

EXECUTION COMMITTEE

ACT NUMBER 41-2008

Session 41-2008 celebrated in the *Banco de Guatemala* building located at *séptima avenida número veintidós guión cero uno, zona uno* of this city, on Thursday, August fourteenth, two thousand eight, at thirteen hours and ten minutes.

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

FIRST: Knowledge of the project of act number 40-2008 corresponding to the session celebrated on August 8, 2008.

CIRCULATE: project of act number 40-2008.

SECOND: Information on markets and monetary variables.

- a) Money Market
- b) Exchange Market
- c) Indicative Variables
- d) Estimated Monetization Flow
- e) Proposal of quotas for bids in term deposits
- f) Determination of quotas for bidding of term deposits

THIRD: Third running of the Semi-structural Macroeconomic Model of the MMS 2008.

FOURTH: Inflation Risks Balance

FIFTH: Discussion

SIXTH: Other matters and reports.

Not having observations, the Committee approved the Order of the day.

FIRST: The coordinator submitted the projects of the corresponding acts for consideration.

Not having observations, the Committee approved Act number 40-2008.

SECOND: Information of markets and monetary variables.

The Coordinator requested the corresponding information be provided.

a) The Director of the Department of Monetary Stabilization Operations, regarding the Money Market informed that during the period from August 8 to 13, 2008, registered a placements for LTD's of Q2,547.3 million and maturity for Q2,120.5 million, which gave as a result net placements for Q426.8 million, associated to the

operations made in bidding through commerce exchanges (net placements for Q17.0 million), in the Electronic Banking Money Table –MEBD- and in the *Bolsa de Valores Nacional, S. A.* stock exchange (net placements for Q449.0 million); and at the window (net maturity for Q39.2 million).

Regarding the DP fund-raising, it was indicated that during the period of August 8 to 13, 2008, for the biddings case, the same were made per due date and price, indicated that in the bidding made through the commerce exchanges, the cut price was of 95.8370% for maturities dated March 9, 2009, equivalent to a yield rate of 7.5500%; for the maturities on June 8, 2009 the cut price was of 94.0661%, equivalent to a yield rate of 7.6495%; while for the direct bid there were no bids. In the MEBD and in the *Bolsa de Valores Nacional, S. A.* stock exchange, the fund-raising was held for a 7 day term, the leading interest rate was of 7.25%.

Regarding liquidity injecting operations it was reported that, during the period of August 8 to 13, 2008, operations for Q23.6 million for a 7 day term; at an interest rate of 8.75%. It was indicated that in the referred operations they received Representative Certificates of Treasury Bonds from the Republic of Guatemala expressed in quetzales and in US dollars as a guarantee.

As to the weighted average interest rates of total operations of repurchase agreements made in the stock exchange of the country, it was indicated that, during the August 8 to 13, 2008 period, the minimum was of 7.29% observed on August 8, 2008 and the maximum was of 7.46% registered on August 13, 2008. It also pointed out that the amounts negotiated were guaranteed with public titles and that the weighted average interest rate during said period was of 7.37%.

On the other hand, it was informed that on August 13 of this year, they had repurchase agreement operations in the exchange market and in the over the counter market, in the banks of the system and the financial stock companies, with term deposits from the *Banco de Guatemala* and Guatemalan Treasury Bonds for Q97.0 million with a weighted average yield of 7.2881%; of which Q22.0 million were made in the exchange market at a weighted average yield rate of 7.3273% and Q75.0 million in the over the counter market, at a weighted average yield rate 7.2767%; as well as operations in the stock market for US\$4.6 million with an average weighted yield of 4.0000%.

