October 2009
IMF Country Report No. 09/305

Guatemala: First Review Under the Stand-By Arrangement and Requests for Modification of Performance Criterion and Consultation Clause—Staff Report; Staff Supplement; Press Release on the Executive Board Discussion; and Statement by the Executive Director for Guatemala

In the context of the First Review Under the Stand-By Arrangement, the following documents have been released and are included in this package:

- The staff report for the First Review Under the Stand-By Arrangement and Requests for Modification of Performance Criterion and Consultation Clause prepared by a staff team of the IMF, following discussions that ended on August 13, 2009, with the officials of Guatemala on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on September 8, 2009. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- An informational annex to the staff report of September 8, 2009.
- A press release summarizing the views of the Executive Board as expressed during its September 22, 2009 discussion of the First Review Under the Stand-By Arrangement.
- A statement by the Executive Director for Guatemala.

The documents listed below have been separately released.

Letter of Intent sent to the IMF by the authorities of Guatemala*
*Also included in Staff Report

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

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INTERNATIONAL MONETARY FUND

GUATEMALA

First Review Under the Stand-By Arrangement and Requests for Modification of Performance Criterion and Consultation Clause

Prepared by the Western Hemisphere Department
(In collaboration with other departments)

Approved by Patricia Alonso-Gamo (WHD) and Dominique Desruelle (SPR)

September 8, 2009

Executive Summary

Background. An 18 month Stand-By Arrangement (SBA) with total access of SDR 630.6 million (300 percent of quota) was approved by the Executive Board on April 22, 2009. With completion of this review, a total of SDR 462.44 million will be available for drawing. The authorities are treating the arrangement as precautionary.

Economic outcomes. GDP growth has been slower than expected, and is projected to be below ½ percent in 2009. Inflation plummeted to -0.3 percent (y-o-y) at end-July, due to the decline in commodity prices and weak domestic demand. The current account deficit is narrowing sharply because of a large fall in imports, and net capital inflows have declined but the overall balance of payments remains in surplus. The exchange rate has depreciated moderately and international reserves are at adequate levels. The financial system is holding up well.

Policy implementation. Program implementation has been strong. The fiscal deficit is increasing due to a sharp decline in revenues, associated with the contraction in imports and domestic demand. The policy interest rate has been cut. All quantitative performance criteria through June have been met. Inflation has fallen below the consultation band set in the program, triggering a consultation with staff. On the structural front, the amendments to the banking law (end-June structural benchmark) were submitted to Congress in June.

Policy recommendations. Fiscal policy needs to continue striking a balance between avoiding a procyclical stance and maintaining debt sustainability. Monetary policy should remain supportive as long as inflation remains subdued and there are no external pressures. Staff supports the authorities' intention to increase the fiscal deficit in 2009 and 2010, and their request for revising upward the overall balance of the central government (end-September performance criterion) and revising the inflation consultation bands.

Discussions. They were held in Guatemala City during August 3–14. The staff team comprised Mr. López Mejía (Head), Ms. Martin, and Mr. Morra (all WHD), and Mr. Henn (SPR). Mr. Delgado (the new regional resident representative) participated in the policy discussions. The mission met with President Colom, Minister of Finance Fuentes Knight, Central Bank President de Bonilla, Superintendent of Banks Barquín, and other members of the economic cabinet. Mr. Gramajo (OED) joined the policy discussions.

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I. Introduction

1. **The authorities' economic program for 2009–10, supported by the current Stand-By Arrangement (SBA), aims at mitigating the impact of the global crisis**. The strategy is centered on four pillars: a moderate fiscal stimulus to support domestic demand; a monetary policy focused on reducing inflation and a flexible exchange rate to facilitate economic adjustment; a strengthening of financial sector policies to increase banking sector resilience and enhance its safety net and resolution procedures; and a refocusing of public expenditures toward social spending and public investment.

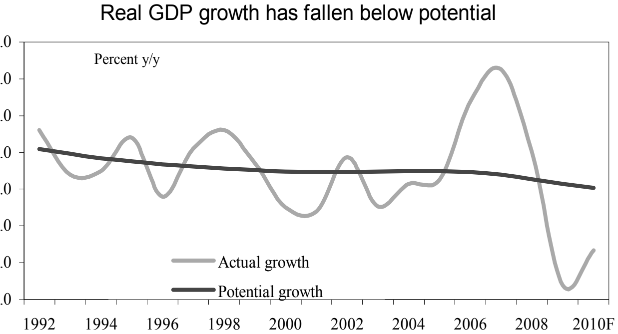
2. **An 18-month SBA in the amount of SDR 630.6 million (300 percent of quota) was approved on April 22, 2009**. The authorities are treating the arrangement as precautionary and their commitment to their economic program remains strong (see attached letter of intent). When approving the SBA, Executive Directors noted that a potentially deeper or longer recession could put further pressure on the balance of payments, and considered that firm implementation of the program was crucial to enhance investor confidence and reduce the risks associated with large external financing requirements and vulnerabilities in the banking sector.

3. **Political tensions have eased since May, but passing legislation remains difficult**. After a standstill of several months, Congress recently passed key legislation, including the authorization to increase bond issuance to finance the 2009 budget. A more transparent process to select judges was approved in June. The selection and appointment of the judges of the country's main tribunals, including the Supreme Court, is scheduled to conclude in October, and is expected to improve judicial administration.

II. Recent Developments

4. **Real GDP growth and inflation have been significantly lower than anticipated**. Output growth slowed from 6 percent in 2006–07 to 4 percent in 2008, with a sharp deceleration in the fourth quarter. Indicators of economic activity suggest that growth could decelerate to below ½ percent in 2009, largely owing to lower investment. The monthly indicator of economic activity slowed to 1.6 percent (y-o-y) in June (down from 2.1 percent a year earlier). Inflation plummeted to -0.3 percent (y-o-y) by end-July, from a peak of 14.2 percent in mid-2008, due to the decline in commodity prices and weak domestic demand conditions (¶15).

Real GDP growth has fallen below potential

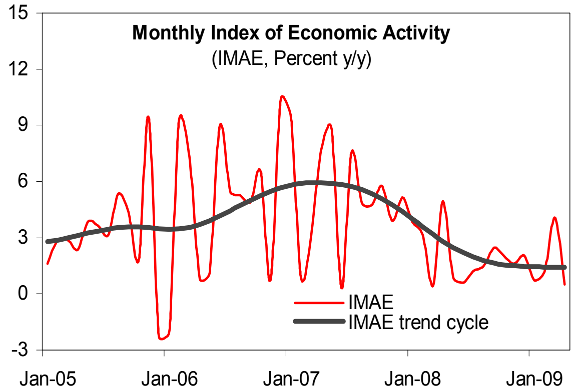


Source: Fund staff estimates

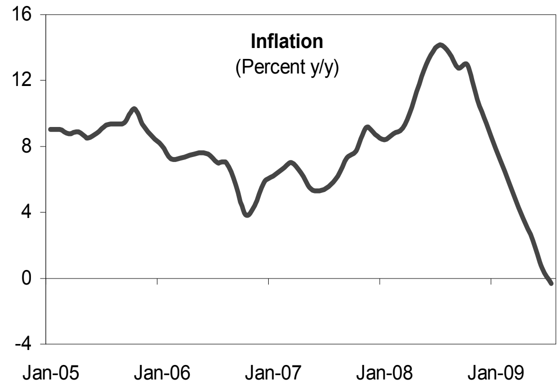
Figure 1. Guatemala: Main Macro Developments

The authorities are implementing policies to mitigate the economic slowdown

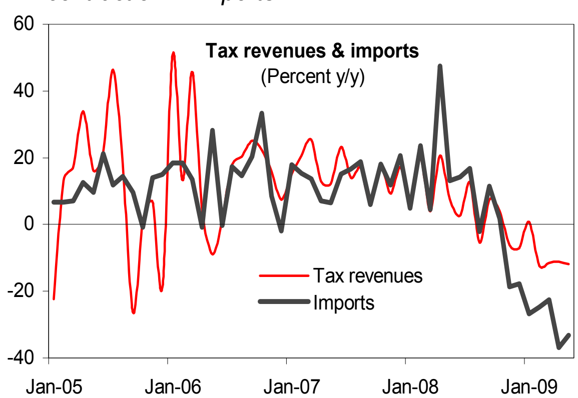
Economic growth has slowed,…



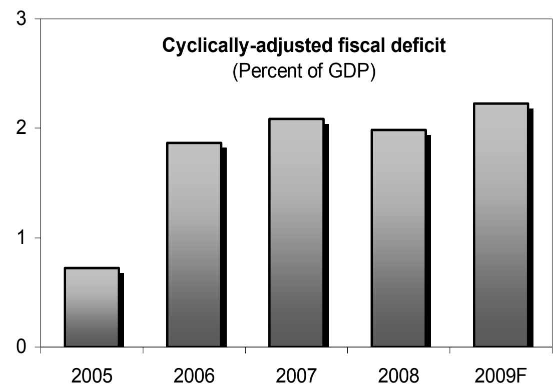
…inflation has declined sharply,…



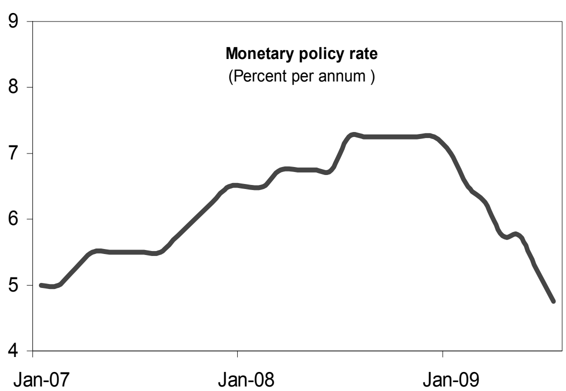
…and tax revenues are falling, partly due to the contraction in imports.



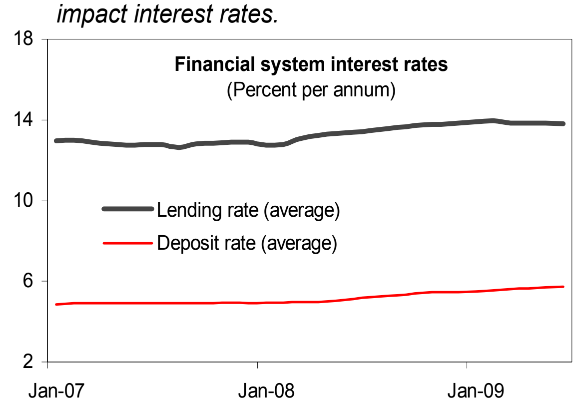
In response, the authorities are implementing a moderate counter-cyclical fiscal policy…



…and have reduced the monetary policy rate.



However, the monetary policy easing has yet to impact interest rates.



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

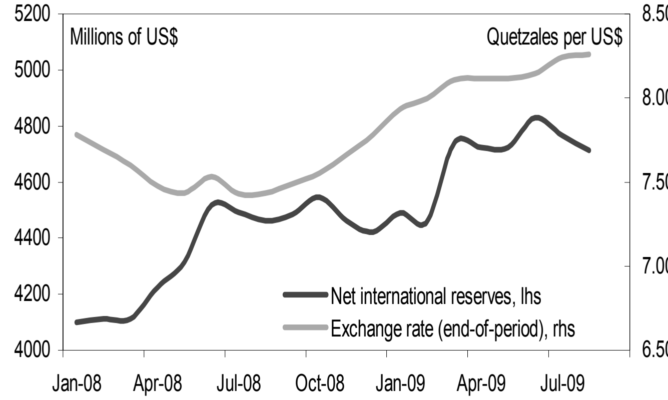
5. **The current and capital accounts are contracting** (Figure 2):

- ***In the first half of the year, the current account turned into surplus driven by a decline in investment and lower oil and food prices***. In the first half of 2009, capital and intermediate goods imports declined by more than 30 percent (y-o-y), as firms adjusted investment plans in light of weak demand. The non-oil import contraction and to a lesser extent the fall in oil and food prices outweighed the declines in total exports, remittances, and tourism receipts, turning the current account balance into surplus.

- ***The capital account surplus is also shrinking, largely in response to lower activity***. As the drop in imports reduced the demand for external credit, private sector debt rollover rates decreased and domestic banks partially repaid external credit lines. Net private credit flows turned negative as a result, partially offsetting inflows from FDI and private borrowing.

6. **The financial system has held up well so far** (Figure 3). Banks' deposits have increased and, as liquidity pressures dissipated, the central bank did not renew the temporary liquidity facilities introduced earlier in the year. The system's capitalization level has remained stable at 13.5 percent of risk-weighted assets. Nonperforming loans have risen moderately from low levels. However, the economic slowdown may further deteriorate the quality of loan portfolios.

Despite the shock to the balance of payments, the exchange rate has depreciated moderately and reserves have remained at adequate levels.



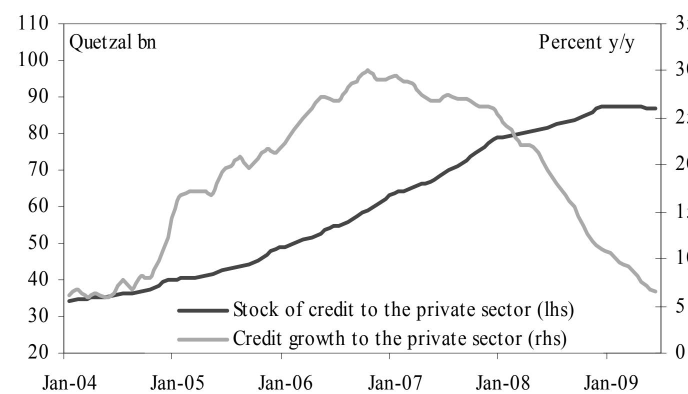
Source: Banguat

Private capital outflows do not seem to reflect a decline in confidence

	2006	2007	2008	2009Q1
	(millions of US$)			
Other private sector investment	**378**	**686**	**624**	**-307**
Financial sector	**43**	**354**	**-181**	**-172**
Assets	-251	-168	-3	-93
of which: Money and Deposits	-21	-87	-66	-101
Liabilities	293	521	-178	-79
of which: Loan Amortization	-117	-6	-319	-89
Non-financial sector	**336**	**333**	**805**	**-135**
Assets	-275	-478	73	29
Liabilities	611	810	732	-164
of which: Commercial Credit	305	452	173	-108
of which: Amortization	-136	-6	-89	-56
Memorandum items:				
Private sector external debt	**6,913**	**8,283**	**8,946**	**8,703**
Financial sector	1,378	1,834	1,781	1,702
Non-financial sector	5,535	6,450	7,165	7,001
Commercial credits	2,350	2,888	3,061	2,953
Loans	3,185	3,562	4,104	4,049

Sources: Banguat, and Fund staff estimates.

