterpart funds. The authorities would like to increase social spending. They are requesting a modification of the program adjustor that allows for additional social spending of up to US$40 million (0.2 percent of GDP) if the government receives excess external financing from multilateral creditors. Specifically they would like to increase the limit on additional social spending to US$60 million, which would represent additional spending of 0.1 percent of GDP. If the government were to use the full amount of the limit, total central government expenditure would rise by 3 percent in nominal terms (a decline of about 3 percent in real terms) in 2002, and the overall public sector deficit would reach 1.6 percent of GDP. (This adjustor also affects the ceiling on total central government expenditure and on contracting of nonconcessional external debt).[8]

26. **For 2003**, the authorities are preparing a budget that reduces the overall public sector deficit to about 1 percent of GDP. They want to focus on expenditure control to avoid a pre-election surge in spending. They remain committed to increasing tax revenue to 12 percent of GDP in 2004, as agreed with donor countries, but they cautioned that significant tax increases would be difficult ahead of the election, especially in light of the widespread public demonstrations following the increase in the VAT in August 2001. The staff urged the authorities to secure some increase in taxes by widening the income tax base and increasing excise taxes on gasoline, beverages, and tobacco products. The details of fiscal policy for 2003 will be discussed later this year.

B. Monetary Policy

27. **The authorities plan to tighten monetary policy to bring inflation back to the target of 4–6 percent.** It was agreed that the sustained high inflation probably reflected many non-monetary factors, such as the lagged effects of the rapid growth in public spending in 2001 and the large minimum wage increases since 2000, that prolonged the inflationary impulse created by the VAT increase. The staff commented that the steady decline in open market interest rates in 2001 and so far in 2002 suggested that monetary policy has probably helped sustain the inflationary momentum. The central bank will contract its net domestic assets by more than targeted in the program with a view to slowing the growth in currency issue during the year from 7.7 percent in the program to 5½ percent, well below the expected growth in nominal economic activity. Based on this policy adjustment, the authorities agreed to lower the ceiling on net domestic assets of the central bank for end-September and end-December 2002.[9]

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[8] The revisions to this paragraph in the technical memorandum of understanding are presented in the authorities' letter of intent.

[9] Currency issue has a significant impact on demand, because the sizable informal sector has few links with the banking system. The ceiling for end-September and end-December will be reduced by Q 100 million (1 percent of currency issue at end-2001). If average

(continued)

28. **The central bank is considering the adoption of an inflation-targeting (IT) framework,** and plans to request technical assistance from MAE to fully assess the implications of an IT framework for Guatemala. They noted that the new legal framework sets price stability as the primary objective for the central bank and grants it instrument independence. The staff agreed that IT might provide the right framework to achieve long run price stability, and that the central bank might need several more years to put this framework in place.

C. External Sector

29. **The strengthening of fiscal policy in 2002 is expected to reduce the external current account deficit to 4.8 percent of GDP.**[10] Based on developments through June, exports in U.S. dollar terms are projected to rise by less than expected. Imports would grow faster than anticipated, while recorded workers' remittances are projected to rise by 60 percent, both based on the improved reporting systems. Total net capital inflows are projected to decline to less than 4 percent of GDP for several reasons. There were several unusual inflows in 2001 (privatization proceeds and the government's US$325 million bond issue) and the improved recording of workers' remittances led to a decline in errors and omissions (which had been positive). The overall balance of payments is still expected to register a deficit of US$210 million.

30. **The staff and the authorities agreed that the reasons for the recent currency appreciation were unclear**, partly because the balance of payments data were hard to interpret in light of the recent improvements in reporting systems. The authorities were concerned that the tightening of monetary policy would raise interest rates and appreciate the quetzal further. Nonetheless, they agreed that high inflation posed a greater threat to external competitiveness and would continue to let market forces determine the exchange rate, while directing monetary policy to lowering inflation. They agreed that a prudent wage policy was particularly important for a country like Guatemala, with maquila and other labor-intensive exports with costs directly related to the minimum wage.

31. **Guatemala has a relatively open trade regime**, with a rating of 4 on the Fund's scale. The authorities expect to complete free trade agreements with Chile, Canada, and Panama by end-2002 or early 2003, and will participate in the regional negotiation on a free trade agreement with the United States. The authorities also noted that Guatemala's agricultural products face significant barriers in industrial countries, in particular Europe,

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monthly inflation stays above 0.3 percent in the third quarter of 2002, the ceiling for end-December will be reduced by another Q 100 million.

[10] Because of the data revisions, it is difficult to compare this estimate with the program projection of 4.5 percent of GDP in 2002.

and reiterated that Guatemala would continue to address this issue in the Doha round of negotiations.

D. Structural Policies

32. **The four financial sector laws approved in April will lead to a much stronger financial system** by providing the legal basis for the implementation of most of the recommendations of the FSSA (Box 2). The authorities have already begun to carry out several key reforms. Specifically:

- The superintendency has started to conduct on-site inspections of all banks. As of end-August, the audits for 18 of the country's 32 banks were completed, and the superintendent has issued instructions to those banks that need to take corrective action. Banks that are unable to provide the additional capital and reserves will be subject to a regularization plan in accordance with the new legal framework. The capitalization program has begun as three banks have already increased their capital by a combined total of about Q 350 million (0.2 percent of GDP) to meet the minimum capital-asset ratios. Other banks have agreed to lengthen the maturity of problem loans in return for increased collateral.

- Offshore banks have until end-2002 to join a licensed financial conglomerate, or lose their license. The staff expressed concern about possible weaknesses hidden in the offshore banks that could spread to the onshore system, but the authorities and the banking sector were confident that any problems would be minor.

- In November 2002, the government intends to recapitalize the central bank as required under the recently approved central bank law. The central government will transfer a zero coupon bond with a long maturity (perhaps as much as 50 years) to the central bank equivalent to the stock of central bank losses accumulated until end-2001, which amount to about 7 percent of GDP. This step will raise total public debt to 25 percent of GDP. The staff noted that an interest-bearing bond would have been a more effective way to solidify the central bank's balance sheet, but the authorities responded that this option lacked sufficient political support. The government will cover the central bank losses for 2002 by transferring a market-interest-bearing bond to the central bank in the amount of the losses, which will enable it to reduce its stock of open market certificates. This transfer would take place in 2004, after the central bank's financial statements for 2002 have been audited and congress has included the bond and the related interest payments in the budget. The central bank's losses for each subsequent year will be financed in the same manner, and this approach is expected to eliminate central bank losses over the medium term.

Box 2: Key Features of New Financial System Laws

Central bank legislation

- Makes price stability the policy objective of the central bank.

- Gives president of central bank a four-year term that does not coincide with the political cycle and sets strict limits on the causes for dismissal of the president.

- Requires central government to cover past and future losses of the central bank.

- Limits lender-of-last-resort facilities to short-term credit to banks with liquidity problems. These credits should not amount to more than 50 percent of the bank's net worth.

- Eliminates central bank role as implicit guarantor of clearinghouse settlements. Required reserves to serve as collateral for clearing. Failure to meet these payments triggers liquidation.

- Requires an external audit of BANGUAT's financial statements.

- Still grants significant role to monetary board.

Banking law

- Establishes a framework for consolidated supervision of financial conglomerates, including the offshore sector, and allows for stronger prudential regulations.

- Introduces mechanism for the resolution of insolvent banks. Performing assets backed by liabilities to be sold to a viable bank. If needed, insured deposits will be reimbursed.

- Gives bank superintendent (SB) the authority to enforce prompt corrective actions.

Monetary law

- Improves framework to facilitate exchange convertibility, capital mobility, and domestic intermediation in foreign currency.

Law of financial supervision

- Clearly defines the SB as the supervisory agency of the central bank, banks, and other financial institutions, including conglomerates.

- Establishes that the supervised institutions finance the SB by contributions in proportion to deposits. Additional financing needs should be covered by the central bank.

- Introduces a special fund at the SB to provide legal help to officials and retirees of the SB indicted as a result of dispatching their supervisory related obligations.

33. **With regard to public banks**, the authorities have decided to close the Bank of the Military (Banejer). The performing assets of Banejer, and an equivalent amount of deposits, will be transferred to the National Mortgage Bank (CHN). The newly created Trust Fund will provide a subordinated loan to CHN, which will count as tier-two capital, and will manage the liquidation of the bad loans of Banejer. In addition, CHN already received a capital transfer of Q 50 million from the government in May, and will receive an additional Q 50 million before end-year.

34. **The legal framework to combat money laundering has improved considerably** following the recent approval of the banking and financial supervision laws and of the anti-money laundering law in late 2001.[11] The current legislation criminalizes money and assets laundering arising from any crime, provides for customer due diligence and suspicious transactions reporting, establishes a financial investigation unit under the superintendency of banks and authorizes the freeze or seizure of proceeds or assets derived from money laundering. In late 2002, the authorities intend to submit draft legislation that makes the financing of terrorism a crime.

35. **Fiscal transparency is a key component of the effort to improve governance**. The authorities are working with the World Bank to carry out the third phase of strengthening the government's integrated financial management system (SIAF), which transparently records a large share of public expenditure. The plan is to focus on broadening SIAF's coverage of public institutions outside the central government. In this regard, the authorities already have extended the SIAF to the social investment fund and the social security system, and will extend it to other social funds and the largest municipalities over the next several years. An FAD assessment of the transparency of the fiscal accounts is underway, and is expected to be completed later this year. Also, the government is working with the World Bank to develop an anti-corruption program.

E. Medium-Term Outlook

36. **The medium-term outlook assumes** that the government would continue to pursue strong policies (Table 13). The overall public sector deficit would decline to the sustainable level of 1 percent of GDP by 2003 and beyond, which would keep total public debt at about 25 percent of GDP. The authorities would continue to implement financial sector reforms and improve transparency and governance. Tax revenues would rise to 12 percent of GDP by 2004, which would allow for additional spending on social programs. Monetary policy, supported by fiscal policy, would aim to reduce inflation to 3 percent a year by 2004, which—together with a flexible exchange rate and prudent increases in the minimum wage—would preserve external competitiveness. The outlook also incorporates the latest WEO forecast, which includes a slower than expected pace of recovery in the United States economy.

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[11] The authorities responded to the AML/CFT questionnaire in July 2002.

37. **On this basis,** real GDP growth would rise to 3 percent in 2003 and to 4½ percent by 2006, while the external current account deficit would fall to 4.0 percent of GDP by 2005. Net capital inflows would rise to almost 5 percent of GDP by 2005, leading to a steady accumulation of net international reserves. By 2007, net international reserves would amount to 150 percent of short-term debt on a remaining maturity basis and somewhat over three months of imports of goods and services.

38. **According to the staff's sustainability analysis, the profile of public debt through 2007 appears sound**, provided the overall public sector deficit declines to about 1 percent of GDP as projected. Total public debt would remain at 25 percent of GDP throughout the medium term in the baseline scenario and would range from 25 to 35 percent of GDP under various stress tests, such as higher interest rates or slower growth (Table 14).

39. **The external sector is more vulnerable.** The staff made a tentative estimate of the stock of private sector external debt by adding the net medium and long-term external borrowing by the private sector over the past 20 years. Under the baseline scenario and based on this rough estimate of private external debt, total external debt would rise from 37 percent of GDP in 2001 to 42 percent of GDP in 2002, while the debt-export ratio would decline from about 185 percent to 175 percent (Table 15).[12] However, under various stress tests, total external debt would range from 41 percent of GDP to 57 percent of GDP. Moreover, the composition of the financing of the external current account deficit is a source of concern, as most of the net capital inflows are private flows not related to foreign direct investment. The staff commented that this situation made the country more vulnerable to shifts in confidence that could reduce or reverse the private inflows. It added that strong macroeconomic policies and continued structural reforms, especially to strengthen the financial system and governance, would improve the climate for foreign direct investment, which was a more stable source of financing of the external current account.