Finally, regarding the placement of treasury bonds of the Republic of Guatemala, during the period of August 8 to 13, 2008, maturities were registered for Q4.0 million.

b) The Director for the Monetary Stabilization Operations Department regarding the Institutional Market for foreign currency reported that during the period of August 7 to 12, 2008, the average daily operations for purchase were of US\$58.6 million and the sale was of US\$64.1 million and that the weighted average exchange rates of the referred operations showed a tendency to rise. In effect, on Thursday, August 7 they were of Q7.38180 per US\$1.00 for purchase and of Q7.39721 per US\$1.00 for sale; in that order, on Friday, August 8 was of Q7.38008 and Q7.40404; on Monday, August 11 were of Q7.38312 and Q7.41214; and on Tuesday, August 12 they were Q7.39477 and Q7.41998. Also, it was indicated that the current exchange reference rate for August 14, 15, 16 and 17 of the current year is Q7.40845 per US\$1.00.

In the operations of the electronic systems of negotiations of foreign currency administered by the *Bolsa de Valores Nacional, S.A.* (National Stock Exchange, S.A.), for the period of August 8 to 13, 2008, it was commented that the Private Institutional Foreign Currency System –SPID-, there were no operations. Regarding the Electronic Foreign Currency Negotiation System –SINEDI-, according to the established in the participation rules of the *Banco de Guatemala* in the institutional foreign currency market, did not convene any bids in US dollars.

On the other hand, they informed that the Future Foreign Currency Market that is operated by the National Stock Exchange, S.A., during the period of August 8 to 13, 2008, did not close operations and that on Wednesday, August 13 there was no reference price for the market to settle in September 2008.

c) The Director for the Economic Studies Department reported that between August 7 and 13, 2008, according to preliminary numbers, the daily legal reserve of the banking system went from a position of Q668.8 million to a one of Q390.8 million, while for the balance of investments in DP to 7 days in that period, went from Q2,383.0 million to Q2,832.0 million, so the amount of liquid resources of the banking system (daily position of legal reserve plus investments in DP to 7 days) went from Q3,051.8 million on August 7 to Q3,222.8 million on August 13, 2008. They also mentioned that during said period they registered net placements of liquidity giving operations of the *Banco de Guatemala* for Q43.5 million.

The highlights during the period of August 7 to 13, 2008, of the main monetizing

factors of the monetary issue were the decrease in the balance of the legal banking reserve for Q449.6 million and the deposits of the Central Government in the *Banco de Guatemala* for Q185.1 million; while the main demonetizing factors were the increase in the balance of the monetary stabilization operations for Q426.8 million and the decrease in the balance of the Net International Reserves for the equivalent in quetzales of Q372.0 million.

Regarding the indicative variables of the Monetary, Foreign Exchange Rate and Credit Policy they indicated that with data to July 2008, for December 2008 the total expected inflation estimated with a model of ordinary squared minimums is of 11.17% and with a softened exponential model of 12.14% the simple average of both models is located at 11.66%, percentage which is found over the tolerance margin of the policy target (5.5% +/- 1.5 percentage point), which suggests a restrictive monetary policy; and, for December 2009 the total expected inflation, estimated with an ordinary squared minimum model, is of 8.98% and with a softened exponential model of 8.10%; the simple average of both models is at 8.54%, which is over the tolerance margin of the policy target (5.5% +/- 1 percentage point), which suggests a restrictive monetary policy.

Regarding the expected subjacent inflation for December 2008, with data up to July 2008, estimated with an integrated auto-regression model of mobile averages ARIMA was of 8.83%, whereas the estimated with a softened exponential model was of 8.71%; the simple average of both models is of 8.77%, which is over the punctual value of the inflation target and within the tolerance margin of the same (5.5% +/- 1.5 percentage point), which suggests a restrictive monetary policy; and, for December 2009 the estimated subjacent inflation with an integrated autoregressive model of mobile averages ARIMA, was of 7.72%, whereas the estimated softened exponential model was of 6.97%; the simple average of both models is of 7.35%, which is located over the tolerance margin of the same (5.5% +/- 1 percentage point), which suggests a restrictive monetary policy.