Credit growth has come to a halt

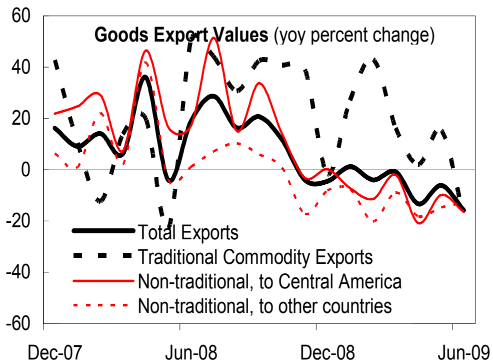


Source: Banguat

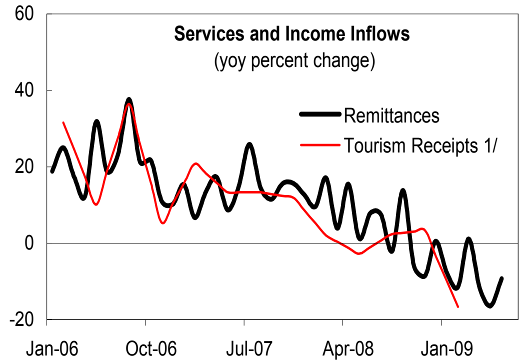
Figure 2. Guatemala: External Sector Developments, 2006-2009

The balance of payments is facing a double blow as a result of the external shock.

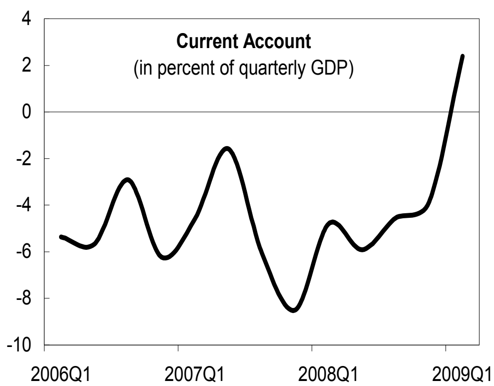
Weak external demand has reduced exports…



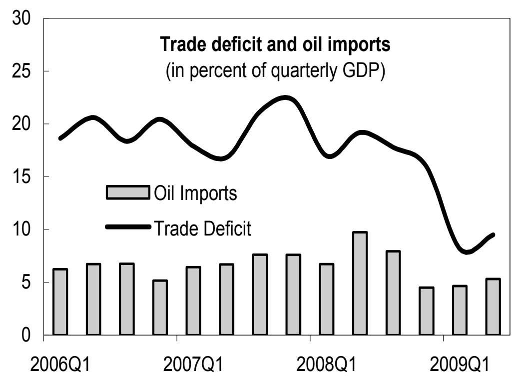
…and remittances and tourism receipts are falling.



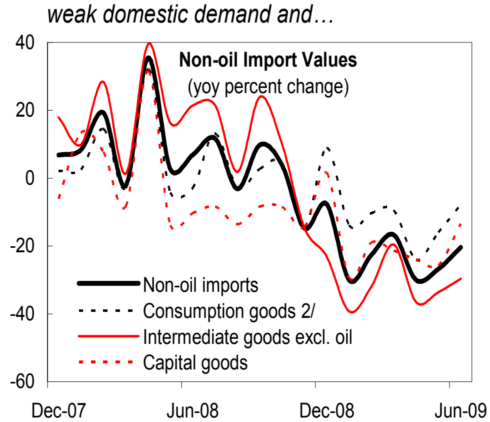
However, the current account turned into surplus in the first quarter of 2009, owing to…



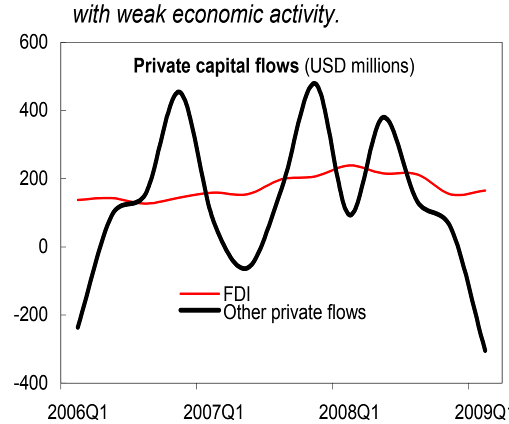
…a lower trade deficit, not associated with oil imports, but rather with…



…a sharp decline in non-oil imports driven by weak domestic demand and…



… large private capital outflows, associated with weak economic activity.



Sources: Banguat; and Fund staff estimates.

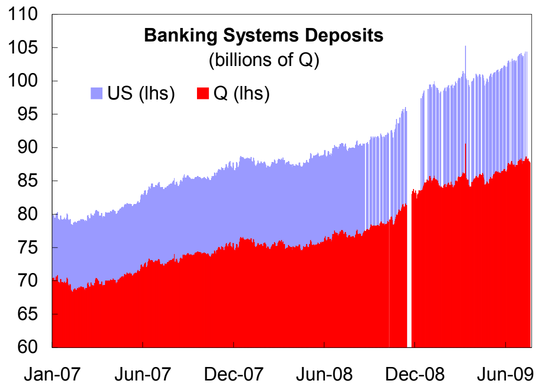
1/ Quarterly BOP data.

2/ The lion's share of 2009 declines in consumption goods imports is caused by lower prices, particularly of durable consumption goods.

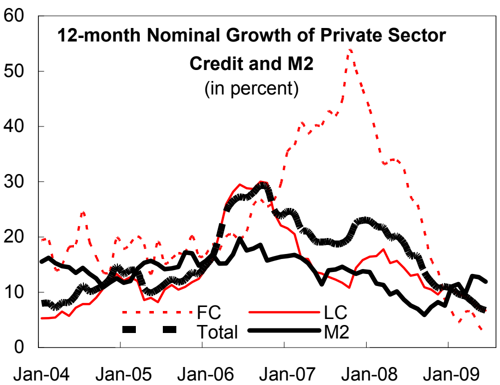
Figure 3. Guatemala: Financial Sector Developments

The financial system is holding up well

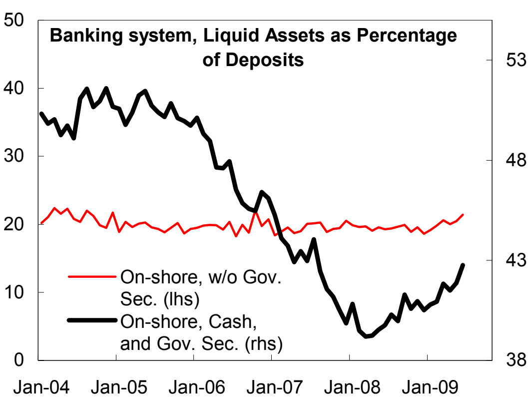
As bank deposits are increasing...



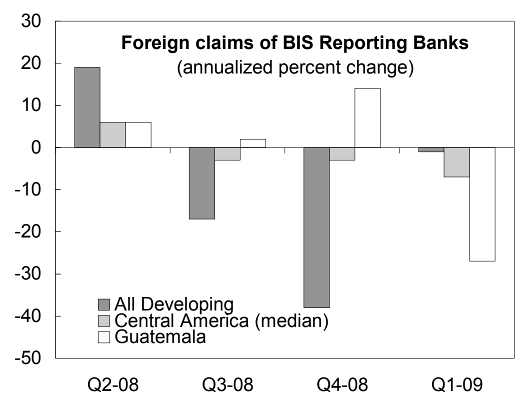
…and demand for credit is slowing...



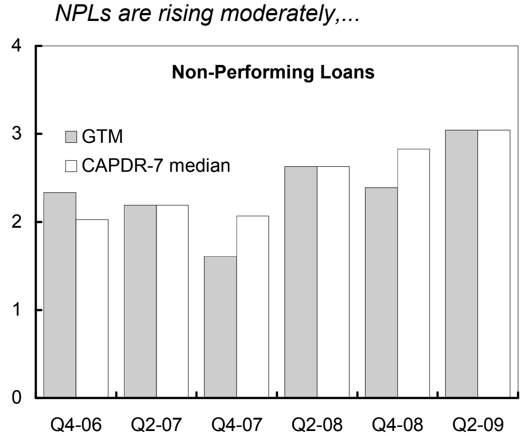
… liquidity is ample ...



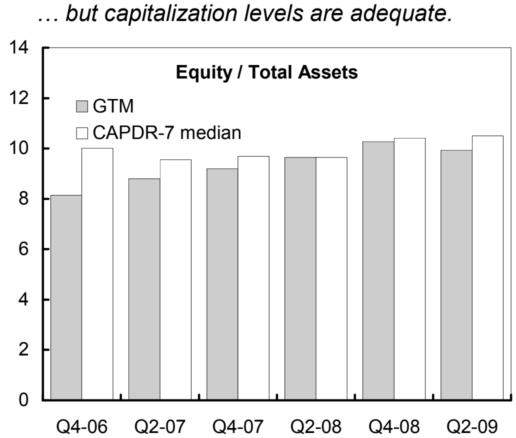
...and banks are paying back their external credit lines.



NPLs are rising moderately,...



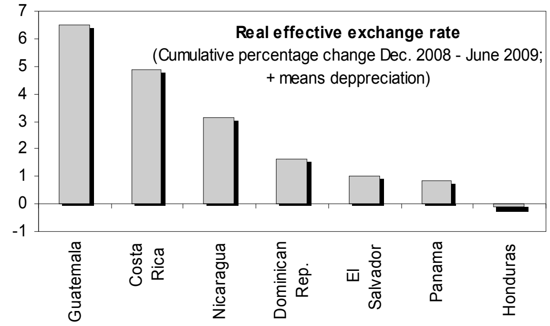
… but capitalization levels are adequate.



Sources: Banguat; Ministry of Finance; BIS; and Fund staff estimates and projections.

7. **The flexible exchange rate regime has facilitated external adjustment**. The real effective exchange rate has depreciated by about 6 percent since end-December 2008, more than in neighboring countries, enhancing competitiveness and remittances' purchasing power. The central bank has undertaken some limited intervention on a discretionary basis to smooth exchange rate volatility. In early September the central bank modified its foreign exchange intervention rule to provide better guidance to market expectations.[1]

The exchange rate has depreciated more than in neighboring countries



Source: Fund staff.

8. **The authorities are implementing counter-cyclical policies to mitigate the economic slowdown**. The Monetary Board reduced the policy interest rate by 250bp since January 2009 to 4.75 percent, but this decline so far has had little impact on the banks' interest rates because of a weak monetary policy transmission and banks' cautious approach to lending given the uncertain economic outlook. The fiscal deficit reached 0.9 percent of GDP in January-July due to an 8 percent (y-o-y) decline in tax revenues associated with the contraction in trade flows and domestic demand, and a boost in spending (13 percent y-o-y during January/June), mainly social expenditure (Figure 4).

9. **The authorities have safeguarded social spending despite the drop in fiscal revenues**. With half of the population living below the poverty line, the government's social protection policy is enhancing existing programs to help offset the effects of the crisis on the neediest. The key conditional cash transfer program initiated in 2008 (*Mi familia progresa*) is being expanded to 0.3 percent of GDP as anticipated, supporting consumption.

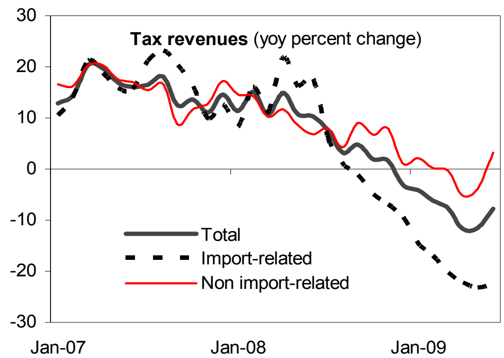
10. **All end-June quantitative performance criteria were met**. The net international reserves and fiscal deficit targets were met by a wide margin. Government deposits at the central bank were below the end-June indicative target, reflecting lower-than-anticipated tax revenues and external disbursements, as well as delays in the approval by Congress of the bond issuance authorization to finance the budget. Inflation fell to 0.6 percent (y-o-y) at end-June 2009, below the consultation band set in the program, triggering a consultation with the staff (¶15). On the structural front, the authorities submitted the amendments to the Banking Law to Congress (end-June structural benchmark).

[1] The new rule allows the central bank to intervene in the foreign exchange market (up to US$24 million daily) when the exchange rate deviates from its 5-day moving average by 0.5 percent (previously 0.75 percent). In addition, the new rule allows for intra-day intervention (previously there was a one-day lag).

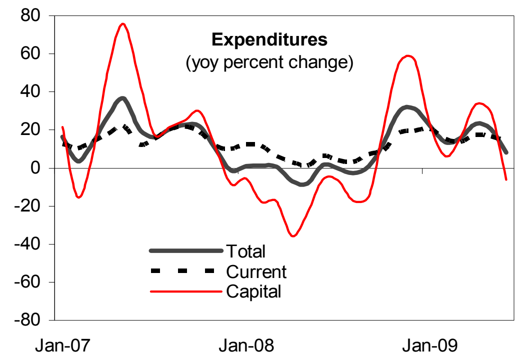
Figure 4. Guatemala: Fiscal Developments

Fiscal policy has become moderately counter-cyclical.