40. **In discussing the risks to the outlook**, the authorities commented that volatility in the terms of trade and the business cycle in the United States as well as in private capital inflows could slow growth and widen the external current account deficit, compared with the baseline scenario. Economic difficulties in South America were also a risk. To deal with these risks, the authorities agreed on the importance of maintaining a low overall public sector deficit, which would keep demand pressures under control and eliminate the need to secure financing from international capital markets. The central bank would need to use monetary policy to keep inflation under control, while letting the exchange rate adjust as needed. They added that they had some room for maneuver, as net international reserves were comfortable in relation to short-term external debt and base money.

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[12] An estimate of private external debt was derived.

F. Performance Criteria and External Financing Requirements

41. The program will continue to be monitored through the quantitative performance criteria on net international reserves and net domestic assets of the central bank, the deficit of the combined public sector, total expenditure of the central government, and the contracting and guaranteeing of new nonconcessional external debt. The program will continue to include an indicative target on central government social expenditures and a continuous performance criterion on the non-accumulation of external payments arrears.

42. On the financing side, the gross financing requirement in 2002 is now estimated at slightly over US$1.1 billion, based on a larger external current account deficit than expected (Table 16). The sources of financing are projected to include about US$620 million of financing from private creditors and almost US$400 million in official credit to the public sector.

IV. Staff Appraisal

43. **The authorities' medium-term strategy seeks to promote faster real economic growth and improve social conditions**. This strategy seeks to tackle many deep-rooted problems, such as poor social conditions and weak governance, which will take time to resolve. To be successful, it will be crucial to implement these policies on a sustained basis, as underscored by the uneven economic performance of 2000–01. Also, tax revenues will need to rise to 12 percent of GDP by 2004 to support further increases in social spending and to provide sufficient counterpart funds for externally-financed capital expenditure.

44. **The authorities' program for 2002 is designed to carry out this strategy in a consistent framework.** The authorities have changed the direction of fiscal policy through the increased taxes that are allowing the government to make room for social spending, while bringing the overall public sector deficit close to sustainable levels. The technical difficulty in reporting expenditure in the first half of the year is a sign that the ceiling on total government expenditure is enhancing the authorities' control over spending by all public entities. As a result, expenditure policy has been extremely tight, with a substantial real decline in total spending by the central government the first half of the year. The authorities want to maintain this tight expenditure policy, but would like to create room for a small amount of additional social spending. In this context, the staff supports the authorities' requests to modify the ceiling for total central government expenditure for end-September and to increase the adjustor on the amount of excess external financing that can be spent on social programs from US$40 million to US$60 million.

45. **The major difficulty so far this year has been the continued high rate of inflation**. The authorities have agreed to tighten monetary policy with a view to bringing inflation back to the program target of 4–6 percent during the year. Their request for a reduction in the ceiling on net domestic assets for end-September and end-December 2002 is consistent with this adjustment.

46. **The flexible exchange regime is suitable for Guatemala and helps the economy adjust to shifts in external conditions.** The authorities will continue to let the exchange rate reflect market conditions, even though the tighter monetary policy might lead to some further currency appreciation. In the end, high inflation poses a greater threat to external competitiveness, particularly if the high inflation translates into rapid wage increases. In this regard, it is important to support external competitiveness with a prudent minimum wage policy.

47. **On structural policies**, in April congress approved four laws that establish a new legal framework for the financial sector, which greatly enhances the authorities' ability to resolve the difficulties in this sector. Nonetheless, the new legal framework is only the first step toward strengthening the financial system, and it will be crucial to follow through by adopting more effective regulations and carrying out closer supervision. In this regard, the superintendency of financial institutions is proceeding with its on-site inspections of all banks, and several banks have already taken corrective action. The staff encourages the authorities to continue to press weak banks to take corrective actions as quickly as possible. By end-2002, offshore banks will have to join a regulated financial conglomerate or lose their license. In this regard, the staff would urge the authorities to pay closer attention to the potential problems that may surface in the offshore banks. With respect to governance and transparency, congress approved the law on the office of the comptroller general and the government has submitted legislation to strengthen public procurement. The authorities also are continuing to strengthen the transparency of the fiscal accounts. They are working with the World Bank as well as FAD to improve expenditure management and reporting. It will be important to incorporate the recommendations of FAD's fiscal transparency assessment into economic policies in 2003 and beyond.

48. **Over the medium term, the external position is expected to strengthen over time, provided the overall public sector deficit stays around 1 percent of GDP**. However, this outlook is vulnerable to several risks. In particular, non-FDI private inflows account for a significant share of total net capital inflows, and economic difficulties elsewhere in the region could trigger a reduction or a reversal of these flows. To limit these risks, it will be important to keep fiscal policy on a sustainable medium-term path, while using monetary policy to bring inflation under control and letting the exchange rate reflect market forces.

49. **The authorities are taking steps to improve the quality of economic statistics,** and it will be important to upgrade this data to make surveillance more effective and to enhance the analysis of economic trends. In this regard, the staff notes that the authorities moved quickly to improve the system for reporting central government expenditures.

50. **On balance, the staff recommends the completion of the midterm review and the modifications of performance criteria**. It also recommends the approval of the three waivers requested by the authorities, as the deviations did not affect the overall stance of policies and have been reversed.

51. It is proposed that Guatemala move to a 24-month Article IV consultation cycle, as long as a Fund-supported program remains in place.

V. PROPOSED DECISION

The following decision, which may be adopted by a majority of the votes cast, is proposed for adoption by the Executive Board:

1. Guatemala has consulted with the Fund in accordance with paragraph 3(c) of the Stand-By Arrangement for Guatemala (EBS/02/49, Supplement 1, 4/02/02) and paragraph 2 of the letter from the President of the Bank of Guatemala and the Minister of Finance dated March 15, 2002, in order to review program implementation and reach new understandings concerning the phasing and conditions for disbursements under the Stand-By Arrangement.

2. The letter from the President of the Bank of Guatemala and the Minister of Finance dated September 13, 2002 (the "Letter") shall be attached to the Stand-By Arrangement for Guatemala, and the letter from the President of the Bank of Guatemala and the Minister of Finance dated March 15, 2002, with its respective attachments, shall be read as supplemented and modified by the Letter.

3. Accordingly,

(a) The quantitative performance criteria on the limits on the central government expenditure and the stock of the net domestic assets of the Bank of Guatemala, as specified in paragraphs 3(a)(ii) and 3(a)(iii) of the Stand-By Arrangement, respectively, shall be as set in Tables 1 and 2 of the Letter.

4. The Fund decides that the first review contemplated in paragraph 3(c) of the Stand-By Arrangement for Guatemala is completed and that Guatemala may resume purchases under the Stand-By Arrangement notwithstanding the non-observance of the end-June performance criterion on net domestic assets of the Bank of Guatemala, the end-June performance criterion on net international reserves of the Monetary Authorities, and the continuous performance criterion on the non-accumulation of external arrears specified in paragraphs 3(a)(iii), 3(a)(iv) and 3(b) of the Stand-By Arrangement, on the condition that the information provided by Guatemala on performance under these criteria is accurate.

Table 1. Guatemala: Financial Benchmarks Under the SBA 1/

	2002			
	Indicative Target	Performance Criteria		
	Mar.	Jun.	Sep.	Dec.
(Cumulative amounts from December 31, 2001 in millions of quetzales)				
Deficit of the combined public sector				
Unadjusted limit	535	50	1,140	2,585
Adjusted limit	535	50	...	...
Actual	563	-185	...	...
Margin (+)/shortfall/(-)	-28	235	...	...
Central government expenditure				
Unadjusted limit	4,665	9,280	15,225	22,515
Adjusted limit	4,665	9,395	...	...
Actual	4,770	9,368	...	...
Margin (+)/shortfall/(-)	-105	27	...	...
Central government social expenditure				
Unadjusted floor	1,515	3,515	6,070	9,095
Adjusted floor	1,515	3,590	...	...
Actual	1,999	3,835	...	...
Margin (+)/shortfall/(-)	484	245	...	...
(Stock, in millions of quetzales)				
Net domestic assets of the central bank				
Unadjusted limit 2/	-8,490	-10,080	-9,280	-6,628
Adjusted limit	-8,502	-10,080	...	...
Actual	-8,177	-9,159	...	...
Margin (+)/shortfall/(-)	-325	-921	...	...
(Stock, in millions of U.S. dollars)				
Net international reserves of the central bank				
Target	2,200	2,350	2,220	2,091
Adjusted target	2,198	2,350	...	...
Actual	2,190	2,237	...	...
Margin (+)/shortfall/(-)	-8	-113	...	...
Contracting of nonconcessional external debt (maturity more than one year) 3/				
Limit	440	540	665	710
Actual	112	133	...	...
Margin (+)/shortfall/(-)	328	408	...	...
External debt with maturities up to one year 3/				
Limit	40	30	15	15
Actual	34	29	...	...
Margin (+)/shortfall/(-)	6	1	...	...

Source: Data provided by the Guatemalan authorities.

1/ Program limits and targets adjustable for the shortfalls and excess in net external financing and credit to coffee producers -subject to a maximum-, excess of central government revenue, and debt substitution described in Table 2.

2/ If monthly average inflation rate exceeds 0.3 percent in the third quarter, the NDA ceiling will be adjusted downwards by an additional Q 100 million.

3/ Disbursements of public and publicly guaranteed external debt.