As to the parameter rate, it was reported to August 7, 2008, the lower limit was 7.54%, and the upper limit is 11.49%; while the leading interest rate of the monetary policy was at 7.25%, which is below the lower limit of the tolerance margin estimated for the parameter rate, situation that suggests a restrictive monetary policy. When referring to the parity liable rate, they declared that up to August 7, 2008, the lower limit was 4.83% and the upper limit was 5.73%, and the weighted average rate of long

term deposits of the banking system was of 7.56% which is located over the upper limit of the fluctuation margin of the parity liable rate, which suggests relaxing the monetary policy.

As to primary liquidity it was indicated that monetary issue observed to August 13, 2008, is found Q580.1 below the lower limit of the programmed runner, which would indicate relaxing the monetary policy, whereas the broad monetary base, on that same date, is within the programmed runner at Q723.4 million over the upper limit of the programmed runner, which suggests a restrictive monetary policy. The average orientation of the deviation for the present week (Q71.7 million) would indicate restricting the monetary policy.

As to the total payment means, the inter-annual variation observed to August 7, 2008, rose to 5.8%, which is below the lower limit of the estimated runner for said variable on the same date (10.7% to 13.7%), which suggests relaxing the monetary policy; whereas, the econometric estimation of the payment means for December 2008 is of 9.5%, which is below the lower limit of the expected range for December 2008 (11.0% to 14.0%), which suggest relaxing the monetary policy. The average orientation of the deviation (-3.20%) therefore suggests relaxing the monetary policy. Also, up to said date, the inter-annual variation of banking credit of the private sector registered growth of 17.3%, which is below the lower limit of the estimated runner for August 7, 2008 (19.7% to 22.7%), which suggests a relaxed monetary policy; on the other hand, the econometric estimation for the end of 2008 of the banking credit to the private sector is 14.7%, which is below the expected range (17.0% to 20.0%), which suggests a relaxed monetary policy. The average orientation of the deviations for the present week of -2.35%, therefore suggests a relaxed monetary policy.

As to the inflation expectations of the panel of private analysts, it was indicated that, according to the survey made in July 2008, for December 2008 the inflation projection is at 12.42%, which is over the tolerance margin of the policy target (5.5% +/- 1.5 percentage points), which suggests a restrictive monetary policy; and, for December 2009, the inflation projection will be at 9.29%, which is also over the tolerance margin of the inflation target (5.5% +/- 1 percentage point), which suggests restricting the monetary policy. Also indicating that the implied inflation expectations variable with data to July 2008, showed an inflationary rhythm of 6.29%, which is over the punctual value of the inflation target and within the tolerance of the monetary policy target for 2008 (5.5% +/- 1.5 percentage points), which suggests a moderately

restrictive monetary policy.

Regarding the Semi-structural Macroeconomic Model (MMS) used in August 2008 to forecast the total inflationary rhythm, this is projected for December 2008 at an inflationary rhythm of 11.90%, conditioned to gradual adjustments in the leading interest rate of the monetary policy until locating itself, on average, in the last quarter of said year at 8.26%. Also the forecast for said model of a mid-term horizon projected an inflationary rhythm for December 2009 of 7.59%, conditioned to gradual adjustments to the leading interest rate, in the last year at 4.85%.

As to the orientation of the indicative variables, regarding the previous week, it was indicated that two varied, in the following manner: "Parameter Interest Rate" variable went from suggesting an invariable monetary policy to advising a restrictive monetary policy and the "Inflation Forecast in the Medium Term of the Semi-structural Macroeconomic Model" for December 2009, in its third running, went from advising a moderately restrictive monetary policy to advising the same be restrictive. In that sense, according to the relative weight assigned to the indicative variables, it was reported that 63.73% of the same suggest a restrictive monetary policy orientation (46.15% the previous week), 9.34% suggest a moderately restrictive monetary policy orientation (17.58% the previous week); 0.0% suggest an invariable monetary policy (9.34% the previous week); and 26.93% suggest a relaxed monetary policy orientation (equal percentage the previous week).