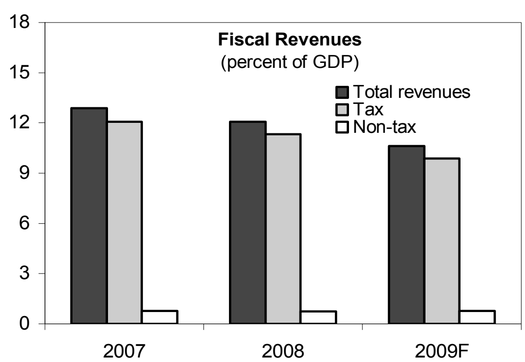
Revenues have fallen sharply, in particular import-related revenues, ...



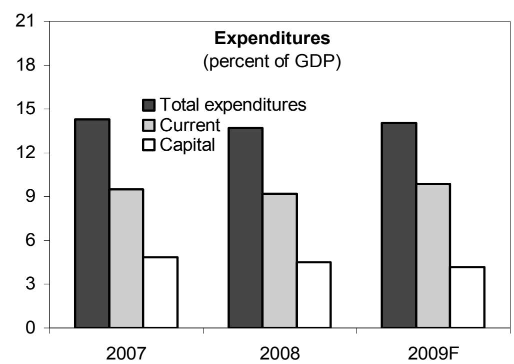
… and expenditures have risen, mostly current expenditures associated with social programs.



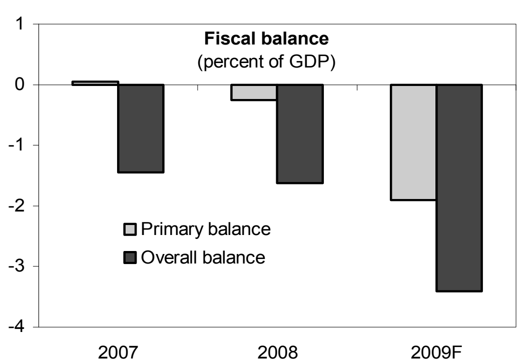
While revenues are projected to fall,...



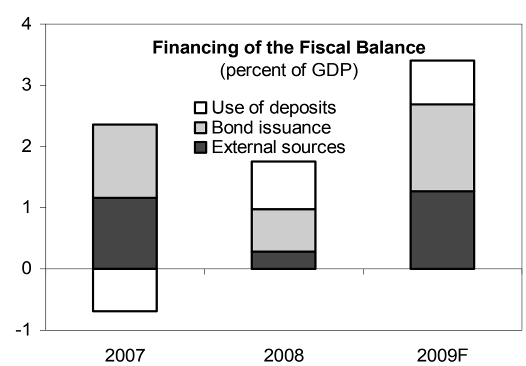
… expenditures will remain stable in percent of GDP,...



… thus increasing the fiscal deficit.



The deficit will be financed by multilateral loans, domestic bond issuance and use of deposits.



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

III. Policy Discussions

A. Macroeconomic Framework

11. **The revised macroeconomic framework reflects the impact of the global crisis on Guatemala**. The recession in the advanced economies and Central America, the associated falls in remittances and private capital flows, and the slowdown in private sector credit growth have dampened growth prospects. High-frequency data do not yet allow to ascertain whether growth has bottomed out. Real GDP growth is now projected to be lower than ½ percent in 2009 (1 percent at program approval), and to pick up moderately to 1.3 percent in 2010. Inflation is projected to reach 1.5 percent in 2009, and rise to 3.8 percent in 2010. The external current deficit is projected to decline to about 1.7 percent of GDP in 2009, down from 4.8 percent in 2008. After posting a small surplus in the first semester of this year due to the economic slowdown and the decline in commodity prices, the current account is projected to turn back into deficit as the economy begins to recover, which may lead to a further moderate depreciation of the exchange rate.

The impact of the global economic crisis has been larger than anticipated

	2007	2008	2009		2010	
			EBS/09/49	rev. proj.	EBS/09/49	rev. proj.
	(in percent of GDP, unless otherwise indicated)					
Real GDP growth (percentage change)	6.3	4.0	1.0	0.4	1.8	1.3
Inflation (percentage change, end of period)	8.7	9.4	5.5	1.5	4.7	3.8
Central government balance	-1.4	-1.6	-2.8	-3.4	-2.6	-3.0
Public sector debt	21.8	20.2	22.8	23.2	24.4	25.6
External current account balance	-5.2	-5.2	-4.0	-1.7	-4.9	-3.3
Capital account balance	4.7	4.1	2.7	2.3	3.6	3.2
of which: Foreign direct investment (FDI)	2.1	2.1	1.5	1.8	1.6	1.8
of which: Non-FDI	2.6	2.0	1.2	0.5	2.0	1.3
Net international reserves (in US$ billion)	4.1	4.4	4.4	4.7	4.4	4.9

Sources: Banguat; Ministry of Finance; and Fund staff projections.

B. Fiscal Policy

12. **There was agreement to revise upward the 2009 fiscal deficit target to 3.4 percent of GDP** (compared to 2.8 percent in the original program). Government revenues are expected to fall below the original program projections by about 7 percent due to the sharper-than-expected decline in imports and a steeper economic slowdown. The new deficit target fully accommodates automatic stabilizers, helps protect social spending, is still consistent with a positive fiscal impulse of about 0.4 percent of GDP (compared to 0.6 percent of GDP originally in the program), and leads to a moderate increase in public debt. The higher deficit

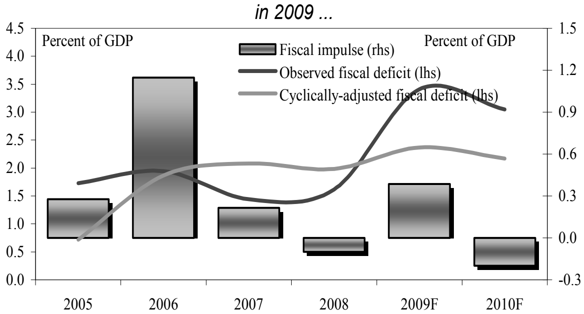
The fiscal deficit targets were revised upwards

	2008	2009		2010	
		EBS/09/49	rev. proj.	EBS/09/49	rev. proj.
	(in percent of GDP)				
Central government balance	-1.6	-2.8	-3.4	-2.6	-3.0
Revenues	12.1	11.3	10.6	11.4	10.9
Expenditures	13.7	14.1	14.0	14.0	14.0
Financing	1.6	2.8	3.4	2.6	3.0
External (net)	0.3	1.6	1.3	1.6	1.4
Domestic bond issuance (net)	0.7	1.0	1.4	0.6	1.3
Use of deposits	0.8	0.1	0.7	0.4	0.3
Other	-0.1	0.0	0.0	0.0	0.0
Memorandum item:					
GDP (millions of quetzales)	294,664	314,445	310,005	335,288	323,299

Sources: Ministry of Finance; and Fund staff estimates.

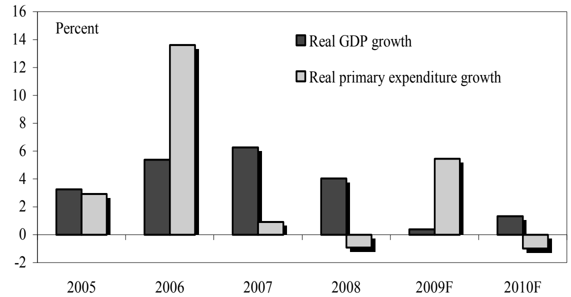
is expected to be financed by higher domestic bond issuance and by drawing down more government deposits than originally envisaged. The indicative target of government deposits at the central bank was revised accordingly, bringing the stock of deposits to a level equivalent to 1.9 percent of GDP (the authorities noted that about 2/3 of these deposits would be readily available)

Fiscal policy would be moderately countercyclical in 2009 ...



Source: Fund staff estimates.

… due to the increase in government spending

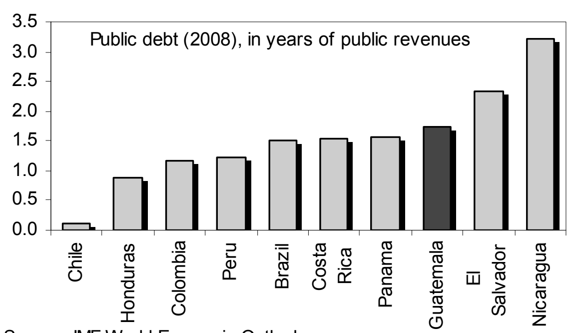


Sources: Ministry of Finance and Fund staff estimates.

13. **The 2010 budget is expected to continue striking a balance between supporting domestic demand and maintaining public debt ratios on a sustainable path**. The budget was submitted to Congress in early September. The authorities are determined to maintain medium-term debt sustainability and plan to start reducing the fiscal deficit in 2010 as the economy recovers. Thus, staff agreed to set the 2010 fiscal deficit target at 3.0 percent of GDP. This deficit would be consistent with a slightly negative policy stance, would only increase the public debt-to GDP ratio by less than 2.5 percent of GDP, and would be financed by a combination of external borrowing (mostly from multilaterals) and domestic resources.

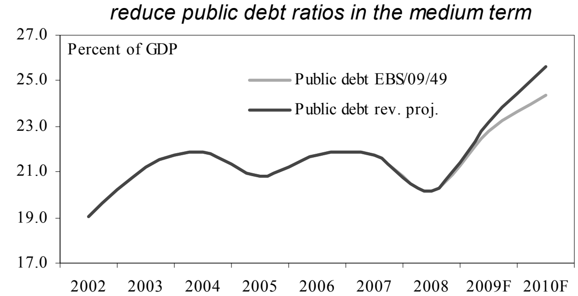
14. **The authorities reiterated their commitment to maintain medium-term fiscal sustainability**. Although Guatemala debt-to GDP ratio is moderate, low tax revenues limit its debt repayment capacity. The mission underscored the need to increase tax revenues and return to deficit levels below 2 percent of GDP starting in 2011 to stabilize the public debt at around 26 percent of GDP to ensure public debt sustainability. This would require discretionary measures equivalent to about ½ percent of GDP. Given the need to increase social and infrastructure spending, staff recommended to rekindle the fiscal reform agenda. This agenda includes a revenue-enhancing reform, limiting tax exemptions, and further strengthening tax administration. The authorities indicated their plans to pursue an income tax reform once economic growth

Low tax revenues limit the debt repayment capacity



Source: IMF World Economic Outlook.
1/ Consolidated public sector, except for Costa Rica and Panama (nonfinancial public sector), and for Guatemala (central govt).

Rekindling the fiscal reform agenda is essential to reduce public debt ratios in the medium term

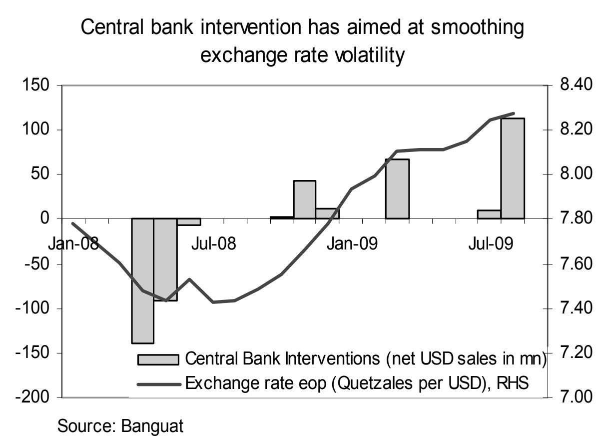


Sources: Authorities and Fund staff estimates bounces back. Staff expressed its concern about a law on free trade zones (ZOLIC), which broadens tax exemptions further. The authorities noted that enabling regulations will minimize the scope of the exemptions, limiting the revenue losses. Staff indicated that it is important to advance in the preparation of a medium-term fiscal framework (MTFF) and medium-term expenditure framework (MTEF).

C. Inflation Consultation and Monetary and Exchange Rate Policies

15. **Discussions focused on the drivers of inflation, the inflation outlook, and the policy response**. The decline in commodity prices has pushed headline inflation to -0.3 percent y-o-y by end-July (from a peak of 14.2 percent a year before), while core inflation has declined to 1.7 percent (from a peak of 9.4 percent in July 2008). Weak domestic demand conditions have also reduced inflationary pressures. At the same time, deflationary risks are not a major concern. With monthly inflation turning positive in recent months, and projected to remain so in the remainder of the year, annual inflation is expected to return to positive territory during the second half of 2009 as commodity price base effects dissipate. However, with growth well below potential, the authorities and staff concurred that inflation will likely remain subdued at historically-low levels during the remainder of 2009 and 2010.

16. **The staff viewed the gradual relaxation of monetary policy as appropriate**. The central bank has been prudent in reducing its policy interest rate gradually to avoid disorderly adjustments in the foreign exchange market. Recognizing that real interest rates should remain positive, the mission suggested that there was still some room to cut the policy interest rate as long as inflation remains low and foreign exchange market conditions are calm. While stressing the limited impact on domestic demand of further cuts in the policy rate because of a weak monetary policy transmission, the authorities indicated their commitment to shift to the use of an overnight interest rate by 2010 to influence monetary conditions better and to work on deepening secondary markets for securities to help develop a yield curve (in line with the Fund's technical assistance advice).



17. **The flexible exchange rate has helped cushion the impact of the global economic crisis**. During the mission, there was agreement that discretional foreign-exchange interventions should continue to be oriented to smooth exchange rate volatility. In more recent communications, the authorities indicated that the September modification in the foreign exchange intervention rule would be transitory, allow for more timely intervention, and help manage market expectations without preventing movements driven by fundamentals. Staff recommended to continue pursuing exchange rate flexibility and safeguarding international reserves.

D. Financial Sector Policies

18. **There was consensus on the need to remain vigilant of banking sector developments and step up the reform agenda**. The mission welcomed the authorities' efforts to continue strengthening the financial system, including progress in enhancing on-site supervision, and revamping provisioning requirements. The recent undertaking of stress tests, in collaboration with the World Bank, is an important step toward boosting crisis preparedness.