Table 2. Guatemala: Macroeconomic Flows

	Average 1991-98	1999	2000	2001	2002 Jan.-Jun. Prel.	2002 Prog.	2002 Proj.
	(Annual percent change, unless otherwise indicated)						
Income and prices							
Real GDP	4.3	3.8	3.6	2.1	1.0	2.3	2.3
GDP deflator	13.1	5.0	5.7	7.6	...	5.7	5.7
Consumer prices (end of period)	10.6	4.9	5.1	8.9	9.1	5.0	6.0
Consumer prices (average)	10.8	5.2	6.0	7.3	8.6	6.5	7.1
Monetary sector							
Credit to private sector 1/	18.9	11.4	8.2	8.7	9.9	6.2	9.1
Liabilities to private sector	19.3	9.8	23.2	8.1	9.4	7.9	11.3
Interest rate (annual rate, time deposits) 2/	14.8	17.9	15.3	11.3	10.4	...	...
External sector							
Exports	9.1	-2.3	10.9	-7.1	...	4.5	3.3
Imports	10.7	-2.0	13.4	8.4	...	8.7	9.0
Terms of trade	-0.3	-8.7	-0.4	...	...	...	...
Real effective exchange rate 3/	....	-6.0	6.2	1.2	2.3	...	...
	(In percent of GDP, unless otherwise indicated)						
Current account	**-4.9**	**-5.5**	**-5.4**	**-5.9**	...	**-4.5**	**-4.8**
Trade balance	-8.4	-9.7	-10.8	-13.0	...	-9.4	-14.0
Exports	13.9	15.2	16.0	13.6	...	14.7	13.2
Imports	22.3	24.9	26.8	26.6	...	24.1	27.2
Factor payments (net)	-1.1	-1.0	-1.1	-0.4	...	-1.4	-1.0
Current transfers (net)	3.5	3.9	4.5	4.7	...	4.6	7.1
Other	1.1	1.3	2.0	2.8	...	1.7	3.2
Capital account	**5.3**	**4.9**	**9.2**	**8.3**	...	**3.5**	**3.9**
Public sector	0.5	1.7	1.1	1.2	...	0.0	0.4
Private sector	4.5	2.8	7.6	6.6	...	3.1	3.1
Official transfers	0.4	0.4	0.5	0.4	...	0.4	0.4
Net official reserves (in U.S. dollars) (increase -) 4/	**-169**	**126**	**-728**	**-500**	**65**	**210**	**210**
Gross domestic investment	**16.1**	**17.4**	**17.0**	**15.4**	...	**16.2**	**16.4**
Public sector	3.0	5.5	4.1	4.2	...	4.2	4.0
Private sector	13.1	11.9	12.9	11.2	...	12.0	12.4
Gross domestic saving	**11.2**	**11.9**	**11.6**	**9.5**	...	**11.7**	**11.6**
Public sector	2.1	2.3	2.0	1.7	...	2.4	2.3
Private sector	9.1	9.6	9.6	7.8	...	9.3	9.3
External saving	**4.9**	**5.5**	**5.4**	**5.9**	...	**4.5**	**4.8**
Combined public sector balance (including central bank losses)	**-1.7**	**-3.0**	**-2.2**	**-2.3**	**0.1**	**-1.5**	**-1.4**
Overall balance of the nonfinancial public sector (deficit -)	-0.5	-2.7	-1.8	-1.5	0.5	-0.9	-0.9
Financing	**1.7**	**3.0**	**2.2**	**2.3**	**-0.1**	**1.5**	**1.4**
External financing	0.5	1.7	0.8	1.1	-0.7	0.3	0.4
Domestic financing	1.2	0.7	0.5	-0.6	0.6	0.8	0.7
Privatization proceeds	0.0	0.6	0.7	1.8	0.0	0.3	0.3
Memorandum items:							
Nominal GDP (in billions of quetzales)	...	135,287	149,743	165,042	89,211	175,460	178,421

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

1/ In relation to the stock of liabilities to the private sector at the beginning of the period.

2/ End-period.

3/ End-period; a positive change indicates an appreciation. In 2002 refers to the 12-month change through end-June.

4/ The change in net international reserves in 2001 includes US$180 million of a temporary deposit of the government at the central bank, which is part of proceeds from a Eurobond floated at end 2001 earmarked to pay short-term debt. Consequently, in 2002 the change in net international reserves includes the use of these US$180 million. Net of this temporary deposit, the net international reserves would increase by US$320 million in 2001 and would decrease by US$30 million in 2002.

Table 3A. Government and Private Health Expenditures
(In percent of GDP)

	Public Spending		Private Spending		
	Social Security	Other	Insurance	Other	Total
Costa Rica	4.7	0.8	0.0	1.5	6.8
Dominican Republic	0.5	1.4	1.1	3.6	6.5
El Salvador	1.7	1.5	0.2	4.6	8.3
Guatemala	1.3	0.7	0.2	2.2	4.4
Honduras	0.6	3.0	0.2	2.3	6.4
Nicaragua	1.2	2.2	--	2.1	5.7
Panama	3.2	2.0	0.5	1.8	7.5
Central America	1.9	1.7	0.3	2.6	6.5
Latin America	1.8	1.6	0.7	2.3	6.6

Sources: Corbacho and Davoodi (2002); and World Health Organization (2001).

Table 3B. Government Education Spending

(In percent of GDP)

Year	Costa Rica	Dominican Republic	El Salvador	Guatemala	Honduras	Nicaragua	Panama	Central America	Latin America
1985	4.1	1.5	...	1.5	4.0	...	4.4	...	3.1
1986	4.5	1.3	...	1.6	4.5	...	4.3	...	3.2
1987	4.2	...	...	1.8	4.5	...	4.9	...	3.2
1988	4.1	...	...	1.8	...	...	5.1	...	3.0
1989	4.1	...	2.0	1.8	4.0	...	5.1	...	2.8
1990	4.4	...	1.9	1.4	...	3.4	4.7	...	2.8
1991	3.4	...	1.8	1.3	3.8	3.4	4.6	3.1	3.0
1992	3.3	1.3	1.9	1.4	...	3.1	5.0	3.0	3.1
1993	3.5	1.6	1.8	1.5	...	2.8	4.7	2.7	2.9
1994	3.5	1.9	2.0	1.5	3.4	2.8	4.5	2.8	3.3
1995	3.5	1.9	2.2	1.7	3.6	3.1	5.0	3.0	3.3
1996	4.1	1.9	2.3	1.6	...	3.2	5.2	3.0	3.3
1997	...	2.2	2.5	...	...	3.7	5.0	...	...
1998	6.0	...	...	2.0	4.0	4.2	...	...	...

Sources: Corbacho and Davoodi (2002); and World Development Indicators (2002).

Table 3C. Consolidated Central Government: Tax Structure for Latin American Countries, 1995–99

(In percent of GDP)

	Sample Size	Total Revenue	Tax Revenue	Taxes on Income, Profits, and Capital Gains Total	Social Security Taxes	Payroll Taxes	Domestic Taxes on Goods and Services: Total	Of which: General sales turnover or VAT	Of which: Excises	International Trade Taxes Total	Property Taxes	Other Revenue
Latin America 1/		**19.1**	**16.1**	**3.4**	**2.9**	**0.1**	**7.4**	**4.8**	**2.3**	**1.8**	**0.3**	**2.9**
Central America 1/		**19.4**	**16.5**	**3.2**	**2.5**	**0.0**	**7.1**	**4.2**	**3.3**	**2.7**	**0.1**	**2.9**
Costa Rica	1995–99	20.3	17.9	2.4	5.7	0.0	7.7	4.8	2.5	1.9	0.1	2.4
Dominican Republic	1995–98	16.3	14.9	2.6	0.6	0.0	5.6	...	4.7	5.9	0.1	1.4
El Salvador	1995–99	11.7	11.1	3.2	0.0	0.0	6.2	5.5	0.6	1.5	0.1	0.6
Guatemala	1995–99	9.2	8.9	2.0	0.0	0.0	5.2	3.8	1.1	1.5	0.0	0.3
Honduras	...	...	...	...	...	...	...	...	...	...	...	...
Nicaragua	1995	25.8	23.9	2.8	3.3	0.0	10.9	2.9	7.6	5.3	0.0	2.0

Sources: Stotsky (2002); *Government Finance Statistics* (IMF), *International Financial Statistics* (IMF); and *World Economic Outlook* (IMF).

1/ Single average for each revenue classification, only countries for which data are available are included in the calculation.

Table 4. Guatemala: Comparative Social Indicators

	Guatemala	Nicaragua	Honduras	El Salvador	Costa Rica	Average for Latin America and the Caribbean
Rank in UNDP Human Development Index (out of 162 countries) (2001)	108	107	106	95	41	...
GDP per capita in PPP, U.S. dollars (1999)	3,674	2,279	2,340	4,344	8,860	7,352
People not expected to survive to age 40 (in percent of population) (1999)	15.6	11.5	16.0	10.9	4.0	9.7
Life expectancy at birth (years) (2000)	64.5	68.1	65.7	69.5	76.2	69.8
Infant mortality (per 1,000 live births) (2000)	38.8	38.0	33.0	35.0	13.0	32.0
Population without access to safe water (1999)	8.0	21.0	10.0	26.0	2.0	22.0
Per capita health exp. in PPP, U.S dollars (1998)	155.0	266.0	210.0	298.0	509.0	n.a.
Physicians per 100,000 people (1990-99)	93.0	86.0	83.0	107.0	141.0	n.a.
Adult illiteracy (1999)	31.9	31.8	26.0	21.7	4.5	12.0
Primary school net enrollment (1997) (percent of relevant age of the population)	73.8	78.6	87.5	89.1	91.8	93.3
Secondary school net enrollment (1997) (percent of relevant age of the population)	34.9	50.5	36.0	36.4	55.8	65.3
Ratio of the per capita income of the richest 10 percent to the per capita income of the poorest 10 percent of the population (1987-98)	29.1	70.7	119.8	28.5	20.7	n.a.
Gini index (World Development Report, 2001) 1/	59.6	50.3	53.7	52.3	47.0	n.a.
Percentage of population below the poverty line (1984-99)	57.9	50.3	53.0	48.3	11.0	n.a.

Source: UNDP Human Development Report 2001.

1/ For Guatemala, the information refers to the 1989 survey, for Nicaragua, to the 1993 survey; for Honduras, El Salvador, and Costa Rica, to the 1996 surveys.

Table 5. Guatemala: Indicators of Governance

	Voice and Accountability		Political Stability		Government Effectiveness		Regulatory Quality		Rule of Law		Control of Corruption	
	1997/98	2000/01	1997/98	2000/01	1997/98	2000/01	1997/98	2000/01	1997/98	2000/01	1997/98	2000/01
Costa Rica	88	91	82	86	74	78	92	85	71	71	77	81
El Salvador	50	62	48	71	45	46	99	87	30	31	43	47
Guatemala	34	40	22	20	46	31	67	53	11	14	20	29
Honduras	52	52	37	57	36	33	44	39	17	10	12	32
Nicaragua	58	51	39	61	30	28	38	39	26	21	19	24
Panama	71	72	56	70	43	49	94	86	40	53	38	42
Dominican Republic	51	65	55	65	17	46	71	76	65	57	24	50
Regional averages												
Central America	58	62	48	61	42	44	72	66	37	37	33	43
Latin America and the Caribbean	60	60	46	54	49	49	67	59	44	46	47	51
Latin America	60	59	44	52	50	46	71	60	41	42	42	46
OECD	92	92	88	90	91	90	87	88	90	90	91	90
Sub-Saharan Africa	38	36	30	28	35	32	34	36	33	33	37	34
Eastern Europe	61	67	56	55	49	51	54	54	53	57	50	54
Former Soviet Union	32	32	37	31	19	21	17	15	29	27	18	22
East Asia	42	42	62	58	59	57	48	49	54	54	55	49
South Asia	37	32	28	26	30	30	43	35	35	32	43	34
Middle East and North Africa	32	33	48	50	50	54	41	49	58	56	47	52

Source: Kaufmann, Kraay, and Zoido-Lobaton (2002).

Notes: Each entry in the table indicates percent of countries worldwide rate that rate below selected country or a region for each governance indicator.
Higher score for any indicator shows better governance outcome.
All indicators are subjective or based on individuals' perceptions. Each average is the simple arithmetic average.