On the other hand, they indicated that regarding the behavior of the nominal exchange rate, the upper and lower limits for the estimated runner (according to its seasonality) for the week of August 11 to 14, 2008 were of Q7.760 and Q7.640 per US\$1.00, respectively; and the observed level (calculated as the average of the exchange rate in the Institutional Market of Foreign Currency for the period between August 11 and 13) was of Q7.407 per US\$1.00; with which the observed value of the nominal exchange rate is located below the lower limit of the referred runner.

d) The Sub-Director of the Department of Economic Studies informed the Committee of the monetizing and demonetizing factors forecast in the Estimated Monetization Flow for the week of August 18 to 21, 2008, which indicate an excess of primary liquidity for Q3,040.2 million mainly due to the maturity of CDs and the use of deposits by the Central Government in the Banco de Guatemala; if we add the negative daily banking liquidity position for Q10.8 million and the negative deviation observed in the monetary issue for Q464.2 million, resulting in excess aggregate

liquidity estimated for the referred period of Q2,565.3 million; if these factors are given, to make a compatible issue offer with the programmed demand, it would be necessary for the CDs that mature during the period (Q2,515.3 million; according to the registry to August 13, 2008) and fund-raise additionally for around Q49.9 million.

e) The Director of the Department of Monetary Stabilization Operations based on the estimated monetization flow and on the guidelines established for the determination of the quotas for the bidding of term deposits through the commodity exchanges, proposed to the Execution Committee that they be Q10.0 million, Q10.0 million, Q20.0 million and of Q25.0 million for the following maturity dates: September 8, 2008 and December 8, 2008, March 9, 2009 and June 8, 2009, respectively; and the due date of June 7, 2010, without a pre-established quota.

f) Determination of the quotas for term deposit bidding

Regarding the determination of quotas for bidding on August 4, 2008, the proposal from the Department of Monetary Stabilization Operations was taken into account, that includes the information that provides the estimated monetization flow for the following week and, on the other hand, the guidelines to keep the number of weekly bids. Based on this, the Committee approved the proposal of the technical departments and, therefore, agreed to establish the fund-raising quotas in the following manner: for September 8, 2008, Q10.0 million; for December 8, 2008, Q10.0 million; and, for March 9, 2009, Q20.0 million; June 8, 2009, Q25.0 million; as well as the due date of June 7, 2010, without a pre-established quotas.

THIRD: Third Running of the Semi-structural Macroeconomic Model –MMS [For its acronym in Spanish]- 2008.

The Committee continued deliberating on the analysis of the leading interest rate of the monetary policy to be presented to the Monetary Board in session dated Wednesday, August 20, date on which said licensed body will decide on the level of said interest rate. The technical departments presented the Committee with the medium term forecasts generated by the third running in 2008 of the Semi-structural Macroeconomic Model and, on the other hand, the Inflation Risks Balance.

Concerning the third running of the MMS in 2008, they began with a summary of the initial conditions of the running; following, they presented a report of the changes in the forecast of the inter-annual inflation rate and of the leading interest rate of the monetary policy regarding the forecast generated in the second running of the MMS in

2008 (made in May). In said report they indicated that the inter-annual inflation forecast for December 2008 (11.90%), is higher by 3.28 percentage points to the forecast generated, for the same date, in the second running of 2008 (8.62%). Said increase in the forecast of inflation mainly explains the changes in the following factors: short term inflation forecast (2.05%) and the price of diesel (0.89%). It was also indicated that the inflation forecast for December 2009, generated in the third running of 2008 (7.59%), is higher by 1.15 percentage points to the forecast generated, for the same date, in the second running of 2008 (6.44%). In this case, the increase in the forecast is mainly explained by the changes in the following factors: forecast of short term inflation (0.53%) and the price of diesel (0.31%).