While the financial system is holding up well, there is a need to remain vigilant

	2007	2008		2009	
	Dec	Jun	Dec	Mar	Jun
Capital to assets ratio	9.8	10.1	10.5	10.4	10.5
Non-performing loans (Percent of total)	3.8	2.6	2.4	2.6	2.9
Bank Provisions to NPLs	41.6	66.4	68.3	69.0	69.3
Liquid assets to deposits and financial obligations /1	46.2	45.8	46.2	48.1	48.2
Return on assets (ROA)	1.7	2.2	1.7	2.2	2.0
Return on equity (ROE)	17	21.6	15.8	21.2	19.4

1/ For Banks only.
Source: Superintendency of Banks

19. **Approval of the amendments to the Banking Law will strengthen further the banking system**. The draft law submitted to Congress includes measures to reduce risks from offshore operations and connected lending, strengthen the supervision and enforcement power of the superintendency of banks, and enhance bank resolution procedures and the system's safety net (in line with FSAP recommendations). The elaboration of draft regulations on banks' liquidity management and foreign currency risk management (end-December benchmarks) is on track, and their implementation is set to begin in the first quarter of 2010.

The amendements to the Banking Law, submitted to Congress in end-June 2009, are broadly in line with the FSAP recommendations

Reduce risks from offshore operations and connected lending
- Establishment of more effective firewalls between onshore banks and their offshore affiliates
- Introduction of a minimum of $12,500 for off-shore deposits.
- Reasons for revoking banking licences for off-shore banks brought in line with those for on-shore banks, giving equality of treatment to all supervised banking entities.
- Introduction of limits on related lending.

Strengthen supervision and enforcement power of the superintendency of banks
- Annual rating requirement for all banks, financial institutions and off-shore banks.
- Introduction for an overall limit for total loans to all shareholders to control credit concentration.
- Strengthen the supervisor's capacity to request regularization plans and issue cease and desist orders
- Power to limit or prohibit dividend distribution for prudential reasons.
- Reform capital adequacy regulations, including deductions from consolidated capital of excess risk with shareholders, directors, and their respective related parties.

Enhance bank resolution procedures and the system's safety net
- Increased scope for the Central Bank to act as a lender of last resort.
- Increase in banks' contributions to the deposit insurance scheme (FOPA) and introduction of a risk related variable contribution.
- Foreign banks allowed to participate in domestic banks' resolution.

Source: IMF Staff based on Superintendency of Banks.

IV. Risks to the Program

20. **Risks to the outlook remain tilted to the downside**.

- Guatemala continues to have large external financing requirements, now estimated at 12 percent of GDP in 2009 (compared to 16.2 percent of GDP at program approval) and 13.8 percent of GDP in 2010. The potential financing gap estimated under the program (2.5 percent of GDP) could still materialize during 2009–10 in the event rollover rates of external nontrade-related private debt were not to recover as envisaged.
- Political uncertainties and delays in Congress' approval of key legislation could also present a risk. In late August, the government withdrew a reform on indirect taxation

from Congress because of lack of political support. Also, Congress is yet to approve the draft banking law and authorize the disbursement of a US$350 million loan from the World Bank. Were Congress to delay the approval of this loan, fiscal policy could turn procyclical, and growth could be lower, with adverse implications for banking soundness indicators. A potential deterioration of the economic conditions in Honduras also poses risks given the close financial and trade links with Guatemala.

The balance of payments still faces downside risks

		Baseline Scenario			Alternative Scenario 1/		
	2008	2009		2010	2009		2010
		EBS/09/49	rev. proj.		EBS/09/49	rev. proj.	
	In US$ billion unless otherwise indicated						
Gross external financing requirement	**6.2**	**6.2**	**4.5**	**5.2**	**6.4**	**4.5**	**5.2**
(in percent of GDP)	*15.9*	*16.2*	*12.0*	*13.8*	*16.7*	*12.0*	*13.8*
Current account deficit	1.9	1.5	0.6	1.2	1.7	0.6	1.2
External debt amortizations	4.3	4.7	3.9	4.0	4.7	3.9	4.0
Public sector	0.3	0.2	0.2	0.3	0.2	0.2	0.3
Private sector	4.1	4.4	3.7	3.7	4.4	3.7	3.7
Financing sources	6.2	6.2	4.5	5.2	5.4	4.1	4.7
Public sector gross borrowing	0.4	0.9	0.8	0.8	0.9	0.8	0.8
Private sector flows	5.6	4.8	3.7	4.4	4.1	3.3	3.9
FDI	0.8	0.6	0.7	0.7	0.5	0.7	0.7
Rollover of short-term debt	4.7	4.3	3.1	3.7	3.6	2.6	3.2
Other capital flows (includes E&O)	0.6	0.5	0.3	0.2	0.5	0.3	0.2
Change in NIR	-0.3	0.0	-0.3	-0.2	0.0	-0.3	-0.2
Financing gap	**0.0**	**0.0**	**0.0**	**0.0**	**0.9**	**0.5**	**0.5**
(in percent of GDP)	…	…	…	…	2.5	1.2	1.3
Rollover of private sector debt (in %)	141%	91%	64%	96%	65%	35%	65%

Sources: Authorities; and Fund staff estimates.
1/ Assumes lower rollover of private sector debts (excluding commercial credit).

V. Program Modalities

21. **Program implementation has been strong**. Given the still significant uncertainties to the economic outlook, program implementation will continue to be monitored through quarterly reviews. The program is fully financed for 2009–10. A new set of quantitative performance criteria has been agreed through end-March 2010 (as well as indicative targets up to end-2010). In this context, staff supports:

Good progress is being made toward completion of the remaining structural benchmarks in the program

	Test Date
Elaboration of draft regulations on bank's liquidity management	end- December 2009
Elaboration of draft regulations on bank's foreign currency credit risk	end- December 2009

- ***Revising the 2009–10 fiscal targets upwards to avoid a procyclical stance***. The end-September quantitative performance criterion (PCs) on the overall deficit has been revised upwards and new PCs have been set for end-December 2009 and end-March 2010 (in addition to indicative quarterly targets up to end-2010; see Letter of Intent, Table 1).

- ***Leaving the net international reserves (NIR) targets unchanged, even taking into account the recent SDR allocation***. Reserves are at adequate levels and significantly above the programs targets. The SDR allocation would provide an additional liquidity buffer if downside risks were to materialize.

- ***Adjusting the inflation consultation bands for the remainder of the program*** to take into account the lower-than-anticipated inflation outlook for 2009–10.

22. **The update safeguards assessment found that, since the 2002 assessment, the Bank of Guatemala has strengthened safeguards in the areas of financial reporting transparency and the management of foreign exchange reserves**. Additional measures are needed to ensure independent governance oversight through the establishment of a nonexecutive audit committee and direct access of internal auditors to senior management and the Monetary Board, and to address remaining vulnerabilities in the bank's legal structure and independence. The bank has recently embarked on the implementation of International Financial Reporting Standards to further enhance transparency and accountability.

VI. Staff Appraisal

23. **The Guatemalan economy is being negatively affected by the global crisis**. After a solid performance in recent years, economic growth is slowing driven by falling domestic demand and declines in exports, remittances, tourism receipts, and capital inflows. Downside risks remain on account of Guatemala's close ties to the region and the United States through trade, the banking system, and remittances. Inflationary pressures have declined sharply as a result of weaker domestic demand conditions.

24. **The authorities' response to the external shock has been appropriate**. On the macroeconomic front, policies have struck an appropriate balance between supporting demand and maintaining fiscal sustainability as well as avoiding disorderly adjustments in the foreign exchange market. Several measures were adopted to reduce risks to the financial system, including continuous on-site supervision, temporary and enhanced liquidity provision mechanisms, and tighter provisioning requirements.

25. **Looking ahead, fiscal policy will continue to seek striking a balance between supporting domestic demand and maintaining debt sustainability**. With revenues falling due to lower trade flows and weak domestic demand, the authorities' intention to maintain spending will increase the fiscal deficit in 2009 and 2010. Staff indicated that the scope for a positive fiscal impulse is limited because of financing constraints and the need to maintain sustainable public debt dynamics. In prioritizing spending, it is key to continue protecting social programs.

26. **Rekindling the fiscal reform agenda is necessary to signal strong commitment to medium-term fiscal sustainability**. Revenue-enhancing reforms are essential to address social and infrastructure needs and enhance the capacity to implement countercyclical fiscal policies. The withdrawal of the indirect tax reform from Congress because of lack of political

support is regrettable. Building consensus on a revenue reform is key to boost confidence in the authorities' capacity to reverse the increase in fiscal deficits by 2011 and maintain public debt on a sustainable path. Staff urges the authorities to minimize the scope of the exemptions associated with the law on free trade zones, which is yet to become effective. Curtailing tax exemptions is key to safeguard fiscal revenue and ensure a level playing field. The preparation of medium-term fiscal and expenditure frameworks is also important.

27. **The authorities' gradual easing of monetary conditions has been appropriate**. As inflationary pressures declined, the central bank has reduced its policy rate cautiously to avoid a disorderly adjustment in the exchange rate. While ensuring that the real policy rate remains positive, monetary policy is expected to continue supporting domestic demand until activity recovers and as long as inflation remains subdued and there are no external pressures. To strengthen the monetary policy transmission mechanism, the staff welcomes the authorities' intention to shift monetary policy toward an overnight policy rate and promote the deepening of secondary markets to help develop a yield curve.

28. **A flexible exchange rate has facilitated the adjustment to the external shock**. Foreign exchange interventions should aim at smoothing exchange rate volatility. Staff encourages the authorities to continue pursuing exchange rate flexibility while safeguarding international reserves.

29. **The financial system has weathered the economic slowdown well, but there is a need to remain vigilant of banking sector developments and move ahead with banking sector reforms**. To better assess the impact of shocks on the financial sector, staff welcomes the efforts of the superintendency of banks to improve stress-test methodologies to assess better the impact of shocks on the financial sector. The submission of the amendments to the banking law is also commendable. Swift congressional approval and a decisive implementation would significantly strengthen the banking system. The proposed amendments reduce risks from offshore operations and connected lending, enhance the enforcement powers of the superintendency, strengthen the instruments and size of the banking sector safety net, and improve resolution procedures.

30. **Staff recommends the completion of the first review of the SBA**. While risks remain tilted to the downside given large private sector debt rollover needs and/or a deeper recession, the authorities remain committed to contain those risks by implementing the policies envisaged under the program. Staff supports the authorities' request for lowering the inflation consultation bands, modifying the performance criterion on the central government overall balance through end-September, and establishing new quantitative performance criteria though end-March 2010.

Table 1. Guatemala: Selected Economic and Social Indicators

I. Social and Demographic Indicators

Population 2006 (millions)	13.0	Gini index (2002)	55.1
Percentage of indigenous population (2006)	38.4	Life expectancy at birth (2005)	69.7
Percentage of population below the poverty line (2006)	51.0	Adult illiteracy rate (2005)	28.2
Rank in UNDP development index (2008)	121 of 179	GDP per capita (US$, 2007)	2,550

II. Economic Indicators

	2006	2007	2008	2009		2010	
				EBS/09/49	rev. proj.	EBS/09/49	rev. proj.
	(Annual percent change)						
Income and prices							
Real GDP	5.4	6.3	4.0	1.0	0.4	1.8	1.3
Consumer prices (end of period)	5.8	8.7	9.4	5.5	1.5	4.7	3.8
Monetary sector							
M2	18.8	14.3	7.6	6.4	5.5	6.6	6.6
Credit to the private sector	37.5	24.7	11.0	6.8	4.3	7.2	4.8
	(In percent of GDP, unless otherwise indicated)						
Savings and investment 1/							
Gross domestic investment	20.8	20.7	17.6	15.8	15.0	17.2	16.5
Public sector	3.1	3.6	3.5	3.6	3.5	3.6	3.6
Private sector	17.7	17.1	14.1	12.2	11.4	13.6	13.0
Gross national saving	15.8	15.5	12.8	11.8	13.3	12.3	13.3
Public sector	1.2	2.2	1.9	0.8	0.1	1.0	0.5
Private sector	14.6	13.3	10.9	11.0	13.2	11.3	12.8
External saving	5.0	5.2	4.8	4.0	1.7	4.9	3.3
External sector							
Current account balance	-5.0	-5.2	-4.8	-4.0	-1.7	-4.9	-3.3
Trade balance	-16.1	-16.1	-14.3	-11.9	-9.7	-12.8	-12.0
Exports	20.1	20.5	20.1	18.2	18.8	18.5	19.9
Imports	-36.2	-36.6	-34.4	-30.1	-28.5	-31.4	-31.9
o/w Oil & lubricants	-5.8	-6.7	-6.9	-4.2	-5.1	-4.9	-5.5
Other (net)	11.0	10.9	9.5	7.9	8.0	7.9	8.7
o/w Remittances	12.1	12.3	11.3	9.9	10.3	9.9	10.5
Capital and financial account	4.4	4.7	4.1	2.7	2.3	3.6	3.2
Public sector	1.1	0.7	0.3	1.6	1.3	1.6	1.5
Private sector	3.4	4.1	3.8	1.0	0.9	2.0	1.7
o/w FDI	1.8	2.1	2.1	1.5	1.8	1.6	1.8
Errors and omissions	1.4	1.1	1.5	1.3	0.1	1.3	0.6
Overall balance	0.8	0.6	0.9	0.0	0.7	0.0	0.5
Net international reserves (in millions of U.S. dollars)	**3,878**	**4,098**	**4,421**	**4,416**	**4,687**	**4,416**	**4,864**
(Stock in months of next-year NFGS imports)	3.2	3.2	4.3	3.9	4.1	3.5	3.8
(Stock over short-term debt on residual maturity)	1.0	0.9	1.0	1.0	1.2	0.9	1.2
Public finances							
Central government							
Revenues	12.7	12.9	12.1	11.3	10.6	11.4	10.9
Expenditures	14.7	14.3	13.7	14.1	14.0	14.0	14.0
Current	9.4	9.5	9.2	9.6	9.9	9.7	10.6
Capital	5.3	4.8	4.5	4.4	4.2	4.3	3.4
Primary balance	-0.6	0.0	-0.3	-1.2	-1.9	-1.0	-1.4
Overall balance	-1.9	-1.4	-1.6	-2.8	-3.4	-2.6	-3.0
Financing of the central government balance							
Net external financing	1.2	1.2	0.3	1.6	1.3	1.6	1.4
Net domestic financing	0.7	0.3	1.3	1.2	2.1	0.9	1.6
o/w Use of government deposits	-0.4	-0.7	0.8	0.1	0.7	0.4	0.3
Rest of nonfinancial public sector balance	0.7	1.1	0.9	0.4	0.4	0.5	0.5
Combined nonfinancial public sector							
Overall balance	-1.2	-0.3	-0.7	-2.4	-3.0	-2.1	-2.6
Primary balance	0.1	1.2	0.6	-0.8	-1.5	-0.5	-0.9
Nonfinancial public sector debt	**21.8**	**21.8**	**20.2**	**22.8**	**23.2**	**24.4**	**25.6**
External	13.1	12.5	11.3	13.1	13.3	14.4	14.9
Domestic	8.7	9.3	8.9	9.7	9.9	10.0	10.8
Memorandum items:							
GDP (US$ billions)	30.2	34.0	39.0	38.0	37.7	39.0	37.2

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

1/ Investment excludes changes in inventories, and its breakdown between public and private is taken from the national accounts. Investments in IMF Country Report No. 09/143 included changes in inventories, and its breakdown in public and private was based on Fund staff esti from fiscal data.