Table 6. Guatemala: Indicators of External Vulnerability

	1995	1996	1997	1998	1999	2000	2001
Financial indicators							
Broad money (12-month percentage change)	14.5	13.3	23.5	12.9	7.2	17.8	16.7
Private sector credit (12-month percentage change)	33.2	10.7	19.9	27.5	14.4	10.0	11.7
Central bank paper yield (nominal) 1/	22.2	18.0	9.2	11.8	23.2	17.9	10.3
Central bank paper yield (real)	12.6	6.5	2.0	4.0	17.4	12.2	0.5
External indicators							
Merchandise exports (12-month percentage change)	27.9	3.4	16.4	9.6	-2.3	10.9	-7.1
Merchandise imports (12-month percentage change)	18.4	-4.4	22.4	20.7	-2.0	13.4	8.4
Terms of trade (12-month percentage change)	15.4	-9.8	11.0	6.1	-9.4	-0.4	...
Current account balance (in percent of GDP)	-4.1	-2.9	-3.5	-5.3	-5.5	-5.4	-5.9
Net international reserves 2/							
In millions of U.S. dollars	493.5	669.9	957	1,200	1,074	1,802	2,301
In percent of base money	36.8	46.9	56.2	80.2	75.4	113.2	128.7
In percent of short-term external debt on a remaining maturity basis 3/	84.4	83.7	78.0	78.3	73.7	121.0	175.4
In months of next-year's imports of goods and services	1.8	2.0	2.2	2.8	2.2	3.4	4.0
Real effective exchange rate appreciation, 12-month period (-)	-4.6	12.8	8.1	-4.5	-6.0	6.2	1.2
Public indebtness indicators							
Total public sector debt (in percent of GDP)			18.4	17.6	20.4	22.5	24.1
Domestic public sector debt (in percent of GDP) 4/	5.4	6.1	3.1	2.5	2.4	5.8	7.2
Public sector external debt (in percent of GDP)	17.0	15.7	15.3	15.1	18.0	16.7	16.9
External interest payments in percent of exports	4.6	5.0					
of goods and services			4.1	3.7	3.7	3.4	3.4
External amortization payments in percent of exports	9.3	5.7					
of goods and services			5.4	4.6	3.8	3.5	3.9
Public sector and financial sector external debt (in percent of GDP)	18.8	18.2	17.9	17.7	20.7	20.9	19.5

Sources: Bank of Guatemala; and Fund staff estimates.

1/ Refer to open market operations weighted interest rates, except for 1997 and 1998 which refer to 180-day bond interest rates.

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/ End of period short-term debt on a remaining maturity basis as recorded by the BIS. In 2001, preliminary data.

4/ Includes central government debt with residents and open market certificates of the Bank of Guatemala with the private sector.

Table 7. Guatemala: Operations of the Combined Public Sector

(In percent of GDP)

	1999	2000	2001	Jan.-Jun. 2002 Prog.	Jan.-Jun. 2002 Prel.	2002 Prog.	2002 Proj.
I. Central Government Operations							
Total revenue	**10.5**	**10.5**	**11.2**	**11.0**	**10.9**	**11.6**	**11.5**
Tax revenue	9.3	9.5	9.8	10.2	10.2	10.7	10.7
Direct taxes	2.1	2.5	2.4	2.6	2.8	2.7	3.0
Indirect taxes	7.2	7.0	7.4	7.6	7.4	8.0	7.7
Nontax revenue and transfers	1.1	0.9	1.4	0.8	0.7	0.9	0.8
Total expenditures	**13.3**	**12.4**	**13.4**	**10.6**	**10.5**	**12.8**	**12.8**
Current expenditures	8.1	8.6	9.4	8.3	8.0	8.7	9.0
Wages and salaries	3.2	3.5	3.7	3.1	3.3	3.5	3.8
Goods and services	1.1	1.3	1.6	1.1	1.1	1.2	1.3
Interest	1.3	1.2	1.4	1.4	1.3	1.5	1.3
Transfers	2.4	2.6	2.7	2.7	2.3	2.4	2.6
Capital expenditure	5.2	3.7	4.0	2.3	2.5	4.1	3.8
Of which							
Fixed capital formation	1.8	1.5	1.4	0.8	1.1	1.5	1.1
Net lending	0.0	0.0	0.0	0.5	0.3	0.3	0.2
Current account balance (deficit -)	**2.2**	**1.6**	**1.6**	**2.5**	**2.7**	**2.7**	**2.4**
Overall balance (deficit -) 1/	**-3.3**	**-2.4**	**-2.4**	**0.4**	**0.4**	**-1.3**	**-1.3**
Financing	**3.3**	**2.4**	**2.4**	**-0.4**	**-0.4**	**1.3**	**1.3**
External (net)	2.4	0.9	1.3	0.4	-0.6	0.4	0.5
Domestic (net)	0.3	0.7	-0.4	-0.8	0.2	0.6	0.6
Sale of assets	0.6	0.7	1.5	0.0	0.0	0.3	0.3
II. Combined Public Sector Operations							
Combined public sector balance	**-3.0**	**-2.2**	**-2.3**	**-0.1**	**0.1**	**-1.5**	**-1.4**
Current account	2.3	2.0	1.7	2.3	2.5	2.4	2.3
Nonfinancial public sector	-2.8	-1.8	-1.5	0.8	0.5	-0.8	-0.8
Central government	-3.3	-2.4	-2.4	0.4	0.4	-1.3	-1.3
Rest of the nonfinancial public sector	0.5	0.6	0.9	0.4	0.1	0.5	0.5
Bank of Guatemala losses	-0.3	-0.4	-0.8	-0.9	-0.3	-0.6	-0.6
Combined public sector financing	**3.0**	**2.2**	**2.3**	**0.1**	**-0.1**	**1.5**	**1.4**
External (net)	1.7	0.8	1.1	0.3	-0.7	0.3	0.4
Foreign loans (net)	0.8	0.4	0.1	1.0	0.0	0.8	0.8
Bonded debt	0.9	0.4	0.9	-0.7	-0.7	-0.4	-0.4
Domestic (net)	0.7	0.7	-0.6	-0.2	0.6	0.9	0.7
Banking system	1.7	1.0	-1.0	-0.2	0.8	0.9	0.7
Bank of Guatemala 2/	1.9	1.2	-1.5	-0.1	1.0	1.0	1.4
Commercial banks	-0.2	-0.2	0.5	-0.1	-0.2	-0.1	-0.7
Bonded debt	-1.0	-0.5	0.0	0.0	0.0	0.0	0.0
Change in floating debt	0.0	0.2	0.4	0.0	-0.2	0.0	0.0
Sale of assets	0.6	0.7	1.8	0.0	0.0	0.3	0.3
Memorandum item:							
GDP (in millions of quetzales)	135,287	149,743	165,042	87,730	89,210	175,460	178,421

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

1/ Includes statistical discrepancy between results from "above the line" and "below the line."

Table 8. Guatemala: Summary Accounts of the Monetary Authorities

	1999	2000	2001	2002 Jan.-Jun. Prog.	2002 Jan.-Jun. Prel.	2002 Prog.	2002 Proj.
Exchange rate (quetzales/U.S. dollars)	8.0	8.0	8.0	8.0	8.0	8.0	8.0
(Stocks in millions of quetzales)							
Net official reserves 1/	**8,591**	**14,413**	**18,410**	**18,809**	**17,898**	**16,728**	**16,728**
(in millions of U.S. dollars)	1,074	1,802	2,301	2,351	2,237	2,091	2,091
Net domestic assets	**-163**	**-6,199**	**-8,934**	**-10,081**	**-9,159**	**-6,528**	**-6,728**
Net claims on nonfinancial public sector	-7,354	-6,572	-10,361	-10,969	-9,796	-9,463	-8,835
Central government	-5,004	-3,625	-6,533	-6,732	-5,901	-4,954	-4,690
Rest of nonfinancial public sector 2/	-2,351	-2,947	-3,828	-4,238	-3,895	-4,509	-4,145
Bank of Guatemala losses	9,205	9,753	11,014	11,790	11,319	12,088	12,006
Net credit to banks	-2,642	-4,203	-3,524	-4,035	-3,480	-4,205	-4,241
Of which							
Reserve 3/	-3,336	-5,004	-5,970	-6,261	-5,735	-6,431	-6,467
Open market operations 4/	-485	-6,090	-7,451	-8,278	-8,513	-6,462	7,160
Medium- and long- term foreign liabilities	-852	-731	-635	-581	-615	-544	-554
Other assets (net)	1,965	1,644	2,023	1,992	1,927	2,058	2,058
Currency issue	**8,429**	**8,214**	**9,476**	**8,728**	**8,740**	**10,200**	**10,000**
(Flows in millions of quetzales)							
Net official reserves 1/	**-1,005**	**5,822**	**3,997**	**4,283**	**3,439**	**-1,682**	**-1,682**
(in millions of U.S. dollars)	-126	728	500	544	430	-210	-210
Net domestic assets	**3,001**	**-6,036**	**-2,735**	**-3,409**	**-2,487**	**2,407**	**2,206**
Net claims on nonfinancial public sector	738	783	-3,584	-3,455	-2,248	693	1,320
Bank of Guatemala losses	379	548	1,261	1,379	908	1,074	992
Net credit to banks	1,695	-1,561	475	-1,666	-1,145	-476	-512
Of which							
Reserve 3/	1,275	-1,668	-966	-1,534	-1,009	-461	-497
Open market operations 4/	-91	-5,605	-1,361	-431	-667	990	391
Medium- and long- term foreign liabilities	174	121	96	96	62	92	81
Other assets (net)	222	-321	379	668	603	35	35
Currency issue	**2,122**	**-214**	**1,262**	**940**	**952**	**725**	**524**
(12-month percentage change over the stock of currency issued at the beginning of the period)							
Net domestic assets	**47.6**	**-71.6**	**-33.3**	**-43.8**	**-31.9**	**25.4**	**23.3**
Net claims on nonfinancial public sector	11.7	9.3	-43.6	-44.4	-28.9	7.3	13.9
Bank of Guatemala losses	6.0	6.5	15.3	17.7	11.7	11.3	10.5
Currency issue	**33.6**	**-2.5**	**15.4**	**12.1**	**12.2**	**7.7**	**5.5**
Memorandum item:							
Outstanding stock of open market securities 5/	2,634	8,616	11,015	12,265	12,189	10,634	10,955

Sources: Bank of Guatemala; and Fund staff estimates.

1/ Excludes claims on Nicaragua amounting to US$145.7 million up to 1999 and US$75.7 million in 2000, which are included in official data. The stock of NIR in December 2001 includes US$180 million corresponding to part of the proceeds from a Eurobond issue that will be deposited at the central bank.

2/ Includes open market placements with the nonfinancial public sector.

3/ Includes cash deposits, and remunerated reserves.

4/ Includes open market placements with both the financial and nonfinancial private sector.

5/ Open market placements with the private and public sectors.

Table 9. Guatemala: Summary of the Structure and Performance of the Financial Sector 1/

	1997	1998	1999	2000	2001	Prel. Jun. 2002
Number of banks	**35**	**34**	**34**	**32**	**31**	**31**
Majority state-owned (in percent of total assets)	5.1	6.5	8.8	8.5	3.4	2.8
Majority foreign-owned (in percent of total assets)	0.1	0.3	0.5	0.6	0.5	0.5
Foreign branches (as a percent of total assets)	2.6	2.9	3.0	3.5	4.0	3.8
Number of banks accounting for at least						
25 percent of total assets	3	3	3	3	1	1
75 percent of total assets	15	15	14	14	9	9
Total assets of banks (in percent of nominal GDP)	29.1	29.1	29.0	33.9	35.2	35.3
Credit to private sector (in percent of nominal GDP)	19.1	21.3	22.3	22.2	22.5	22.2
Foreign currency-denominated assets (in percent of total assets)	9.2	10.3	10.3	11.2	14.9	14.5
Contingent and off-balance sheet accounts (in percent of total assets)	13.5	16.6	13.2	15.1	11.8	11.7
Of which						
Foreign currency denominated (in percent of total assets)	3.7	4.5	2.9	2.7	2.3	2.3
Average pretax return on total assets (in percent)	1.3	1.0	1.4	1.1	1.0	0.8
Average financial spread 3/	10.5	10.8	9.3	9.1	9.1	9.1
Interest rate spread in interbank market (in percent)	8.0	7.7	6.8	6.3	5.9	5.8
Loans that are nonperforming, substandard, or of lower quality (in percent of total loans)	7.2	8.5	12.7	12.8	13.2	13.6
Total provisions for loan losses (specific plus general)						
In percent of nonperforming loans	22.8	23.7	28.0	27.8	25.4	55.9
In percent of total loans	1.6	2.0	3.6	3.6	2.1	7.6
Risk-weighted capital/asset ratio	13.3	12.4	14.0	14.2	14.1	14.4
Foreign currency debt rating 4/	Ba2	Ba2	Ba2	Ba2	Ba2	Ba2

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

1/ The Guatemalan financial system consists of the central bank, 29 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/ The off-balance sheet accounts are referred to September 2001.