As to the leading interest rate of the monetary policy, it was pointed out that the average forecast for the third and fourth quarters of 2008, generated in the third running of 2008 (8.20%), is higher by 80 basic points to the forecast generated, for the same period in the second running of 2008 (7.40%). This behavior is mainly explained by the following factors: short term inflation forecasts (68 basic points), the price of diesel (49 basic points) and the leading interest rate of the monetary policy (-43 basic points). On the other hand, the forecast of the leading interest rate of the monetary policy average for the last six quarters understood between the third of 2008 and the fourth of 2009, that was generated in the third running of 2008 (6.87%), is higher by 101 basic points to the average forecast generated, for the same period, in the second running of 2008 (5.86%). The increase of this average forecast is mainly explained by the changes in the following factors: inflation forecast in the short term (93 basic points), price of diesel (44 basic points) and the leading interest rate of the monetary policy (-34 basic points). It was also indicated that when comparing the inter-annual inflation forecast of the model with inflation targets established in resolution JM-211-2007, we can observe that at the end of 2008 and 2009 the inter-annual inflation rate would be over the monetary policy targets.

Following they presented the risks balance of the MMS and of the corresponding fan graphs. They indicated that according to the forecast generated in the second running of 2008, there was a 16.54% probability that the inter-annual inflation rate would be within the policy target for 2008, an 83.15% probability that the rate in question would be over the target and a 0.31% probability that the rate would be below the monetary policy target. However, according to the forecast generated in the third running in 2008, there is a 100.0% probability that the rate in question will be

over the monetary policy target. Therefore, the risk of exceeding the inflation target for the end of 2008 was increased.

On the other hand, according to the forecast generated in the second running of 2008, there is a 24.53% probability that the inter-annual inflation rate will be within the policy target for 2009, a 48.91% probability that the rate in question will be over the target and a 26.56% probability that the inflation rate will be below the target of the monetary policy. On the other hand, according to the forecast generated in the third running of 2008, there was a 20.46% probability that the inter-annual inflation rate is within the monetary policy target for December 2009, a 64.35% probability that the rate in question is over the target and a 15.19% probability that the inflation rate is below the referred monetary policy target. Therefore, the risk of exceeding the inflation rate for the end of 2009, also increased.

They indicated that the inflation forecasts mentioned are conditional to the monetary authority's leading an active monetary policy that seeks the consecution of the inflation target in the medium and long terms. In that sense, the leading interest rate, compatible with the MMS forecast generated in the third running of 2008, went from an average observed value of 6.75% in the second quarter of 2008 to 8.13% in the third quarter of 2008 and to 8.26% in the fourth quarter of the same year. Then, from the first quarter of 2009 a falling trajectory began that reached 7.63% in said quarter and 4.85% in the fourth quarter of 2009. Comparing the recently described trajectory with that which was prescribed by the second running of the MMS in 2008, the prescribed policy rates for the third running of 2008 are higher for the forecast horizon, which is consistent with the forecast of the highest inflation rates.

FOURTH: Inflation Risks Balance

Regarding Inflation Risks Balance, the following aspects were highlighted: As to the external conditions, it was indicated that the international price of oil, from August 1 to 13, 2008, on average, was at US\$118.10 per barrel, which means an decrease of US\$15.38 per barrel (11.52%) regarding the average price registered in July 2008 (US\$133.48 per barrel) and an increase of US\$26.36 per barrel (28.73%) regarding the average price registered during December 2007 (US\$91.74 per barrel). On the other hand, the price of crude oil for delivery in December 2008, according to Bloomberg, on August 13 was at US\$116.58 per barrel, lower by US\$14.94 per barrel (11.36%) regarding the price prevalent for that same position on July 17, 2008

(US\$131.52 per barrel) higher by US\$25.61 per barrel (28.15%) to the price registered for the same position on December 31, 2007 that was of US\$90.97 per barrel.

As to the behavior of the international price of corn, it was reported that it registered a decrease, when on August 13, 2008 it was US\$9.68 per quintal, lower by US\$2.20 per quintal (18.52%) to the observed at the end of July (US\$11.88 per quintal), and higher by US\$2.11 per quintal (27.87%) to the registered in December 2007 (US\$7.57 per quintal). It is worth stating that the international price of corn continues to be over the observed levels in 2007. Taking into account that the price of said product continues to be high and given its incidence on the prices of other products of the basic food basket (particularly of the tortilla products and poultry meats), its follow up in the risks balance continues to be relevant as a supply factor.