Table 2. Guatemala: Summary Balance of Payments

	2008	2009		2010		2011	2012	2013	2014
		EBS/09/49	rev. proj.	EBS/09/49	rev. proj.	Projections			
	(In millions of U.S. dollars)								
Current account balance	**-1,863**	**-1,511**	**-624**	**-1,915**	**-1,209**	**-1,550**	**-1,789**	**-1,965**	**-2,148**
Trade balance (goods)	-5,574	-4,517	-3,646	-4,998	-4,463	-5,277	-5,981	-6,695	-7,373
Exports, f.o.b. 1/	7,848	6,936	7,091	7,224	7,407	7,878	8,470	9,186	10,089
Imports, f.o.b. 1/	-13,422	-11,453	-10,736	-12,223	-11,870	-13,155	-14,451	-15,881	-17,462
of which: Oil & lubricants	-2,677	-1,602	-1,934	-1,909	-2,054	-2,467	-2,806	-3,186	-3,601
Real services (net)	-370	-335	-348	-374	-253	-266	-270	-281	-303
Rent (net)	-929	-990	-979	-1006	-902	-1126	-1392	-1584	-1789
Current transfers (net)	5,010	4,331	4,349	4,463	4,409	5,119	5,854	6,595	7,318
of which: remittances	4,403	3,753	3,895	3,866	3,905	4,551	5,216	5,889	6,544
Capital and financial account	**1,596**	**1,015**	**852**	**1,406**	**1,188**	**1,530**	**1,771**	**1,951**	**2,143**
Capital account	0	0	0	0	0	0	0	0	0
Financial account	1,596	1,015	852	1,406	1,188	1,530	1,771	1,951	2,143
Central Bank	-3	0	274	0	0	0	0	0	0
Public sector	115	618	508	630	564	149	207	107	221
Bonds (net)	-1	0	0	0	0	-325	0	0	0
Loans	116	618	508	630	564	474	207	107	221
Disbursements	382	860	753	894	828	800	547	749	523
Amortization	-266	-242	-245	-264	-264	-326	-341	-642	-302
Private sector	1,485	398	70	777	625	1,381	1,564	1,845	1,922
FDI	822	553	661	624	688	775	845	939	1,068
Portfolio investment	39	-27	-7	-28	24	27	30	34	38
Other investment	624	-128	-584	181	-87	578	689	871	816
Errors and omissions	**599**	**496**	**43**	**508**	**211**	**232**	**246**	**262**	**279**
Overall balance	**333**	**0**	**271**	**0**	**190**	**212**	**228**	**248**	**275**
	(In percent of GDP)								
Current account balance	**-4.8**	**-4.0**	**-1.7**	**-4.9**	**-3.3**	**-3.8**	**-4.1**	**-4.3**	**-4.4**
Trade balance (goods)	-14.3	-11.9	-9.7	-12.8	-12.0	-12.9	-13.8	-14.5	-15.0
Exports, f.o.b. 1/	20.1	18.2	18.8	18.5	19.9	19.3	19.6	19.9	20.5
Imports, f.o.b. 1/	-34.4	-30.1	-28.5	-31.4	-31.9	-32.2	-33.4	-34.4	-35.5
of which: Oil & lubricants	-6.9	-4.2	-5.1	-4.9	-5.5	-6.0	-6.5	-6.9	-7.3
Real services (net)	-0.9	-0.9	-0.9	-1.0	-0.7	-0.6	-0.6	-0.6	-0.6
Rent (net)	-2.4	-2.6	-2.6	-2.6	-2.4	-2.8	-3.2	-3.4	-3.6
Current transfers (net)	12.9	11.4	11.5	11.4	11.9	12.5	13.5	14.3	14.9
of which: remittances	11.3	9.9	10.3	9.9	10.5	11.1	12.0	12.8	13.3
Capital and financial account	**4.1**	**2.7**	**2.3**	**3.6**	**3.2**	**3.7**	**4.1**	**4.2**	**4.4**
Capital account	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	4.1	2.7	2.3	3.6	3.2	3.7	4.1	4.2	4.4
Public sector	0.3	1.6	1.3	1.6	1.5	0.4	0.5	0.2	0.4
Bonds (net)	0.0	0.0	0.0	0.0	0.0	-0.8	0.0	0.0	0.0
Loans	0.3	1.6	1.3	1.6	1.5	1.2	0.5	0.2	0.4
Disbursements	1.0	2.3	2.0	2.3	2.2	2.0	1.3	1.6	1.1
Amortization	-0.7	-0.6	-0.6	-0.7	-0.7	-0.8	-0.8	-1.4	-0.6
Private sector	3.8	1.0	0.2	2.0	1.7	3.4	3.6	4.0	3.9
FDI	2.1	1.5	1.8	1.6	1.8	1.9	2.0	2.0	2.2
Portfolio investment	0.1	-0.1	0.0	-0.1	0.1	0.1	0.1	0.1	0.1
Other investment	1.6	-0.3	-1.5	0.5	-0.2	1.4	1.6	1.9	1.7
Errors and omissions	**1.5**	**1.3**	**0.1**	**1.3**	**0.6**	**0.6**	**0.6**	**0.6**	**0.6**
Overall balance	**0.9**	**0.0**	**0.7**	**0.0**	**0.5**	**0.5**	**0.5**	**0.5**	**0.6**
Memorandum items:									
Value of exports, f.o.b. (percentage change)	12.4	-11.5	-9.7	4.7	4.5	6.4	7.5	8.5	9.8
Value of imports, f.o.b. (percentage change)	7.6	-14.6	-20.0	7.2	10.6	10.8	9.8	9.9	10.0
NIR in months of next-year NFGS imports	4.3	3.9	4.1	3.5	3.8	3.6	3.5	3.3	3.1
Stock of NIR (in millions of U.S. dollars) 2/	4,421	4,416	4,687	4,416	4,864	5,057	5,269	5,499	5,754
NIR over short-term debt on residual maturity	1.0	1.0	1.2	0.9	1.2	1.2	1.1	1.0	1.0
Nominal GDP (in billions of U.S. dollars)	39.0	38.0	37.7	39.0	37.2	40.9	43.3	46.1	49.2

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

1/ Includes maquila throughout. Values in IMF Country Report No. 09/143 were originally reported net of maquila imports.

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

Table 3A. Guatemala: Public Sector Balance

	2006	2007	2008	2009		2010	
				EBS/09/49	rev. proj.	EBS/09/49	rev. proj.
	(In millions of quetzales)						
Central Government							
Total revenues	**29,250**	**33,611**	**35,578**	**35,504**	**32,966**	**38,303**	**35,357**
Tax revenues	27,238	31,543	33,358	32,866	30,599	35,528	32,512
Nontax revenues	2,012	2,067	2,220	2,637	2,367	2,776	2,845
Total expenditures	**33,721**	**37,382**	**40,355**	**44,221**	**43,537**	**46,927**	**45,215**
Current	21,622	24,781	27,134	30,333	30,641	32,550	34,356
Capital	12,100	12,602	13,221	13,888	12,896	14,377	10,859
Primary expenditures	30,539	33,491	36,330	39,372	38,855	41,726	39,946
Interest	3,182	3,892	4,026	4,849	4,682	5,201	5,269
Primary balance	**-1,289**	**120**	**-752**	**-3,868**	**-5,889**	**-3,423**	**-4,590**
Overall balance	**-4,471**	**-3,772**	**-4,777**	**-8,718**	**-10,571**	**-8,624**	**-9,859**
Financing	**4,471**	**3,772**	**4,777**	**8,718**	**10,571**	**8,624**	**9,859**
Net external financing	**2,867**	**3,040**	**850**	**5,093**	**3,944**	**5,440**	**4,564**
Disbursements of loans	4,440	4,613	2,763	7,090	6,110	7,734	6,776
Amortizations	1,573	1,572	1,913	1,997	2,166	2,294	2,212
Net domestic financing	**1,604**	**731**	**3,928**	**3,625**	**6,627**	**3,183**	**5,295**
Net issuance of bonds	3,763	3,119	2,019	3,168	4,388	2,000	4,200
Gross bond issuance	7,137	5,308	3,851	3,952	5,172	3,719	5,919
Amortizations	3,374	2,189	1,832	784	784	1,719	1,719
Other	-1,160	-594	-393	0	0	0	0
Use of government deposits at Banguat	-999	-1,794	2,302	456	2,239	1,183	1,095
Rest of nonfinancial public sector							
Overall balance	**1,615**	**2,975**	**2,654**	**1,291**	**1,200**	**1,738**	**1,600**
Financing	-1,615	-2,975	-2,654	-1,291	-1,200	-1,738	-1,600
Net external	-37	-81	256	-59	-59	-61	-61
Net domestic	-1,578	-2,893	-2,910	-1,232	-1,141	-1,676	-1,539
Banguat	-176	-665	630	-393	-393	-419	-419
Commercial banks	-1,401	-389	-1,614	0	0	0	0
Central government bonds	0	-1,839	-1,926	-839	-748	-1,257	-1,120
Central bank balance	**-379**	**272**	**609**	**472**	**-435**	**335**	**-469**
Combined public sector							
Overall balance	**-2,857**	**-797**	**-2,124**	**-7,426**	**-9,371**	**-6,886**	**-8,259**
Primary balance	**326**	**3,095**	**1,902**	**-2,577**	**-4,689**	**-1,685**	**-2,990**
Memorandum items:							
Nonfinancial public sector debt	49,992	56,799	59,395	71,667	71,929	81,706	82,818
External	30,061	32,608	33,185	41,207	41,331	48,232	48,020
Domestic	19,932	24,191	26,210	30,459	30,598	33,475	34,798
Central government gross borrowing requirements	10,578	8,127	8,915	11,498	13,520	12,636	13,789
Social spending	11,555	12,022	12,936	15,562	14,976	16,694	16,180

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

Table 3B. Guatemala: Public Sector Balance

	2006	2007	2008	2009		2010	
				EBS/09/49	rev. proj.	EBS/09/49	rev. proj.
	(In percent of GDP)						
Central Government							
Total revenues	**12.7**	**12.9**	**12.1**	**11.3**	**10.6**	**11.4**	**10.9**
Tax revenues	11.9	12.1	11.3	10.5	9.9	10.6	10.1
Nontax revenues	0.9	0.8	0.8	0.8	0.8	0.8	0.9
Total expenditures	**14.7**	**14.3**	**13.7**	**14.1**	**14.0**	**14.0**	**14.0**
Current	9.4	9.5	9.2	9.6	9.9	9.7	10.6
Capital	5.3	4.8	4.5	4.4	4.2	4.3	3.4
Primary expenditures	13.3	12.8	12.3	12.5	12.5	12.4	12.4
Interest	1.4	1.5	1.4	1.5	1.5	1.6	1.6
Primary balance	**-0.6**	**0.0**	**-0.3**	**-1.2**	**-1.9**	**-1.0**	**-1.4**
Overall balance	**-1.9**	**-1.4**	**-1.6**	**-2.8**	**-3.4**	**-2.6**	**-3.0**
Financing	**1.9**	**1.4**	**1.6**	**2.8**	**3.4**	**2.6**	**3.0**
Net external financing	1.2	1.2	0.3	1.6	1.3	1.6	1.4
Disbursements of loans	1.9	1.8	0.9	2.3	2.0	2.3	2.1
Amortizations	0.7	0.6	0.6	0.6	0.7	0.7	0.7
Net domestic financing	0.7	0.3	1.3	1.2	2.1	0.9	1.6
Net issuance of bonds	1.6	1.2	0.7	1.0	1.4	0.6	1.3
Gross bond issuance	3.1	2.0	1.3	1.3	1.7	1.1	1.8
Amortizations	1.5	0.8	0.6	0.2	0.3	0.5	0.5
Other	-0.5	-0.2	-0.1	0.0	0.0	0.0	0.0
Use of government deposits at Banguat	-0.4	-0.7	0.8	0.1	0.7	0.4	0.3
Rest of Non-Financial Public Sector							
Overall Balance	**0.7**	**1.1**	**0.9**	**0.4**	**0.4**	**0.5**	**0.5**
Financing	-0.7	-1.1	-0.9	-0.4	-0.4	-0.5	-0.5
Net external	0.0	0.0	0.1	0.0	0.0	0.0	0.0
Net domestic	-0.7	-1.1	-1.0	-0.4	-0.4	-0.5	-0.5
Banguat	-0.1	-0.3	0.2	-0.1	-0.1	-0.1	-0.1
Commercial banks	-0.6	-0.1	-0.5	0.0	0.0	0.0	0.0
Central government bonds	0.0	-0.7	-0.7	-0.3	-0.2	-0.4	-0.3
Central Bank balance	**-0.2**	**0.1**	**0.2**	**0.2**	**-0.1**	**0.1**	**-0.1**
Combined Non-Financial Public Sector							
Overall balance	**-1.2**	**-0.3**	**-0.7**	**-2.4**	**-3.0**	**-2.1**	**-2.6**
Primary balance	**0.1**	**1.2**	**0.6**	**-0.8**	**-1.5**	**-0.5**	**-0.9**
Memorandum Items:							
Non-financial public sector debt	21.8	21.8	20.2	22.8	23.2	24.4	25.6
External	13.1	12.5	11.3	13.1	13.3	14.4	14.9
Domestic	8.7	9.3	8.9	9.7	9.9	10.0	10.8
Central government gross borrowing requireme	4.6	3.1	3.0	3.7	4.4	3.8	4.3
Social spending	5.0	4.6	4.4	4.9	4.8	5.0	5.0