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 10. Guatemala: Summary Accounts of the Banking System

	1999	2000	2001	2002 Jan.-Jun. Prel.	2002 Proj.
Exchange rate (quetzales/U.S. dollars)	8.0	8.0	8.0	8.0	8.0
(Stocks in millions of quetzales)					
Net foreign assets 1/	**5,168**	**10,113**	**14,531**	**14,219**	**13,195**
(in millions of U.S. dollars)	646	1,264	1,816	1,777	1,649
Net domestic assets	**32,430**	**35,841**	**34,862**	**37,264**	**41,639**
Net claims on nonfinancial public sector	-6,888	-6,884	-9,796	-9,427	-9,341
Central government	-4,074	-2,692	-3,688	-3,387	-2,493
Rest of nonfinancial public sector	-2,814	-4,192	-6,108	-6,040	-6,848
Bank of Guatemala losses	9,205	9,753	11,014	11,319	12,006
Credit to private sector and other investment	30,194	33,207	37,122	38,123	41,538
Other assets (net)	-82	-235	-3,478	-2,750	-2,564
Medium- and long-term foreign liabilities	**1,061**	**944**	**722**	**698**	**650**
Liabilities to the private sector	**36,537**	**45,011**	**48,671**	**50,785**	**54,184**
Money	14,672	17,698	20,532	20,987	22,391
Quasi-money	21,865	27,313	28,139	29,798	31,794
(Flows in millions of quetzales)					
Net foreign assets 1/	**762**	**4,945**	**4,417**	**4,124**	**-1,335**
Net domestic assets	**2,644**	**3,412**	**-979**	**56**	**6,777**
Net claims on nonfinancial public sector	548	4	-2,707	-2,932	249
Bank of Guatemala losses	982	548	1,261	908	992
Credit to private sector and other investment	3,799	3,013	3,915	4,601	4,415
Other assets (net)	-2,684	-153	-3,448	-2,520	1,120
Medium- and long-term foreign liabilities	**158**	**-117**	**-222**	**-177**	**-72**
Liabilities to the private sector	**3,248**	**8,474**	**3,660**	**4,357**	**5,513**
Money	1,759	3,026	2,834	3,420	1,859
Quasi-money	1,489	5,448	827	937	3,655
(12-month percentage change over initial stock of liabilities to the private sector)					
Net domestic assets	7.9	9.3	-2.2	0.1	13.9
Net claims on nonfinancial public sector	1.6	0.0	-6.0	-6.3	0.5
Credit to private sector and other investment	11.4	8.2	8.7	9.9	9.1
Liabilities to the private sector	9.8	23.2	8.1	9.4	11.3
Money	5.3	8.3	6.3	7.4	3.8
Quasi-money	4.5	14.9	1.8	2.0	7.5
Memorandum items:					
Credit to private sector (12-month percentage change)	14.4	10.0	11.8	13.7	11.9
Stock of U.S. dollar deposits (in millions of quetzales)	...	...	2,007.6	2,590.0	2,400.0

Sources: Bank of Guatemala; and Fund staff estimates.

1/ Excludes claims on Nicaragua amounting to US$145.7 million up to 1999 and US$75.7 million in 2000, which are included in official data. The stock of NIR in December 2001 includes US$180 million corresponding to part of the proceeds from a Eurobond issue that will be deposited at the central bank.

Table 11. Guatemala: Summary Balance of Payments, 1997-2002

	1997	1998	1999	2000	2001	2002 Prog.	2002 Proj.
Current account	**-630**	**-1,036**	**-1,015**	**-1,049**	**-1,238**	**-966**	**-1,078**
Trade balance	-1,254	-1,804	-1,779	-2,086	-2,742	-2,000	-3,151
Exports, f.o.b.	2,598	2,847	2,781	3,085	2,865	3,134	2,960
Traditional	1,170	1,167	1,056	1,178	954	1,026	949
Of which							
Coffee	616	581	588	572	305	322	292
Nontraditional	1,428	1,680	1,725	1,907	1,911	2,109	2,011
Imports, c.i.f. 1/	3,852	4,651	4,560	5,171	5,607	5,134	6,111
Services	13	63	49	172	507	59	298
Factor services (net)	-228	-169	-181	-209	-90	-286	-274
Of which							
Interest on public debt	140	-140	-127	-152	-180	-233	-225
Other	-368	-29	-54	-58	89	-53	-49
Nonfactor (net)	241	231	229	381	597	345	571
Current transfers (net)	611	705	715	865	997	975	1,775
Capital account	**862**	**1,279**	**890**	**1,777**	**1,738**	**756**	**868**
Official transfers	85	71	68	85	93	95	97
Public sector	222	234	306	209	259	1	69
Disbursements	144	326	400	255	187	301	289
Amortization	171	157	130	137	152	163	125
Of which							
Bank of Guatemala (net) 2/	83	54	26	24	-11	-13	-10
Bonds (net)	399	66	136	91	500	-97	-96
Public sector deposit (net)	0	0	-101	0	49	-39	0
Private sector 3/	525	944	516	1,482	1,386	660	702
Of which							
FDI and privatization.	85	673	155	230	456	186	151
Medium and long-term debt	434	448	544	677	599	367	659
Balance of payments support	30	30	0	0	0	0	0
Overall balance	**232**	**243**	**-126**	**728**	**500**	**-210**	**-210**
		(Annual percent change)					
Exports, f.o.b.	16.4	9.6	-2.3	10.9	-7.1	4.8	3.3
Imports, c.i.f.	22.4	20.7	-2.0	13.4	8.4	0.3	9.0
		(In percent of GDP)					
Current account	**-3.5**	**-5.4**	**-5.5**	**-5.4**	**-5.9**	**-4.5**	**-4.8**
Trade balance	-7.1	-9.4	-9.7	-10.8	-13.0	-9.4	-14.0
Exports, f.o.b.	14.6	14.8	15.2	16.0	13.6	14.7	13.2
Imports, c.i.f.	21.7	24.2	24.9	26.8	26.6	24.1	27.2
Services	0.1	0.3	0.3	0.9	2.4	0.3	1.3
Of which							
Interest on public debt	0.8	-0.7	-0.7	-0.8	-0.9	-1.1	-1.0
Current transfers (net)	3.4	3.7	3.9	4.5	4.7	4.6	7.9
Capital account	**4.9**	**6.7**	**4.9**	**9.2**	**8.3**	**3.5**	**3.9**
Official transfers	0.5	0.4	0.4	0.4	0.4	0.4	0.4
Public sector 2/	1.3	1.2	1.7	1.1	1.2	0.0	0.3
Private sector 3/	3.0	4.9	2.8	7.7	6.6	3.1	3.1
Balance of payments support	0.2	0.2	0.0	0.0	0.0	0.0	0.0
Overall balance	**1.3**	**1.3**	**-0.7**	**3.8**	**2.4**	**-1.0**	**-0.9**
Memorandum items:							
Net reserves in months of next year imports of goods and services 4/	2.2	2.7	2.2	3.4	4.0	3.7	3.3
Nominal GDP (In US$ millions)	17,775	19,193	18,316	19,288	21,065	21,320	22,471

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

1/ Variations in 2000 and 2001 are due to changes in import registration system implemented in July 2000 and upgraded in June 2001.

2/ In 2000 includes the effect of a restructuring of a US$25 million dollar short-term liability with Mexico.

3/ Includes errors and omissions as well as privatization-related flows equivalent to 0.9 percent in 1999, 0.8 percent in 2000, 1.8 percent in 2001 and 0.3 percent in 2002.

4/ Excludes claims on Nicaragua amounting to US$145.7 million up to 1999 and US$75.7 million in 2000 official data.

Table 12. Guatemala: Summary of External Public Debt

	1998	1999	2000	2001	Proj. 2002
	(In millions of U.S. dollars)				
Outstanding debt 1/	**2,907**	**3,299**	**3,218**	**3,566**	**3,227**
Medium- and long-term debt	2,641	2,864	2,757	3,255	3,091
Public sector	2,120	2,370	2,287	2,785	2,999
Of which					
Bonds	150	150	150	475	475
CORFINA	372	371	371	371	3
Bank of Guatemala	149	123	99	99	89
Short-term debt	266	435	461	312	136
Public sector 2/	187	356	382	232	135
Bank of Guatemala	1	1	1	1	1
Arrears of interest 3/	78	78	78	78	0
Debt flows					
Drawings	156	254	161	237	49
Public sector 4/	180	280	185	248	59
Bank of Guatemala	-54	-26	-24	-11	-10
BOP support	30	0	0	0	0
Scheduled debt obligations	285	257	267	284	286
Interest	127	127	130	132	161
Public sector	113	117	120	125	157
CORFINA	0	0	0	0	0
Bank of Guatemala	15	10	10	7	4
Principal	158	130	137	152	125
Public sector	103	104	112	141	115
CORFINA	1	1	0	0	0
Bank of Guatemala	54	26	24	11	10
Memorandum items:					
Stock of arrears, end of period 3/	0	0	0	0	0
Interest	0	0	0	0	0
Principal	0	0	0	0	0
	(In percent of GDP)				
Outstanding debt	**15.1**	**18.0**	**16.7**	**16.9**	**14.4**
Medium-term	13.8	15.6	14.3	15.5	13.8
Short-term	1.4	2.4	2.4	1.5	0.6
Of which					
Bank of Guatemala	0.0	0.0	0.0	0.0	0.0
Debt flows					
Drawings	0.8	1.4	0.8	1.1	0.2
Scheduled debt obligations	1.5	1.4	1.4	1.3	1.3
Interest	0.7	0.7	0.7	0.6	0.7
Principal	0.8	0.7	0.7	0.7	0.6
Memorandum items:					
Stock of arrears, end of period	0.5	...	0.0	0.0	0.0
Interest	0.4	...	0.0	0.0	0.0
Principal	0.1	...	0.0	0.0	0.0
	(In percent of exports of goods and nonfactor services)				
Total debt service	8.3	7.5	6.9	7.3	6.9
Interest	3.7	3.7	3.4	3.4	3.9
Principal	4.6	3.8	3.5	3.9	3.0
Nominal GDP (in U.S. dollars)	19,193	18,316	19,288	21,065	22,471

Sources: Bank of Guatemala; and Fund staff estimates.

1/ Includes arrears and valuation adjustments.
2/ Includes bonded debt.
3/ Excludes arrears in grace period.
4/ Includes state financial institutions, except CORFINA and Bank of Guatemala.