As to the international price of wheat, they mentioned that on August 13 it was at US\$10.91 per quintal, which represents an decrease of US\$0.63 per quintal (5.46%) regarding the observed level in July 2008 (US\$11.54 per quintal), and a reduction of US\$3.58 per quintal (24.71%) regarding the level registered in December 2007 (US\$14.49 per quintal). Although there was a recent moderation in the international price of wheat, it continues to be a source of inflationary pressure, due to the fact that it still remains over the levels registered in 2007.

As to internal conditions, it was indicated that the monthly inflation in July 2008 was at 1.25%, (1.63% in June 2008) higher by 0.53 percentage points to the registered in July 2007 (0.72%) and higher by 0.52 percentage points to the average of registered variations in July during the last eight years (0.73%).

The total inflationary rhythm (14.16%), the dynamic subjacent inflationary rhythm (9.43%) to July 2008, registered an increase regarding the previous month, located over the tolerance margin of the inflation target determined for 2008 (5.5% +/- 1.5 percentage point).

The econometric projections of total inflationary rhythm for December 2008 and December 2009 (11.66% and 8.54%, in that order), as well as the econometric projections of the dynamic subjacent inflationary rhythm for December 2008 and December 2009 (8.77% and 7.35%, respectively) are over the tolerance margin of the inflation target for both years. As to the results of the survey to inflation expectations of the panel of private analysts made in July, they indicate that the total inflationary rhythm for the end of 2008 and 2009 would be located at 12.42% and 9.29%, respectively. It is important to mention that although the projection made on behalf of

said panel of private analysts for December 2009 decreased, both projections are over the upper limit of the tolerance margin of the inflation target determined for each one of the referenced years.

The execution of public finance, according to preliminary numbers to July 2008, registered a surplus of Q1,364.2 million, equivalent to 0.5% of the GDP (deficit of Q973.0 million to July 2007, equivalent to 0.4% of the GDP). Notwithstanding, emphasis was made on the following aspects: a) that the surplus registered to July, is due to less public expense regarding an equal period in 2007 as well as greater levels of tax collection; b) that the deposits of the Central Government in the *Banco de Guatemala*, net disbursements of external debt were, on average, in the first quarter of 2008, around Q385.0 million below the programmed, while between April 1 and August 13 it was around Q34.4 million over the programmed on average; c) that in July 2008, the deposits of the Central Government in the Banco de Guatemala were reduced by around Q1,300.0 million, as a result of the payment of the Bono 14 [a fourteenth salary in the year.] as well as maturity of Treasury Bonds.

The behavior of the nominal exchange rate toward appreciation until August 13, 2008, is explained by an increase in the income of foreign currency due to exportations, private cash flow in the long term. Regarding the indicative variables they pointed out that the situation to date reported regarding the observed the previous month, 63.73% of variables advise a restrictive monetary policy (44.71% the previous month); 9.34% suggest a moderately restrictive monetary policy (17.10% the previous month); and 26.93% advise a relaxed monetary policy orientation (38.19% the previous month).

The primary liquidity (monetary issue and broad monetary base) to August 13, 2008, showed an average deviation of Q71.6 million, mainly as a result of the deviation of the monetary issue regarding the upper limit of the programmed runner, situation that reflects the tendency the rise in the liquid resources available of banking entities. As to the inter-annual variation of the banking credit to the private sector and of the payment means, both have been decelerating, located below the lower limit of the estimated runner.

FIFTH: Discussion.

The technical departments of the *Banco de Guatemala*, after having presented the inflation risks balance, the third running in 2008 of the Semi-structural Macroeconomic Model –MMS [For its acronym in Spanish], as well as the behavior of

the indicative variables of the monetary policy, concluded that the inflation risks balance on this occasion continues to be complex, where the factors that prevail advise restricting the monetary conditions (acceleration of the observed inflation, increased dynamic subjacent inflation, increase of the inflation forecast, as well as the expectations). Notwithstanding, it was indicated that the international prices of oil, corn and wheat recently, so they would expect to begin moderating the inflation expectations and the effects coming from external shocks.