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

Table 4. Guatemala: Monetary Sector Survey

	2006	2007	2008	2009		2010	
				EBS/09/49	rev. proj.	EBS/09/49	rev. proj.
				(In millions of quetzales)			
Bank of Guatemala (BOG)							
Net international reserves 1/	**29,459**	**31,271**	**34,405**	**37,451**	**39,837**	**38,914**	**43,050**
(In millions of U.S. dollars) 1/	3,878	4,098	4,421	4,416	4,687	4,416	4,864
Net domestic assets	**-14,799**	**-14,291**	**-17,651**	**-19,329**	**-21,667**	**-19,590**	**-23,454**
Net claims on nonfinancial public sector	-12,490	-15,185	-13,074	-13,187	-11,228	-12,488	-10,552
Central government (CG)	-7,551	-9,581	-8,100	-7,820	-5,861	-6,702	-4,766
Rest of nonfinancial public sector	-4,939	-5,604	-4,974	-5,367	-5,367	-5,786	-5,786
Bank of Guatemala losses	15,258	14,986	14,377	13,905	13,912	13,570	13,589
Net credit to banks	-9,919	-10,852	-11,283	-13,113	-12,186	-13,968	-13,010
Of which: legal reserves	-11,985	-12,916	-13,345	-15,175	-14,248	-16,030	-15,072
Open market operations 2/	-9,796	-6,172	-10,848	-7,023	-9,481	-5,270	-9,032
Other assets (net)	2,148	2,933	3,177	89	-2,683	-1,434	-4,448
Currency in circulation	**14,659**	**16,980**	**16,754**	**18,123**	**18,170**	**19,324**	**19,596**
Banking sector 2/							
Net foreign position	**-8,199**	**-11,226**	**-10,870**	**-9,314**	**-9,409**	**-9,155**	**-10,553**
(in millions of U.S. Dollars)	-1,079	-1,471	-1,397	-1,098	-1,107	-1,037	-1,192
Net claims on Bank of Guatemala	**18,223**	**15,411**	**20,897**	**18,819**	**20,369**	**17,833**	**20,688**
Legal reserves	11,985	12,916	13,345	15,175	14,248	16,030	15,072
BOG securities	8,296	4,821	9,606	5,698	8,175	3,857	7,670
Liabilities to BOG	-2,059	-2,057	-2,054	-2,054	-2,054	-2,054	-2,054
Net domestic assets	**68,031**	**85,429**	**89,145**	**93,840**	**96,143**	**101,070**	**103,534**
Net credit to the NFPS	3,172	2,940	-559	1,548	2,132	1,791	4,652
Official capital and reserves	-1,152	-2,005	-2,752	-3,086	-3,200	-3,198	-3,370
Credit to the private sector	62,357	78,567	87,209	93,113	90,957	99,854	95,334
Other items net	3,655	5,926	5,246	2,264	6,254	2,623	6,919
Medium and long-term foreign liabilities	**128**	**557**	**1,214**	**1,144**	**1,079**	**1,106**	**1,224**
Liabilities to private sector	**77,928**	**89,056**	**97,957**	**102,200**	**106,024**	**108,642**	**112,446**
Demand deposits	28,327	33,441	35,710	36,342	36,877	39,034	39,202
Time and savings deposits	41,769	46,449	51,737	55,671	57,679	59,005	61,164
Capital and reserves (private banks)	7,832	9,166	10,510	8,410	11,468	8,717	12,080
Monetary survey 2/							
Net foreign assets	**21,260**	**20,045**	**23,535**	**28,137**	**30,428**	**29,759**	**32,497**
(In millions of U.S. dollars)	2,799	2,627	3,024	3,317	3,580	3,371	3,672
Net domestic assets	**71,454**	**86,548**	**92,391**	**93,704**	**97,148**	**99,751**	**103,166**
Net claims on nonfinancial public sector	-9,318	-12,245	-13,633	-11,638	-9,096	-10,697	-5,900
Bank of Guatemala losses	15,258	14,986	14,377	13,905	13,912	13,570	13,589
Credit to private sector	62,365	78,574	87,217	93,120	90,965	99,862	95,342
Other assets (net)	3,150	5,233	4,430	-1,684	1,367	-2,984	136
Medium and long-term foreign liabilities	**128**	**557**	**1,214**	**1,144**	**3,382**	**1,106**	**3,621**
Liabilities to the private sector	**92,587**	**106,036**	**114,712**	**120,697**	**124,194**	**128,404**	**132,042**
of which: Money	42,986	50,421	52,464	49,214	55,048	52,476	58,798
of which: Quasi-money	41,769	46,449	51,737	71,483	57,679	75,928	61,164
Memorandum items:							
				(Percent change)			
Currency in circulation	17.5	15.8	-1.3	8.2	8.5	6.6	7.8
M2	18.8	14.3	7.6	6.4	5.5	6.6	6.6
Credit to private sector	37.5	24.7	11.0	6.8	4.3	7.2	4.8
				(In percent of GDP)			
Currency in circulation	6.4	6.5	5.7	5.8	5.9	5.8	6.1
M2	36.9	37.1	35.4	34.7	35.4	34.7	36.2
Credit to private sector	29.0	31.8	31.3	29.6	31.0	29.8	31.2
				(In percent of bank liabilities to the private sector)			
Bank liquidity assets	41.7	33.6	34.7	33.4	34.2	30.7	34.7
Demand deposits	36.3	37.6	36.5	35.6	34.8	35.9	34.9
Time and savings deposits	53.6	52.2	52.8	54.5	54.4	54.3	54.4
Capital and reserves (private banks)	10.1	10.3	10.7	8.2	10.8	8.0	10.7

Sources: Bank of Guatemala; and Fund staff estimates.

1/ Program definition excludes foreign currency liabilities of the central bank to financial institutions.
2/ IMF Country Report No. 09/143 figures are not comparable to the revised figures due to a change in the classification of mone
variables.

Table 5. Guatemala: Financial Soundness Indicators

	2006	2007	2008	2009 June
On-shore banks				
Statutory capital to risk-weighted assets	12.8	12.3	13.5	n.a.
Nonperforming loans net of provisions to capital /1	7.5	6.2	3.6	3.9
Nonperforming loans to total gross loans	3.4	2.6	2.3	3.0
Cash to total deposits	21.2	20.8	19.7	19.8
Noninterest expenses to gross income /1	60.7	62.5	52.9	51.0
Return on assets	1.2	1.5	1.7	2.0
Return on equity	15.0	16.8	16.3	20.3
Net open position in foreign exchange to capital	22.0	22.8	22.4	n.a.
Foreign currency-denominated loans to total loans	30.2	33.2	33.6	32.4
Foreign currency-denominated liabilities to total liabilities	21.6	25.1	24.3	23.9
Off-shore banks				
Statutory capital to risk-weighted assets	14.2	15.0	14.7	n.a.
Nonperforming loans to total gross loans	2.9	2.9	2.2	2.0
Return on assets	2.0	2.2	1.5	1.8
Return on equity	18.8	19.4	14.2	16.2
Liquid assets to total assets	21.1	19.0	21.6	13.9
Total assets off-shore banks to total assets on-shore banks	18.9	16.8	16.1	16.3

1/ 2009 data refers to March.
Sources: Superintendency of Banks; Banguat; and Fund staff estimates.

Table 6. Guatemala: Indicators of External Vulnerability

	2006	2007	2008	2009	
				EBS/09/49	rev. proj.
External indicators					
Merchandise exports (12-month percentage change)	11.4	14.8	12.4	-11.5	-9.7
Traditional merchandise exports (12-month percentage change)	5.0	25.2	18.5	-16.3	0.8
Nontraditional merchandise exports (12-month percentage change)	13.3	12.0	10.5	-9.6	-13.0
Merchandise imports (12-month percentage change)	13.3	14.0	7.6	-14.6	-20.0
Imports of oil and lubricants (12-month percentage change)	18.6	29.1	17.4	-40.0	-27.8
Nonoil imports (12-month percentage change)	12.4	11.1	5.4	-7.7	-18.1
Terms of trade (12-month percentage change)	-2.7	-0.2	-1.3	4.8	4.9
Current account balance (in percent of GDP)	-5.0	-5.2	-4.8	-4.0	-1.7
Capital and financial account balance (in percent of GDP)	4.4	4.7	4.1	2.7	2.3
Net international reserves					
In millions of U.S. dollars	3,878	4,098	4,421	4,416	4,687
In percent of M2	36.4	33.3	33.5	34.4	37.1
In percent of base money	111.0	105.2	114.3	112.8	121.4
In percent of short-term external debt on a remaining maturity basis	117.6	102.0	104.9	97.6	122.8
In months of next-year's imports of goods and nonfactor services	3.2	3.2	4.3	3.9	4.1
External indebtness indicators					
Total external debt (in percent of GDP)	34.3	35.1	32.5	35.3	33.6
External private sector debt (in percent of GDP)	21.2	22.6	21.2	24.0	20.4
External public sector debt (in percent of GDP)	13.1	12.5	11.3	11.3	13.3
Public sector external interest payments in percent of exports of goods and nonfactor services	3.6	3.9	3.0	3.4	3.3
Public sector external amortization payments in percent of exports of goods and services	4.2	5.2	3.2	3.6	3.4

Sources: Bank of Guatemala; and Fund staff estimates.

Table 7. Guatemala: Purchase Schedule and Terms Under the Stand-By Arrangement

Date	Conditions for purchase	Purchase: Million SDR	Purchase: Million US$ 1/	Purchase: Percent of Quota	Purchase: Percent of Total Access
April 22, 2009	Board approval of the SBA	420.40	655.01	200.00	66.67
September 15, 2009	First review, based on end-June 2009 performance criteria	42.04	65.50	20.00	6.67
December 15, 2009	Second review, based on end-September 2009 performance criteria	42.04	65.50	20.00	6.67
March 15, 2010	Third review, based on end-December 2009 performance criteria	42.04	65.50	20.00	6.67
June 15, 2010	Fourth review, based on end-March 2010 performance criteria	42.04	65.50	20.00	6.67
September 15, 2010	Fifth review, based on end-June 2010 performance criteria	42.04	65.50	20.00	6.67
Total		630.60	982.52	300.00	100.00

Source: Fund staff estimates.

1/ US$/SDR exchange rate of 0.64182 as of August 13, 2009.

Table 8. Guatemala: Indicators of Fund Credit 2006-2015 1/

				Projections						
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Stocks from prospective drawings 2/										
Fund credit in millions SDR	0.0	0.0	0.0	504.5	630.6	630.6	572.8	289.0	31.5	0.0
In percent of quota	0.0	0.0	0.0	240.0	300.0	300.0	272.5	137.5	15.0	0.0
In percent of GDP	0.0	0.0	0.0	2.1	2.6	2.4	2.1	1.0	0.1	0.0
In percent of exports of goods and services	0.0	0.0	0.0	9.3	10.9	10.2	8.6	4.0	0.4	0.0
In percent of gross reserves	0.0	0.0	0.0	16.9	20.3	19.5	16.9	8.2	0.8	0.0
Flows from prospective drawings 3/ 4/										
Principal (Millions SDR)	0.0	0.0	0.0	0.0	0.0	0.0	57.8	283.8	257.5	31.5
Interest and charges (Millions SDR)	0.0	0.0	0.0	3.3	7.8	8.2	8.2	6.6	2.7	0.3
Total (Millions SDR)	0.0	0.0	0.0	3.3	7.8	8.2	66.0	290.3	260.2	31.8
In percent of quota	0.0	0.0	0.0	1.6	3.7	3.9	31.4	138.1	123.8	15.1
In percent of GDP	0.0	0.0	0.0	0.0	0.0	0.0	0.2	1.0	0.8	0.1
In percent of exports of goods and services	0.0	0.0	0.0	0.1	0.1	0.1	1.0	4.0	3.3	0.4
In percent of gross reserves	0.0	0.0	0.0	0.1	0.2	0.3	1.9	8.2	7.0	0.8

Sources: Bank of Guatemala; IMF Finance Department; and Fund staff estimates.
1/ Assumes a US$/SDR exchange rate of 0.64182 as of August 13, 2009.
2/ End of period.
3/ At a constant basic rate of charge in the GRA of 1.30 percent plus 0.01 basis points for burden sharing.
4/ Excluding commitment charges.

ATTACHMENT: LETTER OF INTENT

Guatemala City, September 4, 2009

Mr. Dominique Strauss-Kahn
Managing Director
International Monetary Fund
Washington, D.C., 20431

Dear Mr. Strauss-Kahn:

1. The Stand-By Arrangement agreed in April 2009 is being implemented successfully. All end-June quantitative performance criteria have been met (Table 1). The targets on net international reserves and the overall deficit of the central government were met by a wide margin. Government deposits at the central bank were below the indicative target for end-June due to lower than expected tax revenues and loan disbursements, together with a later-than-anticipated bond issuance approval by Congress. Consumer prices fell by 0.3 percent year-over-year as of end-July 2009, falling below the outer inflation band agreed under the program. Inflation fell much faster than expected because of the sharp drop in global commodity prices and weak domestic demand conditions. The amendments to the Banking Law (structural benchmark, end-June 2009) were submitted to Congress on June 25, 2009.