Table 13. Guatemala: Medium-Term Projections

					Prel.	Proj. 1/				
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Real GDP growth	**4.4**	**5.0**	**3.8**	**3.6**	**2.1**	**2.3**	**3.0**	**3.5**	**4.0**	**4.5**
Real per-capita income growth 2/	**1.6**	**2.3**	**1.1**	**0.9**	**-0.5**	**-0.3**	**0.5**	**1.0**	**1.6**	**1.6**
Consumer prices (end-period)	**7.1**	**7.5**	**4.9**	**5.1**	**8.9**	**6.0**	**4.5**	**3.0**	**3.0**	**3.0**
ICOR	**2.2**	**2.4**	**3.4**	**3.6**	**6.4**	**6.0**	**6.4**	**4.0**	**3.5**	**3.6**
	(In percent of GDP)									
Savings and investment										
Gross domestic investment	13.7	17.4	17.4	17.0	15.4	16.4	17.4	17.5	17.6	17.6
Public	3.0	4.3	5.5	4.1	4.2	4.0	4.2	4.0	4.1	4.1
Private	10.6	13.1	11.9	12.9	11.2	12.4	13.2	13.5	13.5	13.5
National savings	10.1	12.2	11.8	11.6	9.5	11.6	12.7	13.0	13.3	13.3
Public	3.1	2.4	2.6	2.0	1.7	2.3	3.1	2.9	3.0	3.0
Private	7.1	9.8	9.3	9.6	7.8	9.3	9.6	10.1	10.3	10.3
Overall balance combined public sector	**-0.6**	**-1.8**	**-3.0**	**-2.2**	**-2.3**	**-1.5**	**-0.9**	**-0.9**	**-0.9**	**-0.9**
Financing	0.6	2.1	3.0	2.2	2.3	1.5	0.9	0.9	0.9	0.9
External (net)	1.9	1.5	2.3	0.8	1.1	0.4	1.0	1.0	1.0	1.0
Domestic (net)	-1.3	-2.7	0.1	0.7	-0.6	0.8	-0.1	-0.1	-0.1	-0.1
Sale of assets	0.0	3.1	0.6	0.7	1.8	0.3	0.0	0.0	0.0	0.0
Central government										
Revenues	9.4	9.7	10.5	10.5	11.2	11.5	12.1	12.8	13.1	13.4
Of which										
Tax revenues	8.8	8.7	9.3	9.5	9.8	10.7	11.0	12.0	12.3	12.6
Expenditures	10.1	11.9	13.3	12.6	13.8	12.8	13.2	13.9	14.2	14.5
Of which										
Social and other peace related	4.3	5.8	6.3	5.9	5.5	5.3	5.7	6.4	6.7	7.0
Interest payments	0.8	1.1	1.3	1.2	1.4	1.3	1.3	1.5	2.1	2.0
External sector										
Current account	-3.5	-5.3	-5.5	-5.4	-5.9	-4.8	-4.7	-4.5	-4.3	-4.3
Of which										
Exports, f.o.b.	14.6	14.7	15.2	16.0	13.6	13.2	13.6	14.3	15.1	15.8
Imports, c.i.f.	-21.7	-24.0	-24.9	-26.8	-26.6	-27.2	-28.1	-29.0	-30.2	-31.4
Capital account	5.2	6.4	4.9	9.2	8.3	3.9	5.4	5.3	5.3	5.3
Official capital and transfers	1.9	1.6	2.0	1.5	1.7	0.7	2.0	2.2	2.1	2.0
Private sector	3.3	4.9	2.9	7.7	6.6	3.1	3.4	3.2	3.2	3.3
Net international reserves 3/	**2.2**	**2.7**	**2.2**	**3.4**	**4.0**	**3.3**	**3.3**	**3.3**	**3.3**	**3.3**
In percent of short-term external debt on a remaining maturity basis	78.0	78.3	73.7	121.0	165.6	135.0	139.8	143.6	146.7	151.9
Total public debt	**18.6**	**17.6**	**20.4**	**22.5**	**23.1**	**20.8**	**26.1**	**25.7**	**31.2**	**30.2**
External	15.5	15.1	18.0	16.7	16.9	14.4	14.7	15.6	16.4	17.0
Domestic 4/	3.1	2.5	2.4	5.8	6.2	6.4	11.4	10.1	14.8	13.2

Source: Fund staff estimates and projections.

1/ Assumes additional fiscal adjustment to reach a tax ratio of 12 percent of GDP by 2004 and between 12.5 and 13 percent of GDP in 2006.

2/ In 2002-06, the annual population growth rate is assumed to remain at 2.7 percent.

3/ In months of imports of goods and services. Excludes claims on Nicaragua amounting to US$145.7 million, up to 1999 and US$75.7 million in 2000, which are recorded in official data.

4/ Assumes an increase of 6 percent of GDP in 2003 to capitalize the central bank, and of 6 percent of GDP in 2005 to reform the social security system.

Table 14. Guatemala: Public Sector Debt Sustainability Framework, 1997-2007

	Actual					Projections					
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
I. Baseline Medium-Term Projections 1/											
Public debt/revenues	212.2	200.5	206.6	214.1	215.6	193.9	222.7	208.7	200.5	189.2	193.4
Public debt/GDP	19.9	19.4	21.7	22.5	24.1	21.7	26.9	26.7	26.3	25.3	25.9
Change in public debt/GDP	-1.9	-0.5	2.2	0.8	1.7	-2.43	5.22	-0.23	-0.44	-0.92	0.57
Net debt-creating flows/GDP (lines 5+8+11)	-2.0	-3.8	0.4	-0.7	-1.4	-0.58	-0.91	-1.01	-0.88	-0.85	-0.86
Overall deficit, excluding gross interest payments/GDP (=primary deficit)	-0.3	0.6	1.6	1.0	0.9	0.00	-0.60	-0.60	-1.20	-1.10	-1.10
Revenue and grants/GDP	9.4	9.7	10.5	10.5	11.2	11.20	12.10	12.80	13.10	13.40	13.40
Non-interest expenditure/GDP	9.1	10.3	12.1	11.5	12.1	11.20	11.50	12.20	11.90	12.30	12.30
Minus nondebt creating financing flows/GDP	0.0	-3.0	-0.9	-0.8	-1.7	-0.26	0.00	0.00	0.00	0.00	0.00
Privatization Receipts/GDP	0.0	3.0	0.9	0.8	1.7	0.26	0.00	0.00	0.00	0.00	0.00
Other	0.0	0.0	0.0	0.0	0.0	0.00	0.00	0.00	0.00	0.00	0.00
(r-g-(π+gπ))/(1+g+π+gπ))debt/GDP (lines 13/12)	-1.7	-1.4	-0.3	-0.9	-0.7	-0.32	-0.31	-0.41	0.32	0.25	0.24
Adjustment factor: 1+g+π+gπ	1.1	1.1	1.1	1.1	1.1	1.08	1.09	1.08	1.07	1.07	1.07
(r-g-(π+gπ))debt/GDP (lines 14+15+16)	-1.9	-1.6	-0.3	-0.9	-0.8	-0.35	-0.34	-0.44	0.35	0.27	0.25
r (interest rate) times debt/GDP	1.0	1.3	1.5	1.4	1.5	1.62	1.66	1.61	2.25	2.14	2.14
minus g (real GDP growth rate) times debt/GDP	-1.0	-1.0	-0.7	-0.8	-0.5	-0.56	-0.65	-0.94	-1.07	-1.05	-1.01
minus (π + gπ) (π = GDP deflator, growth rate) times debt/GDP	-1.9	-2.0	-1.0	-1.5	-1.8	-1.41	-1.34	-1.12	-0.83	-0.82	-0.87
Residual, incl. change in assets and valuation changes on external debt /GDP (lines 3-4)	0.1	3.3	1.8	1.5	3.1	-1.85	6.13	0.78	0.43	-0.07	1.43
Memorandum items:											
Key macro and external assumptions											
Nominal GDP (local currency)	107.9	124.0	135.3	149.7	165.0	178.4	197.3	212.3	227.5	243.7	261.0
Real GDP growth (in percent per year)	4.4	5.0	3.8	3.6	2.1	2.3	3.0	3.5	4.0	4.0	4.0
Consumer price index (change, in percent per year)	9.2	6.6	4.9	5.2	6.0	7.3	6.0	4.0	3.0	3.0	3.0
GDP deflator (change, in percent per year)	8.5	9.4	5.1	6.8	7.9	5.7	6.0	4.0	3.0	3.0	3.3
Average interest rate on public debt (percent per year)	4.4	6.7	7.7	6.3	6.9	6.7	7.6	6.0	8.4	8.2	8.5
Growth of revenues (deflated by GDP deflator, in percent per year)	6.4	8.5	12.4	3.6	8.9	2.3	12.7	9.5	6.4	6.4	3.7
Growth of non-interest expenditure (deflated by GDP deflator, in percent per year)	17.9	18.9	21.7	-2.0	7.8	-5.3	7.1	9.8	1.4	7.5	3.7
II. Stress Tests											
1. If interest rate, real GDP growth rate, primary balance and nondebt flows (in percent of GDP) are at average of past 10 years						21.3	26.4	26.4	26.4	25.9	26.8
2. If interest rate in 2002 and 2003 is average plus two standard deviations, others at baseline						22.0	27.3	27.1	26.6	25.7	26.3
3. If real GDP growth rate in 2002 and 2003 is average minus two standard deviations, others at baseline						21.8	27.2	26.9	26.5	25.6	26.2
4. If primary balance (in percent of GDP) in 2002 and 2003 is average minus two standard deviations, others at baseline						24.1	32.2	31.9	31.5	30.6	31.2
5. Combination of 2-4 using one standard deviation shocks						23.0	30.1	29.8	29.4	28.5	29.1
6. One time 30 percent depreciation in 2002, others (except primary balance) at baseline						26.2	31.3	31.0	30.7	29.8	30.4

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

1/ The public debt baseline projection includes an increase of 6 percent of GDP in 2003 to capitalize the central bank, and of 6 percent of GDP in 2005 to reform the social security system.