Based on the presentation of the technical departments, the Committee deliberated on the content of the same with the purpose of presenting the main tendencies and thoughts, as well as analysis elements that could be considered in the decision regarding the level of the leading interest rate of the monetary policy programmed for August 20 of this year.

Regarding the behavior of inflation to June 2008, in the Committee reference was made at to the marked tendency to rise of the total inflationary rhythm in which the year has transpired. The members of the Committee reiterated their concern for the increase in the internal prices observed in June 2008, particularly because the increase in inter-monthly inflation for four consecutive months has been higher than 1%, the highest was 1.63% in June (representing the highest monthly variation in the last eight years), so it could be giving a propagation of goods and services prices where imported inflation should not have a significant incidence.

In the described context, the Committee stated concern for the result of the inflation to July 2008, due to the tendency to rise that has been registered. It was highlighted that the inflation to July 2008 was higher to the average of the inflations to July in the last eight years. However, the Committee considered the fact that the deceleration of the inter-monthly inflation in July regarding the three previous months was positive. Said situation, added to the recent deceleration of the international prices of oil, corn and wheat, could propitiate a moderation in the inflation expectations of the economic agents and a deceleration of the inflationary rhythm to August. They also highlighted that although total inflation rhythm to July (14.16%) registered an increase of 0.60 percentage points regarding the previous month, this was lower than the increases in the previous three months that were higher than one percentage point.

On the other hand, the dynamic subjacent inflation rhythm in July 2008 was at 9.43%, level that, given the recent behavior in the main monetary aggregates, is

mainly evidencing an increase in the inflation expectations of the economic agents. On this, the Committee declared that the monetary policy had an important role for moderating said expectations through additional measures, but it is also important to determine if there would be favorable effects in the referred expectations that would be derived from the recent contention of external shocks. They also highlighted that the inflation expectations of the panel of private analysts, according to the survey made in July, indicate that the total inflationary rhythm for the end of 2008 and 2009 would be at 12.42% and 9.29%, respectively. They highlighted that even when both projections are over the upper limit of the tolerance margin of the inflation target determined for each one of the referred years, the projection for the end of 2008 increased less than the previous months, while for 2009 it decreased regarding the previous month. Said situation could be an indicative that the inflation expectations are beginning to moderate.

When making a prospective analysis of the behavior of inflation, it was indicated that the projections of total inflationary rhythm for the end of 2008 coming from the arithmetic average of the two econometric models that have been used, point toward an inflationary rhythm of 11.66%, over the inflation target determined for the monetary authority for the present year (5.5% +/- 1.5 percentage points). For the end of 2009 they project a total inflationary rhythm of 8.54%, percentage that is also over the inflation target determined for said year. Also, according to the third running of the Semi-structural Macroeconomic Model of 2008, an inflationary rhythm for the end of 2008 of 11.90% is forecast, while for the end of 2009 the forecast is of 7.59%, both over the upper limit of the inflation targets determined for each one of those years and also supposes an active monetary policy for the rest of 2008.

Last, although the inter-annual variation as well as the payment means, like the banking credit to the private sector continues to reflect a falling tendency, the primary liquidity (monetary issue and broad monetary base) are over the upper limit of the programmed runner and went from suggesting a relaxed monetary policy to advising a restrictive one. In the Committee emphasis was made on the comparison of the second running with the third running of the Semi-structural Macroeconomic Model, evidencing an increase in the inflation forecast for 2009, so said variable went from suggesting a moderately restrictive monetary policy to advising a restrictive one.

The Committee analyzed the environmental risks in detail in which the monetary policy is currently executed. As to the associated risks in the external

environment, they highlighted that worldwide, although they are concerned with economic deceleration and how long it will last, as well as the deterioration of the international financial markets, the inflation, judged by various experts, has suggested an important threat, given its behavior toward growth in the current year.