2. Guatemala is feeling the full impact of the global financial turmoil and the ensuing global recession. Our exports, tourism receipts, and remittances are declining, net private capital inflows have fallen, and a large contraction in imports has hit fiscal revenues hard. Notwithstanding these shocks, the exchange rate has remained broadly stable and net international reserves have increased. We remain confident that economic growth will be in a range between 0.4 and 1.2 percent in 2009 and 1.3 and 2.1 percent in 2010.

3. For the period ahead, we intend to continue implementing countercyclical policies to help mitigate the adverse effects of the global crisis. With fiscal revenues declining more sharply than originally envisaged, we have raised the target for the fiscal deficit of the central government to 3.4 percent of GDP in 2009 and 3.0 percent of GDP in 2010. Because of these revisions, the deficit of the consolidated public sector could reach 3.0 percent of GDP in 2009 and 2.6 percent of GDP in 2010. We believe that the revised fiscal targets strike an appropriate balance between imparting a necessary stimulus to domestic demand and keeping public debt dynamics manageable. We will continue enhancing our efforts to broaden the tax base, including working with Congress to enact a revenue reform to help ensure a gradual recovery of tax collections from 2010 onwards. This, together with adherence to our spending targets, is key to ensure sustainable debt dynamics.

4. We expect that the revised fiscal deficits for 2009 and 2010 will be partly financed from external sources, mostly multilaterals. At the same time, our financing strategy envisages that net domestic debt placements and use of government deposits at the central bank will be higher than earlier anticipated. Were tax collections to decline even further than projected

and/or were we to experience difficulties borrowing domestically the planned amounts, we remain committed to protect social spending.

5. In response to the downside risks to inflation and economic activity, the Monetary Board has reduced the policy interest rate by 250 basis points since end-2008, to 4.75 percent. We expect inflation to pick up in the second semester as a result of higher commodity prices and project inflation to be about 1.5 percent by end-2009 and about 4.0 percent by end-2010. The revised quarterly consultation bands for CPI inflation under the program are consistent with these projections. The Monetary Board will continue managing the policy rate as needed to meet the inflation target, and the central bank remains committed to its flexible exchange rate regime. Intervention in the foreign exchange market will remain geared at smoothing out excessive volatility. We expect international reserves to remain at comfortable levels.

6. Our financial system has been resilient to the external shock. This reflects the absence of "toxic" asset holdings in the system, low reliance on external credit, higher capital cushions built since late 2005, and the actions we took as the crisis unfolded, including providing liquidity support, stepping up banking supervision, and revamping provisioning requirements. We remain committed to strengthening further the regulatory framework, including finalizing the elaboration of regulations on banks' liquidity management and foreign currency credit risk by end-December 2009, with their implementation beginning in the first quarter of 2010. Also, we will continue to work closely with Congress to ensure prompt approval of the amendments to the banking legislation, which are key to strengthen regulation and supervision and enhance the current bank resolution framework.

7. In light of this performance and our continued commitment to the program, we request completion of the First Review Under the Stand-By Arrangement. Our intention is to continue treating the arrangement as precautionary. Given the sharp fall in inflation, we request lowering of the inflation consultation bands for end-September and end-December. We also request revising the performance criterion on the overall balance of the central government for end-September. Program implementation will continue to be monitored through quarterly reviews. The revised quantitative performance criteria for September, new performance criteria for December 2009 and March 2010, the inflation consultation clause, and the indicative targets under the program are set out in Table 1.

8. We believe that the policies set forth in this letter, which supplements our letter and the attached Memorandum of Economic and Financial Policies (MEFP) of April 13, 2009, are adequate to meet the objectives of our economic program. We stand ready to take additional measures that may be needed for this purpose and will maintain the usual close and proactive policy dialogue with the Fund.

Sincerely yours,

/s/	/s/
Juan Alberto Fuentes Knight Minister of Finance	Maria Antonieta del Cid Navas de Bonilla President, Central Bank of Guatemala

Table 1. Guatemala: Quantitative Performance Criteria, Indicative Targets, and Inflation Consultation Clause

	2009						2010				
	End-June		End-September		End-December		End-Mar	End-Jun	End-Sept	End-Dec	
	EBS/09/49	Actual	EBS/09/49	Revised	EBS/09/49	Revised	Proposed	Proposed	Proposed	EBS/09/49	Revised
Performance Criteria (for end-Sept and end-Dec 2009, and end-Mar 2010; indicative targets otherwise)											
Overall balance of the central government, floor (millions of quetzales) 1/	-3,075	-1,955	-6,946	-7,700	-8,720	-10,600	-2,500	-4,100	-7,600	-8,742	-10,000
Net international reserves, floor (millions of US$) 2/	4,400	4,828	4,200	4,200	4,000	4,000	4,000	4,000	4,000	4,000	4,000
Accumulation of external arrears 3/	0	0	0	0	0	0	0	0	0	0	0
Indicative Targets											
Central government deposits at Banguat, floor (millions of quetzales)	10,899	9,394	7,695	5,000	7,642	4,900	6,000	4,500	3,500	6,290	3,800
Consultation clause on inflation 4/											
Outer band, upper limit	7.5	7.5	7.5	3.0	8.5	5.5	7.5	8.5	8.5	8.0	7.5
Inner band, upper limit	6.5	6.5	6.5	2.0	7.5	4.5	6.5	7.5	7.5	7.0	6.5
Inner band, lower limit	2.5	2.5	2.5	-2.0	3.5	0.5	2.5	3.5	3.5	3.0	2.5
Outer band, lower limit	1.5	1.5	1.5	-3.0	2.5	-0.5	1.5	2.5	2.5	2.0	1.5

1/ Cumulative from end of preceding year.
2/ The NIR targets were not adjusted for the SDR allocation.
3/ Continuous performance criterion.
4/ Deviations from the band's limits will trigger consultations with the Fund, as indicated in the TMU.

Annex: Summary of Appendices

Fund Relations. Guatemala has no outstanding purchases or loans. An 18-month Stand-By Arrangement was approved on April 22, 2009. The authorities are treating the arrangement as precautionary. In August 2009, Mr. Fernando Delgado was appointed Regional Resident Representative for Central America, based in Guatemala.

Technical Assistance. The regional Technical Assistance Center for Central America, Panama, and the Dominican Republic (CAPTAC-DR), which is based in Guatemala City, was opened in June 2009. Technical Assistance (TA) is already being provided to Guatemala through CAPTAC on revenue administration and issues related to the planned customs union between Guatemala and El Salvador. An STA mission visited Guatemala in July 2009 to provide TA on quarterly national accounts. During March 2008–May 2009, three missions from MCM assisted in designing an action plan for the development of secondary markets for private securities and improving the efficiency and effectiveness of monetary policy.

Statistical Issues. Data provision is adequate for surveillance. Some deficiencies remain in the areas of national accounts, government finance, money and banking, and price statistics. Guatemala became a participant in the General Data Dissemination System (GDDS) in 2004, and has expressed a desire to subscribe to the Special Data Dissemination Standard (SDDS). An SDDS assessment mission is scheduled in 2010 to address these issues.

Relations with the World Bank Group. As of June 30, 2009, the IBRD active portfolio consists of 7 projects with a commitment of US$402.7 million and net disbursements of US$66.2 million (16.4 percent). On July 28, 2009, the Board of Directors approved the Second Programmatic Fiscal and Institutional Development Policy Loan for $350 million. This DPL is part of a series developed within a medium-term framework designed to: (i) enhance macroeconomic stability, governance, and transparency; (ii) expand opportunities for vulnerable groups through improved targeting of social programs; and (iii) promote sustainable growth and productivity for better jobs.

Relations with the Inter-American Development Bank. On June 30, 2009, the IDB approved its country strategy for Guatemala for 2008–2011. The country strategy focuses on: (i) reducing chronic malnutrition; (ii) reducing the intergenerational transmission of poverty; (iii) upgrading and maintaining production infrastructure; and (iv) achieving the revenue collection targets established in the Peace Accords. As of August 7, 2009, the IDB portfolio of approved sovereign guaranteed investment and policy-based loans under execution amounted to US$1,466 million, with an undisbursed balance of US$888.5 million.

INTERNATIONAL MONETARY FUND

GUATEMALA

First Review Under the Stand-By Arrangement and Requests for Modification of Performance Criterion and Consultation Clause—Informational Annex

Prepared by the Western Hemisphere Department
(In consultation with other departments)

September 8, 2009

Approved by Patricia Alonso-Gamo (WHD) and Dominique Desruelle (SPR)

Contents Page

Appendix I. Guatemala—Fund Relations
(As of July 31, 2009)

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

II. **General Resources Account:**

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 Department:	SDR Million	Percentage of Allocation
Net cumulative allocation	27.68	100.00
Holdings	1.16	4.19

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

V. **Latest Financial Arrangements:**

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	04/22/09	10/21/10	630.60	0.00
Stand-By	06/18/03	03/15/04	84.00	0.00
Stand-By	04/01/02	03/31/03	84.00	0.00
Stand-By	12/18/92	03/17/94	54.00	0.00

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

	Forthcoming				
	2009	2010	2011	2012	2013
Charges/Interest	0.05	0.08	0.08	0.08	0.08
Total	**0.05**	**0.08**	**0.08**	**0.08**	**0.08**

VII. **Safeguards Assessment**

Under the Fund's safeguards assessment policy, the Bank of Guatemala was subject to an assessment with respect to the Stand-By Arrangement, which was approved on April 22, 2009 (EBS/09/49). The assessment, which was completed in September 2009, found that the Bank of Guatemala has strengthened safeguards in the areas of financial reporting transparency and the management of foreign exchange reserves. Recommendations were made to further strengthen the bank's governance and independence.

VIII. Exchange Rate Arrangements

Since March 1994, Guatemala has had an arrangement based on an interbank foreign exchange market in which authorized financial institutions buy and sell foreign exchange at market-determined rates. Financial institutions authorized to operate in the foreign exchange market include commercial banks, finance companies, and exchange houses. The exchange regime is classified as "Floating." As of August 19, 2009, the reference exchange rate was Q8.26 per U.S. dollar.

IX. Last Article IV Consultation

The last Article IV consultation was concluded by the Executive Board on May 19, 2008. The next Article IV consultation is scheduled for November 2009.

X. FSAP Participation

An FSAP was conducted on July 3–7, 2000 and on September 11–23, 2000, and the Financial System Stability Assessment was discussed by the Executive Board on May 14, 2001 at the time of the 2001 Article IV consultation. An FSAP update was undertaken during October 27–November 10, 2005.

XI. Technical Assistance

Technical assistance provided in recent years has covered tax policy administration, expenditure management, inflation targeting, financial sector regulation and supervision, and statistics. Since 2004, FAD has provided assistance on tax policy, expenditure management and tax administration in various missions. STA has also assisted in completing General Data Dissemination System metadata for the financial and external sector, and in improving statistics on the balance of payments, the national accounts, and government financial statistics. In July 2009, a STA mission provided technical assistance on quarterly national accounts. MCM has provided assistance on inflation targeting, monitoring the banking system, and improving banking sector regulation and supervision. During March 2008–May 2009, three advisory missions assisted in designing an action plan for the development of secondary markets for private securities and improving the efficiency and effectiveness of monetary policy.

A regional Technical Assistance Center for Central America, Panama, and the Dominican Republic (CAPTAC-DR), started operations in June 2009. CAPTAC-DR, which is based in Guatemala City, will deliver capacity-building and training to seven countries in the region, supporting the implementation of the countries' development strategies in IMF areas of expertise. The center will also provide technical assistance (TA) at the regional and national level in support of ongoing economic and financial integration efforts in the region. TA is already being provided to Guatemala on revenue administration as well as on issues related to the planned customs union between Guatemala and El Salvador.

XII. **Resident Representative**

The Resident Representative office in Guatemala was opened in 2003. In August 2009, Mr. Fernando Delgado was appointed Regional Resident Representative for Central America, based in Guatemala.

Appendix II. Guatemala—Relations with the World Bank

(As of July 28, 2009)

The Bank's Country Partnership Strategy for Guatemala. The Bank's Country Partnership Strategy (CPS) for the period FY09–12 was developed in close collaboration with the government and wide consultation with country stakeholders. The CPS was discussed by the Bank's Executive Board in September 2008 and supports growth and poverty reduction strategies within the government's development program, Plan de la Esperanza. The CPS supports key elements of Guatemala's program, including a new conditional cash transfer program, policies to support natural disaster risk mitigation, fiscal reform, rural infrastructure development, and other poverty reduction efforts.

IBRD Flows and Total Debt Outstanding. IBRD disbursements to Guatemala have increased in recent years, rising from an annual average of about US$90 million during 2003–06 to an average of some US$160 million during 2007–09. Guatemala's total debt outstanding to the IBRD was US$979.5 million as of end-July 2009.

The current portfolio. As of July 28, 2009, the IBRD active portfolio consisted of 7 projects with a total commitment of US$402.3 million and net disbursements of US$66.2 million. These comprise six investment loans and one Catastrophic Development Policy Loan with Deferred Draw-down Option (CAT DPL-DDO).

In addition, the Board of Directors approved the Second Programmatic Fiscal and Institutional Development Policy Loan (DPL) for $350 million on July 28, 2009. This DPL is part of a series developed within Guatemala's medium-term development plan and is designed to: (i) enhance macroeconomic stability, governance, and transparency; (ii) expand opportunities for vulnerable groups through improved targeting of social programs; and (iii) promote sustainable growth and productivity for better jobs.

IBRD Flows (US$ millions)

	2003	2004	2005	2006	2007	2008	2009*
Disbursements	45.0	79.2	34.5	198.8	136.3	132.6	211.4
Amortizations	17.9	29.2	33.0	36.2	38.1	66.5	37.8
Net disbursements	27.1	50.0	1.4	162.6	98.2	66.1	173.7
Charges and fees	18.6	16.9	19.0	28.4	37.3	39.7	19.8
Net cash flows	8.5	33.1	-17.6	134.2	60.8	26.4	153.8
Debt outstanding	427.6	477.7	478.9	641.5	739.7	805.8	979.5

* Through July 31, 2009.