Table 15. Guatemala: External Sustainability Framework, 1997-2007

	Actual					Projections					
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
I. Baseline Medium-Term Projections 1/											
External debt/exports of G&S	141.3	146.5	173.4	166.0	183.2	190.6	194.5	194.6	191.8	187.3	200.4
External debt/GDP	25.9	27.3	33.7	35.1	36.6	36.4	38.7	41.1	43.0	44.5	45.9
Change in external debt/GDP	0.9	1.4	6.4	1.4	1.5	-0.2	2.3	2.4	1.8	1.5	1.3
Net debt-creating external flows/GDP (5+9+12)	0.0	0.0	6.0	2.5	0.8	2.1	2.6	1.3	0.5	0.1	-0.7
Current account deficit, excluding interest payments/GDP	2.8	4.7	4.8	4.7	5.0	3.8	3.6	3.2	3.0	3.0	3.0
Deficit in balance of G&S/GDP	.	.	9.4	9.9	10.6	11.9	12.1	12.0	11.9	11.8	13.5
Exports of G&S/GDP	18.3	18.6	19.4	21.1	20.0	19.1	19.9	21.1	22.4	23.8	22.9
Imports of G&S/GDP	25.3	27.7	28.9	31.1	30.6	31.0	32.0	33.1	34.3	35.6	36.3
Minus net nondebt creating capital inflows/GDP	-0.5	-3.5	-0.8	-1.2	-2.2	-0.7	-0.7	-1.0	-1.3	-1.6	-1.8
Net foreign direct investment, equity/GDP	0.5	3.5	0.8	1.2	2.2	0.7	0.7	1.0	1.3	1.6	1.8
Net portfolio investment,equity/GDP	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
(r-g-(ρ+gρ))/(1+g+ρ+gρ))debt/GDP (14/13)	-2.2	-1.2	2.0	-0.9	-2.1	-1.0	-0.3	-0.9	-1.2	-1.3	-1.8
Adjustment factor: 1+g+ρ+gρ	1.1	1.1	1.0	1.1	1.1	1.1	1.0	1.1	1.1	1.1	1.1
(r-g-(ρ+gρ))debt/GDP (15+16+17)	-2.6	-1.3	1.9	-1.0	-2.3	-1.1	-0.3	-0.9	-1.3	-1.4	-2.0
r (interest rate) times debt/GDP	0.9	0.8	0.7	0.8	0.9	1.1	1.2	1.4	1.4	1.4	1.4
minus g (real GDP growth rate) times debt/GDP	-1.1	-1.3	-1.0	-1.2	-0.7	-0.8	-1.1	-1.4	-1.6	-1.7	-1.8
minus (ρ + gρ) (ρ = US dollar value of GDP deflator, growth rate) times debt/GDP	-2.4	-0.7	2.3	-0.6	-2.5	-1.3	-0.4	-0.9	-1.0	-1.0	-1.6
Residual, incl. change in gross foreign assets/GDP (3-4)	0.9	1.4	0.4	-1.2	0.8	-2.3	-0.3	1.1	1.3	1.4	2.0
Memorandum items:											
Key macro and external assumptions											
Nominal GDP (local currency)	107.9	124.0	135.3	149.7	165.0	178.4	197.3	212.3	227.5	243.7	261.0
Nominal GDP (in U.S. dollars)	17.8	19.2	18.3	19.3	21.1	22.5	23.5	24.9	26.5	28.1	29.9
Real GDP growth (in percent per year)	4.4	5.0	3.8	3.6	2.1	2.3	3.0	3.5	4.0	4.0	4.0
Nominal GDP deflator (in U.S. dollars, change in percent per year)	9.1	2.7	-8.1	1.6	7.0	3.5	1.0	2.3	2.3	2.3	3.5
External interest rate (percent per year)	3.6	3.0	2.4	2.5	2.7	2.9	3.2	3.5	3.4	3.2	3.2
Growth of exports of G&S (in U.S. dollar terms, in percent per year)	15.0	9.8	-0.4	14.5	3.3	2.0	8.9	12.3	12.8	12.8	2.4
Growth of imports of G&S (in U.S. dollar terms, in percent per year)	18.0	18.2	-0.5	13.2	7.6	7.9	8.1	9.5	10.3	10.1	8.7
II. Sensitivity Analysis for External Debt-to-GDP Ratio											
1. If interest rate, real GDP growth rate, US$ GDP deflator growth, non-interest current account, and non-debt flows (in percent of GDP) are at average of past 10 years						35.7	36.8	39.3	41.8	44.4	47.4
2. If interest rate in 2002 and 2003 is average plus two standard deviations, others at baseline						37.2	40.3	42.6	44.4	45.9	47.2
3. If real GDP growth rate in 2002 and 2003 is average minus two standard deviations, others at baseline						36.5	39.1	41.5	43.3	44.9	46.2
4. If US$ GDP deflator in 2002 is average minus two standard deviations, others at baseline						39.9	42.2	44.5	46.3	47.7	48.9
5. If non-interest current account (in percent of GDP) in 2002 and 2003 is average minus two standard deviations, others at baseline						39.6	45.2	47.5	49.1	50.5	51.6
6. Combination of 2-5 using one standard deviation shocks						40.0	44.8	47.1	48.7	50.1	51.2
7. One time 30 percent depreciation in year 2002 (-30% GDP deflator shock), others at baseline.						53.5	55.7	57.7	59.0	60.1	60.8

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

1/ The stock of external private sector debt is derived using medium-and long-term debt flows to the private sector as reported in the balance of payments. The initial stock starting in 1991 is taken from the BIS data. At end 2001, the derived stock of external private sector debt amounted to US$4.1 billion, about 50 percent higher than the stock reported by the BIS data, which only accounts for a subset of external private sector borrowing.

Table 16. Guatemala: External Financing Requirements and Sources

(In millions of U.S. dollars)

	1998	1999	2000	2001	Proj. 2002
Gross financing requirements	1,639	1,328	2,310	2,393	1,154
External current account deficit					
(excludes official transfers)	1,036	1,015	1,049	1,238	1,078
Of which					
Coffee exports	581	588	572	305	292
Non-traditional exports	1,680	1,725	1,907	1,911	2,011
Debt amortization	360	439	534	655	286
Public sector	157	231	137	152	125
Loans 1/	157.4	130	137	152	125
Deposits	0	101	0	0	0
Short-term debt 2/	203	208	397	503	162
Net reserves accumulation	243	-126	728	500	-210
IMF repurchases and repayments	0	0	0	0	0
Available financing	1,639	1,328	2,310	2,393	1,154
Foreign investment (net)	673	155	230	456	151
Debt financing from private creditors	539	706	1,740	1,657	617
To public sector (bonds)	269	345	488	678	66
To commercial banks (net)	103	-37	110	-53	-43
To private sector (net)	168	398	1,143	983	594
Deposits in foreign banks	0	0	0	49	0
Official credit to the public sector	397	468	341	280	386
Official transfers	71	68	85	93	97
Borrowing	326	400	255	187	289
Balance of payments support	30	0	0	0	0
IMF (net)	0	0	0	0	0
Accumulation of arrears (exceptional)	0	0	0	0	0
Financing gap	0	0	0	0	0

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

1/ Excludes the IMF.

2/ Original maturity of less than one year. Stock at the end of the previous period.

GUATEMALA—FUND RELATIONS

(As of July 31, 2002)

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	6.73	22.69

IV. Outstanding Purchases and Loans: None

V. Financial Arrangements:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	4/1/02	3/31/03	84.00	0.00
Stand-By	12/18/92	03/17/94	54.00	0.00
Stand-By	10/26/88	02/28/90	54.00	23.16
Stand-By	08/31/83	12/31/84	114.75	57.38

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

	Overdue	Forthcoming				
	06/30/2002	2002	2003	2004	2005	2006
Charges/interest	0.0	0.5	0.5	0.5	0.5	0.5
Total	**0.0**	**0.5**	**0.5**	**0.5**	**0.5**	**0.5**

VII. Safeguards Assessment

Under the Fund's safeguards assessment policy, the Bank of Guatemala (BANGUAT) is subject to a safeguards assessment with respect to the Stand-By Arrangement approved on April 1, 2002, and expiring on March 31, 2003. The safeguards assessment was completed on August 9, 2002. The assessment concluded that the BANGUAT's procedures and controls to manage resources, including IMF disbursements, are not adequate in all areas of the IMF's safeguards framework. Therefore, specific remedial actions to address identified vulnerabilities have been recommended to the authorities.

VIII. Exchange Rate Arrangements

Since March 1994, Guatemala has 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 central bank is supposed to intervene in the market only to moderate exchange rate fluctuations as well as to purchase foreign exchange to service public sector debt. As of July 31, 2002 the exchange rate in the interbank market was Q 7.81 per U.S. dollar.

IX. Last Article IV Consultation

The last Article IV consultation was concluded by the Executive Board on May 14, 2001 (EBM/01/49, the relevant documents were SM/01/116 and SM/01/139). Guatemala is on the standard 12-month consultation cycle.

X. 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 a MAE mission provided assistance on payments system issues. On February 2001, MAE provided assistance on bank restructuring. On May 2001 FAD provided assistance on tax policy and administration. On February 2002 FAD provided assistance on expenditure management.

GUATEMALA—RELATIONS WITH THE WORLD BANK GROUP

I. Financial Relations

(In millions of U.S. dollars as of July 31, 2002)

A. IBRD Operations by Sector

	Disbursed	Undisbursed
Agriculture	22.9	35.1
Education	81.3	64.3
Electric power and other energy	194.8	0.0
Finance	16.8	0.0
Structural adjustment	120.0	0.0
Public sector management	53.0	96.4
Social protection	76.8	22.7
Telecommunications	69.2	0.0
Transportation	99.1	27.1
Urban development	34.1	0.0
Water supply and sanitation	3.6	0.0
Total IBRD	**771.6**	**400.5**
Repaid principal	420.6	
Debt outstanding [1]	341.6	

IBRD Loan Disbursements (US$ millions, as of July 31, 2002)	1997	1998	1999	2000	2001	2002
Total net disbursement	**4.3**	**15.2**	**55.9**	**38.2**	**34.7**	**11.5**
Gross disbursements	16.5	29.5	70.5	51.4	46.3	18.1
Principal repayments	12.2	14.3	14.5	13.2	11.6	6.6

Source: World Bank

1/ Including exchange rate adjustment (-US$9.4 million).

II. Recent IBRD Activities

Bank assistance to Guatemala intensified considerably during the last Country Assistance Strategy (CAS) implementation period, from 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 an special focus on gender and indigenous issues. In order to set forth Bank assistance plans during the interim period (2002–2003) until the next CAS is ready, a 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.

As of July 31, 2002 the IBRD portfolio contains fourteen investment projects for a total commitment of US$575 million, of which US$401 million remains undisbursed. The portfolio is relatively new (the average implementation period is less than three years), as all projects have become effective after 1998. The two most recent projects are the Financial Sector Adjustment Loan (FSAL) for US$150 million and the Financial Sector Technical Assistance Loan for US$5 million. The latter will support the technical needs of the government for the proper implementation of the financial reforms supported by the FSAL.

Future assistance: there are two projects under preparation for fiscal year 2003 with a combine total of US$180 million: the Rural Roads project and the Social Infrastructure and Safety Nets. Other areas receiving increased attention include the financial and governance sectors, and it is likely that the next CAS will also emphasize health and malnutrition issues more than in the past, reflecting the findings of the highly inclusive Poverty Assessment and the Government's Poverty Reduction Strategy Paper.

GUATEMALA—RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK
(As of July 31, 2002)

I. IDB Current Portfolio as of July 31, 2002
(In millions of U.S. dollars)

Sector	**Approved**	**Undisbursed**
Social sectors	431.9	272.4
Community development	264.8	134.1
Credit to micro-enterprises	10.0	0.0
Environment	64.3	60.4
Housing	60.0	6.9
Education	37.4	22.5
Health	55.4	55.4
Physical infrastructure	192.8	152.7
Agriculture	33.0	29.3
Reform loans	39.1	21.1
Infrastructure and investment	7.7	0.6
Customs	1.4	0.1
Justice	25.0	15.3
Trade	5.0	5.0
Financial sector reform	200.0	200
Emergency assistance	40.0	0.9
Technology development	10.7	10.7
Total	**1,007.5**	**693.9**

A. IDB Loan Disbursements

	1997	1998	1998	2000	2001	2002 1/
Disbursements	**100.9**	**146.6**	**176.6**	**68.0**	**98.5**	**215.9**
Amortization	42.6	45.5	50.4	46.0	38.8	46.0
Interest and charges	31.7	33.7	41.2	46.0	49.5	61.9
Net cash flow	**26.6**	**67.4**	**85.0**	**-24.0**	**10.2**	**108.0**

1/ Estimated for 2002.

B. Recent Economic and Sector Missions

The most recent economic strategy document on Guatemala (Country Paper) was approved by the IDB Board of Directors in September 2001. The Bank's priority, outlined in this document, is to help the government to reduce poverty. The Bank's implementation strategy focuses on three pillars: (i) economic growth, macroeconomic stability, and competitiveness; (ii) human capital development, social protection, and equity; and (iii) modernization of the state and governance.

