Guatemala

The Guatemalan economy grew by 4.6% in 2006, thanks to burgeoning private consumption fuelled by family remittances (10% of GDP). In October, annual inflation stood at 3.9%. As the deficit on the current account of the balance of payments (4.3% of GDP) was easily financed, it was possible to continue to build up international reserves. For 2007, the authorities project GDP growth of 5.1%, inflation between 4% and 6% and a government deficit of 1.8% of GDP.

Macroeconomic stability provided a favourable backdrop between the Dominican Republic-Central America-United States Free Trade Agreement (CAFTA-DR) to enter into force; and this supported the largest inflow of foreign direct investment (FDI) of the last five years. Nonetheless, the oil bill increased once again on the back of higher oil prices.

The government deficit (originally forecast in the budget at 1.8% of GDP) was raised to 2.5%, to allow execution of the rehabilitation and reconstruction programme created to mitigate the damage caused by tropical storm Stan, which had devastated the country in October 2005. Nonetheless, the outturn was similar to the previous year's deficit of 1.5% of GDP, since revenue proved higher than expected and a number of expenses were postponed.

Total revenue grew following the implementation of laws to strengthen tax administration, mainly to combat evasion. In this context, the Fiscal Register of Printing Presses was established, a number of taxation procedures were channelled through bank accounts, and tax administration powers were widened. Steps were also taken to reduce smuggling and tax avoidance. Thanks to these laws and advances in tax administration, government income grew by 7% in real terms, despite a reduction in revenue arising from the tariff cuts mandated by CAFTA-DR. As a consequence, the tax burden rose to 10.2% of GDP in 2006 (compared with 9.6% in 2005). Nonetheless, its low level continues to hamper the execution of social projects.[1]

Total expenditure grew by 7% in real terms, with capital expenses increasing by 9%, reflecting greater execution of physical investment projects and capital transfers to autonomous and decentralized institutions. In addition, resources were allocated in line with the priorities established in the peace agreements.

The external public debt amounted to US$ 3.932 billion, or US$ 200 million more than in 2005. Loan disbursements to the Central Government by the Central American Bank for Economic Integration (CABEI) and the World Bank, were channelled into productive activities.

Monetary policy continued to be aimed at establishing explicit inflation targeting, for which a range of 5%-7% was set for 2006. With a view to reducing inflationary pressures, the authorities raised the monetary-policy interest rate by 0.25 percentage points three times during the year, such that in November the rate stood at 5%. Between January and October, nominal deposit and borrowing rates averaged 4.7% and 12.7%, respectively, while the corresponding real rates were -0.4% and 7.6%.

In addition, to reduce exchange-rate volatility, the Bank of Guatemala purchased US$ 130.5 million on the foreign-exchange market, in keeping with its exchange-rate rule. Government deposits at the Bank of Guatemala were kept above the programmed level, thereby making it possible to mitigate monetization. Despite this support and open-market operations, the broad money supply expanded by 5.5% in real terms, while credit extended to the private sector grew by 6.5%. As a consequence of

[1] The Central American Institute for Fiscal Studies (ICEF) believes the tax burden should be raised to 15% of GDP, since it stood at 10% of GDP in 1995 (according to the new national accounts that will be available in 2007).

the stability of the nominal exchange rate and reduction in domestic inflation, in September the real effective appreciation of the quetzal (3%) eased in comparison with the 2005 figure (7%).

The banking system operated with relatively stable interest rates in 2006, and there was a significant credit expansion, in addition to portfolio quality improvements and a reduction in non-performing assets. In October, Banco del Café (BANCAFÉ) was intervened having failed to fulfil the restructuring programme agreed upon with the authorities, following problems with a subsidiary.[2] This measure had no effect on the rest of the country's banks and financial institutions. Small deposits are protected by the Savings Protection Fund (FOPA).

The economic growth that had begun in 2004 strengthened further, with GDP expanding by 4.6%, the highest rate recorded since 1998, and per capita GDP increasing for the second year running. This performance was assisted by private consumption growth, fuelled by income from family remittances, and the buoyancy of private investment especially in construction. The boom in this sector (29%) was supported by an expansion of credit in real terms. Transport and communications also displayed buoyant growth, along with the banking, insurance and real estate sectors. In contrast, agriculture and manufacturing grew more slowly.

The inflation target for 2006 will be met, since the estimated rate of 5% coincides with the floor of the target range. This result is thanks to the stability of the nominal exchange rate and a good agricultural season, unlike 2005 which was impacted by tropical storm Stan. Although there was no unemployment survey in 2006, the employment rate is likely to have risen on the back of the country's economic growth. The rate of unemployment remains high nonetheless. The minimum wage rose by 5% in real terms.

On the external front, the current account deficit was 4.3% of GDP, similar to the previous year's figure, with the trade gap in goods and non-factor and factor services (15.9% of GDP) being offset by a surplus in current transfers equivalent to 11.6% of GDP.

Merchandise exports grew by 10%, which was less than in 2005, while imports grew by a similar amount (12.5%). Traditional exports were flat. Coffee exports fell by 9% as a result of smaller volumes shipped, with the price unchanged. In contrast, cardamom exports grew as a result of larger shipments, while sugar and oil exports expanded on the back of higher prices. Banana exports were down because of lower prices, despite a larger volume exported. Non-traditional exports expanded by 8%, boosted by sales of rubber, flowers and other products. In contrast, exports of most other non-traditional products declined. External sales to Central American countries remained buoyant, while maquila exports partially recovered.

With regard to imports of intermediate goods, the oil bill increased sharply to account for almost 20% of total purchases. Purchases of inputs destined for the construction sector remained strong, while capital goods imports were led by purchases of machinery and equipment for the manufacturing industry.

Income on the capital and financial account totalled US$ 1.7 billion. Foreign direct investment attained a level of US$ 325 million and was mainly channelled into the communications, commerce, and chemical industry sectors. As the capital inflow more than covered the current account deficit, there was an overall balance-of-payments surplus (US$ 225 million).

Table 1
GUATEMALA: MAIN ECONOMIC INDICATORS

	2004	2005	2006 [a]
	Annual growth rates		
Gross domestic product	2.7	3.2	4.6
Consumer prices	9.2	8.6	4.4 [b]
Average real wage	-2.4	-3.9	...
Money (M1)	10.3	14.5	18.6 [c]
Real effective exchange rate [d]	-3.0	-7.1	-3.5 [e]
Terms of trade	-0.9	-0.9	-1.9
	Annual average percentages		
Urban unemployment rate	4.4	...	...
Central administration overall balance/GDP	-1.0	-1.5	-1.5
Nominal deposit rate	4.5	4.6	4.7 [f]
Nominal lending rate	13.8	13.0	12.7 [f]
	Millions of dollars		
Exports of goods and services	4 546	4 939	5 478
Imports of goods and services	8 483	9 547	10 783
Current account	-1 211	-1 387	-1 533
Capital and financial account	1 819	1 642	1 758
Overall balance	609	254	225

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
[a] Preliminary estimates.
[b] Twelve-month variation to November 2006.
[c] Year-on-year average variation, January to September.
[d] A negative rate indicates an appreciation of the currency in real terms.
[e] Year-on-year average variation, January to October.
[f] Average from January to September, annualized.

2 An offshore subsidiary, Bancafé International Bank, had invested in Refco Capital Markets, a New York stock and bond brokerage firm, which filed for bankruptcy in October 2005.