IBRD Operations by Sector, in US$ millions, as of July 28, 2009

	Disbursed	Undisbursed
Law and public administration	32.3	17.4
Health	8.7	40.2
DPL/DPL-DDO	0	85.0
Transportation	16.0	30.6
Rural development	0.4	29.5
Land management	1.6	60.6
Education	7.2	72.8
Total	**66.2**	**336.1**

Appendix III. Guatemala—Relations with the Inter-American Development Bank

(As of August 2009)

A. Recent Projects and Objectives

1. On June 30, 2009, the IDB approved its country strategy for Guatemala for 2008–2011. The country strategy was the product of dialogue with the current Guatemalan administration. It will focus on supporting the following government goals: (i) reducing chronic malnutrition; (ii) reducing the intergenerational transmission of poverty; (iii) upgrading and maintaining production infrastructure; and (iv) achieving the revenue collection targets established in the Peace Accords.

2. As of August 7, 2009, the IDB portfolio of approved sovereign guaranteed investment and policy-based loans under execution amounted to US$1,466 million, with an undisbursed balance of US$888.5 million. The existing portfolio focuses on: (i) supporting the reform and modernization of the State (including a policy-based loan targeted to support the government's efforts in modernizing its fiscal system); (ii) strengthening the country's social programs (including a policy-based loan directed to support the Conditional Cash Transfer program); and (iii) improving productive infrastructure (especially in the rural areas and in the water and sanitation sector).

3. In the private sector, over the last two years, the IDB has approved one lending facility for the financial sector (US$45 million) and two credit line operations for trade financing (US$75 million).

4. The pipeline includes projects in the areas of health and nutrition and water and sanitation. In addition, the Bank continues to support nonfinancial activities, including assistance in the area of fiscal reform, health and nutrition, education, water and sanitation, and public sector strengthening.

B. IDB Loan Disbursements 2005–2009

(In millions of U.S. dollars)

	2005	**2006**	**2007**	**2008**	*2009**
Disbursements	33.0	130.3	213.7	139.0	377.8
Amortization	56.0	63.2	56.4	85.2	84.2
Net Disbursements	-23.0	67.1	157.3	53.8	293.6
Interest and Charges	45.8	55.0	59.1	71.6	66.9
Subscriptions and Contributions	0.7	2.6	3.5	3.9	
Net Cash Flows	-69.5	9.5	94.7	-21.7	226.7

Source: IDB Financial Department
* Projections

C. IDB Portfolio in Guatemala as of August 2009
(In millions of U.S. dollars)

Sector	**Approved**	*Undisbursed*
Rural development and agriculture	30.1	3.1
Trade	85.0	78.2
Financial and capital markets development	45.0	45.0
Science and technology	6.2	0.0
Urban development and housing	62.9	21.8
Education	150.0	120.0
Energy	92.5	60.1
Social investment	248.0	209.0
Sanitation	49.8	44.1
Environment and natural disasters	89.2	67.7
Reform and modernization of the State	458.5	308.5
Health	105.4	50.9
Transportation	140.0	0.7
Total	**1,562.6**	**1,009.1**

Note: Sovereign guaranteed and nonsovereign guaranteed programs.
Excluding regional programs.

Appendix IV. Guatemala—Statistical Issues

<table>
<tr><td colspan="2">Guatemala—Statistical Issues Appendix
As of August 2009</td></tr>
<tr><td colspan="2">I. Assessment of Data Adequacy for Surveillance</td></tr>
<tr><td colspan="2">General: Data provision is adequate for surveillance.</td></tr>
<tr><td colspan="2">National Accounts: quarterly national accounts data are not available, but the Bank of Guatemala expects to publish quarterly GDP statistics at end-2009. STA has provided technical assistance and is working closely with the Bank of Guatemala in the development of quarterly GDP estimates.</td></tr>
<tr><td colspan="2">Price statistics: a producer price index (PPI) is not compiled. The National Institute of Statistics is planning to develop a PPI in the medium term, subject to resource availability.</td></tr>
<tr><td colspan="2">Public sector data: fiscal statistics do not include social security agencies, local governments, and nonfinancial public enterprises, hindering the calculation of a consolidated public sector balance.</td></tr>
<tr><td colspan="2">Financial sector data: The sectorization of some instruments on the balance sheet of other depositary corporations is pending. In particular, for loans, there is no classification available between nonresidents and residents.</td></tr>
<tr><td colspan="2">II. Data Standards and Quality</td></tr>
<tr><td>Guatemala became a participant in the General Data Dissemination System (GDDS) in 2004, and is interested in subscribing to the Special Data Dissemination Standard (SDDS). Several data categories are yet to meet the periodicity or timeliness requirements prescribed by SDDS. An SDDS assessment mission is scheduled in 2010 to address these issues.</td><td>A data ROSC was completed on October 28, 2004.</td></tr>
</table>

Guatemala: Table of Common Indicators Required for Surveillance

(As of August 20, 2009)

	Date of latest observation	*Date received*	*Frequency of Data*[7]	*Frequency of Reporting*[7]	*Frequency of Publication*[7]	*Memo Items:* Data Quality – Methodological soundness[8]	*Memo Items:* Data Quality – Accuracy and reliability[9]
Exchange Rates	19/08/09	20/08/09	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	19/08/09	20/08/09	D	D	D		
Reserve/Base Money	13/08/09	20/08/09	W	W	W	O, LO, LO, LO	LNO, O, O, O, LNO
Broad Money	13/08/09	20/08/09	W	W	W		
Central Bank Balance Sheet	19/08/09	20/08/09	D	D	D		
Consolidated Balance Sheet of the Banking System							
Interest Rates[2]	13/08/09	20/08/09	W	W	W		
Consumer Price Index	31/07/09	07/08/09	M	M	M	O, LO, LO, LO	LO, LO, LO, LO, LO
Revenue, Expenditure, Balance, and Composition of Financing[3] – General Government[4]			NA	NA	NA	LO, LNO, LO, LO	LO, O, LO, LO, LNO
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	30/06/09	24/07/09	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	31/06/09	24/07/09	M	M	M		
External Current Account Balance	31/03/09	30/06/09	Q	Q	Q	LO, LO, LNO, LO	LNO, LNO, LO, LO, LNO
Exports and Imports of Goods and Services	31/03/09	29/06/09	Q	Q	Q		
GDP/GNP	31/12/08	31/03/09	A	A	A	LNO, LNO, LNO, LO	LNO, LNO, LNO, LNO, LNO
Gross External Debt	31/12/08	29/06/09	A	A	A		
International Investment Position[6]	31/12/08	29/06/09	A	A	A		

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).
[8] Reflects the assessment provided in the data ROSC, (published on June 10, 2005 and based on the findings of the mission that took place during October 14–28, 2004) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).
[9] Same as footnote 7, except referring to international standards concerning source data, statistical techniques, assessment and validation of source data, assessment, and revision studies.

INTERNATIONAL MONETARY FUND EXTERNAL RELATIONS DEPARTMENT

Press Release No. 09/326
FOR IMMEDIATE RELEASE
September 24, 2009

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Completes First Review Under Guatemala's Stand-By Arrangement

The Executive Board of the International Monetary Fund today completed the first review of Guatemala's economic performance under the 18-month Stand-By Arrangement. The arrangement, in the amount of SDR 630.6 million (about US$1 billion) was approved in April 22, 2009 (see Press Release No. 09/142).

With completion of the review, a total of SDR 462.4 million (about US$734 million) will be available for drawing. The Guatemalan authorities intend to continue treating the arrangement as precautionary.

The authorities' economic program for 2009–10, supported by the current arrangement, aims at mitigating the impact of the global crisis. The strategy is centered on four pillars: a moderate fiscal stimulus to support domestic demand; a monetary policy focused on meeting the inflation target and a flexible exchange rate to facilitate economic adjustment; a strengthening of financial sector policies to increase banking sector resilience and enhance its safety net and resolution procedures; and a refocusing of public expenditures toward social spending and public investment.

Following the Executive Board discussion on Guatemala, Mr. Murilo Portugal, Deputy Managing Director and Acting Chair, issued the following statement:

"After a solid economic performance in recent years, the Guatemalan economy is being negatively affected by the global crisis. Economic growth is slowing owing to lower domestic and external demand, reflected in lower exports, remittances, tourism receipts and capital inflows. The authorities are to be commended for their strong program implementation in a difficult environment, and for responding appropriately to the economic slowdown.

"Fiscal policy is striking a balance between supporting demand and maintaining fiscal sustainability. With revenues falling due to lower imports and weak domestic demand, the fiscal deficit target in the program has been revised upward in 2009 and 2010 as the authorities' aim at protecting spending on social programs.

“Rekindling the fiscal reform agenda is essential to preserve sustainable debt dynamics. Revenue-enhancing reforms are at the core of a strategy to address social and infrastructure needs, enhance the capacity to adopt countercyclical policies, and boost confidence in the authorities’ capacity to stabilize the public debt-to-GDP ratio at moderate levels. Given the withdrawal of the indirect tax reform from Congress, the plan to pursue a revenue reform is welcome. In addition, curtailing tax exemptions, including those associated with the law on free trade zones, will be key to safeguard fiscal revenue and ensure a level playing field.

“The gradual easing of the monetary policy stance has balanced the goals of supporting demand and avoiding disorderly exchange rate movements. Monetary policy has scope to support domestic demand as long as inflation remains subdued and there are no external pressures. Exchange rate flexibility has facilitated the adjustment of the economy to the external shock and should be preserved, while safeguarding international reserves.

“The financial system has weathered the economic slowdown well, and the authorities are committed to moving ahead with banking sector reforms. Congressional approval and a decisive implementation of the proposed amendments to the banking law will reduce risks from offshore operations and connected lending, enhance the enforcement powers of the superintendency of banks, and improve bank resolution procedures.” Mr. Portugal said.

Statement by Ramon Guzmán, Executive Director for Guatemala
and Johnny Gramajo-Marroquin, Senior Advisor
September 22, 2009

We would like to thank the Staff for a helpful and well-written report. The Guatemalan Authorities broadly agree with the Staff's assessment. Under the Stand-By Arrangement, all end-June quantitative performance criteria were met. The Authorities want to stress that they continue treating the arrangement as precautionary and they are strongly committed to their economic program.

The global turmoil has had negative impact in most small economies, Guatemala has not been the exception. We are enduring the consequences of, on the one hand, the deterioration in global trade, and on the other, the sharp economic downturn in most of the developed world. The channels through which these imbalances are affecting the Guatemalan economy are: i) lower exports; ii) reduction in tourism receipts; iii) decline in remittances; iv) slowdown in private capital flows; and v) large contraction in imports that impacts fiscal revenues hard. In spite of these developments, the long track record of accomplishment on fiscal and monetary discipline that, along with the implementation of important structural reforms, have contributed to maintain macroeconomic stability. Economic growth is projected to be around 0.4 percent in 2009 and inflation is expected to decline sharply.

To help mitigate the adverse effects of the global crisis my authorities will continue implementing their economic program, which aims at maintaining price stability and giving a countercyclical role to fiscal policy. A key priority for the authorities is to offset the effect of the current crisis on the most vulnerable sectors of the population and to continue with the mid-term effort to reduce poverty. To attend extreme poverty, emphasis has been placed on the government program of conditional cash transfers. The program, *Mi familia progresa*, aims at ensuring that poor children attend school and visit health centers regularly. In 2009, this program expects to cover around 500,000 families with a total budget of US$150 million.

With fiscal revenues declining more sharply than originally envisaged, the target for fiscal deficit of the consolidated public sector has raised to 3.0 percent of GDP in 2009 and 2.6 percent of GDP in 2010. The authorities believe that the revised fiscal targets strike an appropriate balance between providing a necessary stimulus to domestic demand and preserving social spending, while also keeping public debt dynamics manageable.

The revised fiscal deficit for 2009 and 2010 will be partly financed from external sources, mostly multilateral institutions. The authorities' financing strategy foresees that net domestic debt placements and use of government deposits at the central bank will be higher than anticipated.

In response to the downside risks to inflation and lower economic activity, monetary policy actions have been prudent in order to maintain macroeconomic stability. Monetary policy interest rate has been reduced by 275 basis points since end-2008, to 4.50 percent. Inflation is expected to be about 1.5 percent by end-2009 and about 4.0 percent by end-2010, thus the revised quarterly consultation bands for CPI inflation under the program are consistent with these projections. The Monetary Board's intention is to continue managing the policy rate as needed to meet the inflation target, and the central bank remains committed to its flexible exchange rate regime. Intervention in the FX market will remain geared at smoothing out excessive volatility.

The Guatemalan financial system has been resilient to the external shocks. Several reasons come to mind: a) there were no “toxic” asset holdings in the system, b) the low reliance of banks on external credit, c) the higher capital cushions built since late 2005, and d) the measures that authorities took as the crisis unfolded, including liquidity support, intensifying banking supervision and restoring provisioning requirements. The Authorities are committed to further strengthening the regulatory framework, including concluding the design of regulations on banks’ liquidity management and foreign currency credit risk by end-December 2009, with their implementation beginning in the fist quarter of 2010. In addition, they will continue to work closely with Congress to ensure prompt approval of the amendments to the banking legislation, which are crucial to strengthen regulation and supervision and to enhance the current bank resolution framework.

There are two issues that my authorities wish to stress with regard to the evaluation of the risks to the program in the staff report. First, they do not share the view that a potential deterioration of economic conditions in one specific neighboring country poses risks. In their view on the current global economic environment, potential deterioration could stem from many other reasons. Second, my authorities want to emphasize that it was not the lack of political support which caused the withdrawal of the tax reform from Congress but the consideration that many loopholes were being introduced to it, making it ineffective. Thus the Ministry of Finance expects to work closely with Congress to enact a revenue reform to help ensure a gradual recovery of tax collections from 2010 onwards based on a new initiative.

The Authorities believe that the ongoing policies are adequate to meet the objectives of their economic program.