In the 1999–2000 period, the Bank approved loans to support technology development (US$11 million), to modernize the road system (US$150 million), to help municipal development (US$20 million), and to improve health services (US$55 million). The Bank has also supported the implementation of the Fiscal Pact, approved in May 2000, through a comprehensive technical cooperation program. In 2001, the Bank has approved loans to strengthen the ministry of economy (US$5 million), and to expand the education reform (US$22 million). About 90 percent of the projects are current, and are expected to meet their development objectives. In 2002, the Bank approved a financial sector reform loan for (US$200 million), a loan to improve the environment in high basin areas (US$40 million),a loan to help improve the labor market (US$10 million), and a loan for US$46.8 million to combat urban poverty. Other operations in preparation include programs in the areas of rural electricity, water in rural areas, security, poverty reduction, housing, environment, social protection, and micro-credit. The Bank is also helping the authorities to define a strategy to reduce poverty. Other non-financial activities include the Bank's coordination of the Consultative Group meetings with the next meeting scheduled for February 11–12, 2002 at the IDB headquarters.

C. Tentative Schedule of Disbursements

	2001	**2002** 1/	**2003** 2/
Disbursements	**98.5**	**215.9**	**150.0**
Amortization	38.8	44.3	55.0
Interest and charges	49.5	61.9	61.6
Net cash flow	**10.2**	**108.0**	**33.4**

1/ Preliminary figures.
2/ Projected in the pipeline.

GUATEMALA—STATISTICAL ISSUES

The Guatemalan authorities have made efforts to improve the macroeconomic statistical systems 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 mentioned below, except for government finance, the authorities are beginning to address problems with help from STA.

National accounts statistics

Guatemala's national accounts are produced by the central bank based on the 1953 U.N. System of National Accounts (SNA) with 1958 as the base year. The coverage of national accounts statistics is limited to (i) GDP at constant (1958) prices by industry; and (ii) GDP at both constant and current prices, by expenditure components. Data are published annually with preliminary data available with a lag of about three months. With the assistance of a U.N. statistical advisor, the central bank is implementing the 1993 SNA with 1998 as the base year. STA has 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. With respect to the CPI, the NSI 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.

Monetary authorities

Data on the monetary authorities, commercial banks, and other financial institutions are being compiled on a monthly basis and sent regularly to the Fund for publication in the IFS. In 1998 a technical assistance mission recommended to the Bank of Guatemala (BOG) measures to improve the data compilation of the financial system. Such measures included: (i) the compilation of monetary statistics for savings and credit cooperatives; (ii) the revision of the money and credit aggregates; (iii) the classification of domestic institutional units into central and local governments, nonfinancial 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) the breakdown between residents and nonresidents in the monetary accounts. A recent monetary and financial statistics mission (September 2001) advised the BOG to establish a work plan to undertake all of these recommendations. However, the work plan is yet to be developed.

Government finance statistics

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, little work has been made in improving 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

The balance of payments statistics are based on reports of foreign exchange transactions from commercial banks and customs but with considerable lags. The balance of payments data are prepared quarterly and compiled and presented according to the principles of the fourth edition of the balance of payments manual *(BPM4)*. A number of surveys have been introduced to collect information according to the guidelines of the fifth edition of the Balance of Payments Manual *(BPM5)*. The staff of the Bank of Guatemala is currently being trained to apply the methodology of *BPM5*. The authorities are implementing the recommendations of the STA's 1997 multisector mission in the following areas: (i) improving the accuracy of the foreign exchange records by both the Bank of Guatemala and the reporting banks; and (ii) obtaining import, freight, and insurance data directly from customs documents.

Guatemala: Core Statistical Indicators

(As of June 3, 2002)

	Exchange Rates	Interna-tional Reserves	Reserve/ Base Money	Central Bank Balance Sheet	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	GDP/ GNP	External Debt/ Debt Service
Date of Latest Observation	5/31/02	5/31/02	5/17/02	5/31/02	5/24/02	5/31/02	4/30/02	3/31/02	3/31/02	4/30/02	12/31/01	2001
Date Received	6/03/02	6/03/02	5/24/02	12/28/01	12/28/01	6/03/02	5/15/02	5/15/02	5/15/02	5/27/02	4/19/02	3/02
Frequency of Data	D	D	W	W	M	W	W	M	A	M	A	A
Frequency of Reporting	D	D	W	W	M	W	W	O	O	M	A	A
Source of Update	A	A	A	A	A	A	A	A	A	A	A	A
Mode of Reporting	E/C	E/C	C	C	C	C	C	C	C	C	C/E	C/V
Confidentiality	C	D	D	D	D	C	C	D	D	D	C	D
Frequency of Publication	D	M	M	M	M	D	M	Q	A	A	A	A

1/ D-daily, W-weekly, M-monthly, Q-quarterly, A-annual, or O-other (only when requested).

2/ A-direct reporting by central bank, ministry of finance.

3/ E-electronic data transfer, C-cable or facsimile, T-telephone, M-mail, V-staff visits, or O-other.

4/ (A) for use by the staff only, (B) for use by the staff and the Executive Board, (C) for unrestricted use, (D) embargoed for a specified period and are thereafter for unrestricted use, or (E) subject to other use restrictions.

GUATEMALA: SCHEDULE OF PURCHASES UNDER THE STAND-BY ARRANGEMENT

Date	Amount	Conditions
	(In millions of SDRs)	
April 1, 2002	52.55	Board approval
August 15, 2002	10.48	Observance of end-June 2002 performance criteria and completion of review (August 15, 2002)
November 15, 2002	10.48	Observance of end-September 2002 performance criteria
March 15, 2003	10.48	Observance of end-December 2002 performance criteria

Guatemala City, Guatemala
September 13, 2002

Mr. Horst Köhler
Managing Director
International Monetary Fund
Washington D.C. 20431

Dear Mr. Köhler

1. So far in 2002, economic policies have been implemented in line with the Stand-By Arrangement approved by the Fund. For end-June 2002, the overall public sector deficit and central government expenditure were below the targets, social spending was well above the floor, and the limits on external borrowing were observed. Also tax revenues are increasing faster than expected. In the area of governance, congress passed the law on the office of the comptroller general in May, and two other laws—the laws on probity and procurement—have been already submitted to congress. Moreover, the two structural conditions for completion of the midterm review have been met. In April the Guatemalan congress approved the central bank law, the banking law, the banking supervision law, and the monetary law, as envisaged under the program. As of end-August, the superintendency of financial institutions has completed the on-site inspections according to the schedule agreed in the program, and has agreed on action plans for the banks that need corrective actions to meet the prudential regulations.

2. We are concerned that 12-month inflation remained at 9 percent through June, and the central bank intends to tighten monetary policy more than agreed under the original program to ensure that inflation declines to the range of 4–6 percent during 2002. As a first step, the end-September 2002 ceiling on the net domestic assets of the central bank will be reduced by Q 100 million (equivalent to 1¼ percent of currency issue at end 2001). If monthly inflation in the third quarter averages above 0.3 percent, the end-December ceiling on net domestic assets of central bank will be reduced by another Q 100 million (Table 1). The purpose of the tighter credit policy is to slow the growth in currency issue and as a result there will be no corresponding adjustment to the quarterly target for net international reserves.

3. We would also like to propose the following minor modifications to the performance criteria for total central government expenditure:

- We believe it would be important to allow for some additional spending on social programs. Currently the program allows the government to increase social and total expenditure and the overall public sector deficit by up to US$40 million above the program ceiling, if net external financing from multilateral creditors exceeds the amount projected in the program. We would like to increase this limit from US$40 million to US$60 million on the excess net external financing from multilateral creditors that could be spent on social programs and would raise total expenditure and the overall public sector deficit. The nonconcessional external debt ceiling will be adjusted accordingly. A revised version of paragraph 18 of the Technical Memorandum of Understanding is attached.

- While the end-June ceiling for total central government expenditure was observed, the seasonal pattern for expenditure is likely to be different than we had expected. For this reason, we would like to raise the end-September ceiling for central government expenditure, without changing the ceiling for end-December (Table 2).

- We would also like to clarify the language in the Technical Memorandum of Understanding with regard to the adjustor in paragraph 21, which refers to the lending by the government to the coffee producers. The previous language had incorrectly referred to the bonds issued by the government. The corrected paragraph 21 is attached.

4. We are requesting Board approval of waivers for the non-observance of three performance criteria established under the program, consisting of (i) the floor on net international reserves for end-June; (ii) the ceiling on net domestic assets for end-June; and (iii) the continuous performance criterion on the non-accumulation of external arrears. The end-June performance criteria on net international reserves and net domestic assets were not observed due to a delay in the congress' approval of an IDB loan and in the disbursement of a first installment of US$120 million that is expected to be disbursed in late September and not in June as initially projected. Adjusted by the delay in the disbursement of this loan, the end-June targets on net international reserves and net domestic assets would have been observed. The continuous performance criterion on non-accumulation of external arrears was not observed for a brief period in April due to a delay in the payment of external debt service of two decentralized entities, the municipality of Guatemala City, and EMPAGUA, the municipal enterprise for drinking water, for a total amount of US$11.5 million. Once it became aware of this problem, the central government paid these arrears in May. This performance criterion is now being observed.

5. On this basis, we are requesting that the Board approve the completion of the midterm review under the program, the three waivers and the modification of the ceilings on net domestic assets of the central bank for end-September and end-December 2002, the limit on central government expenditure of end-September 2002, the adjustor on excess external financing from multilateral creditors, and the revised language in paragraph 21.

Sincerely yours,

/s/	/s/
Lizardo Arturo Sosa López	Eduardo Humberto Weymann Fuentes
President of the Bank of Guatemala	Minister of Finance

Table 1. Performance Criterion for the Stock of Net Domestic Assets of the Bank of Guatemala

(In millions of quetzales)

	Ceiling (end of period)
June 30, 2001 (actual)	-6,634
December 31, 2001 (estimated)	-8,933
March 31, 2002 (indicative target)	-8,490
June 30, 2002	-10,080
September 30, 2002	-9,280
December 31, 2002 1/	-6,628

1/ This amount will be adjusted downwards by and additional Q 100 million if average monthly inflation in the third quarter exceeds 0.3 percent.

Table 2. Performance Criterion for the Central Government Expenditure

(In millions of quetzales)

	Ceiling
January 1–June 30, 2001 (actual)	9,560
January 1–December 31, 2001 (estimated)	22,330
January 1–March 31, 2002 (indicative target)	4,665
January 1–June 30, 2002	9,280
January 1–September 30, 2002	15,775
January 1–December 31, 2002	22,515

REVISION TO TECHNICAL MEMORANDUM OF UNDERSTANDING

18. In the event of excess net external financing from the IDB, the World Bank, and the Central American Bank for Economic Integration (CABEI), the limit on the overall public sector deficit will be adjusted upward, the ceiling on the central government's total expenditure and the floor on the central government's social expenditure will be adjusted upward by the full amount of excess external financing up to a maximum of US$15 million during the first half of 2002, US$25 million during the first three quarters of 2002 and US$60 million during 2002. The nonconcessional external debt ceilings for each quarter will be adjusted accordingly by the contracted amount.[13] The targets on net international reserves will be adjusted upward and the limit on net domestic assets will be adjusted downward by the amount of excess net external financing that exceeds these quarterly limits.

21. The limit on the overall deficit of the combined public sector will be adjusted upward (to a more negative value)/downward (to a less negative value), and on the central government expenditure will be adjusted upward (downward) by any excess (shortfall) of lending provided to coffee producers with respect to the equivalent of US$40 million in 2001 and US$60 million in 2002. In any event, the lending provided to coffee producers should not exceed the equivalent of US$100 million over the 2001–02 period.

[13] The program assumes cumulative flows of contracted debt from the IDB, the World Bank, and CABEI of US$540 million during the first half of 2002, US$665 million during the first three quarters of 2002 and US$710 million during 2002.