In effect, according to interviews made to five Economy Nobel prize winners, they warned of the danger that inflation represents. In that sense, the world view continues to be complex and with a high degree of uncertainty, so the recommendations of these experts, for developing economies, in general, were centered on the following aspects: a) restrict the monetary policy; b) raise productivity; c) increase energy efficiency; and, d) diversify exportations.

In the described context, in the monetary policy environment, the central banks in general, have maintained an active monetary policy with the purpose of moderating the inflation expectations and counteracting the second round effects. In the last few weeks Chile, Mexico and Costa Rica have adjusted the interest rates of their monetary policy. In the case of Chile, the increase accumulated between December and August is of 150 basic points, while Mexico exhibits an increase of 75 basic points, however, Costa Rica between June and August adjusted 200 basic points, which gave as a result an accumulated increase of 400 basic points.

In the Committee they discussed the evolution of the international prices of oil, corn and wheat. In that regard, they highlighted the evolution of the variables mentioned that continued reflecting the persistence of inflationary risks, so its close follow up continues to be relevant in the inflation risks balance. According to reports from international experts, the referred behavior in the price of crude oil is associated to demand, supply and speculation factors observed in the market. As to demand factors, reference was made to the strengthening of the US dollar before other currencies, to the decision of the US Federal Reserve as to keeping the interest rate of the monetary policy invariable, to the expectation of a decrease in the demand of crude oil on behalf of the industrialized countries, to the decrease of the demand on behalf of China and India. As to supply factors, they mentioned the stability in the level of oil inventories in the United States of America, which are located at 296.5 million barrels, to August 8, 2008, according to information from the Department of Energy of the United States of America. As to market speculation, reference was made to the small gap between world supply and demand of oil makes any news that affects oil

production, influence the behavior of the futures price of the same, as well as its derivatives.

On the other hand, in the Committee they mentioned that the nominal exchange rate, although it has registered some volatility in the year, has been congruent with the season. They highlighted that the behavior of the nominal exchange rate toward appreciation to August 13, 2008, is explained by its seasonality, as well as by the increase in the income of foreign currency for exportations, family remittances and flow of private capital in the long term.

In the Committee they highlighted that in the scheme of explicit inflation targets, the sole fact that the inflation projections are consistently over the targets, reason to suggest an increase in the interest rate of the monetary policy. However, they highlighted that in the complex environment in which the current monetary policy performs, said decision tends to result in an integral analysis. In that context, in the Committee they declared that an integral analysis of variables and macroeconomic indicators indicated that it was important to take into account the elements that advise restricting the monetary conditions as well as those elements that advise keeping them invariable. As to factors that advise restricting, the following were mentioned: a) that inflation forecasts the econometric methods as well as those coming from the third running of the Semistructural Macroeconomic Model –MMS-, are located over the target for 2008 and 2009; b) that the inflation expectations of the Panel of Private Analysts is located over the inflation target for 2008 as well as for 2009; and, c) that the primary liquidity is found over the upper limit of the programmed runner, situation that reflects the tendency to rise of liquid resources available from banking entities.

As to factors that recommend keeping the monetary conditions invariable, the following were mentioned: a) that even when the orientation of indicative variables continues to lean toward the convenience of restricting the monetary policy, the inter-annual variation of the banking credit to the private sector and of the payment means has continued to decelerate and is located below the lower limit of the respective runners; b) that to July 2008, public finance registered a surplus of Q1,364.2 million, equivalent to 0.5% of the GDP; and, c) that the international price of oil, corn and wheat has been reduced recently, although values remain over the registered the previous year, which, on the one hand, could contribute to moderating the total inflationary rhythm in August and, on the other hand, induce a moderation in the inflation expectations.

As a result of the discussion and analysis, in the heart of the Committee there was consensus in recommending that the Monetary Board, in said opportunity, make a pause in the measures of the monetary policy, keeping the level for the leading interest rate invariable at 7.25%. Also, the Committee highlighted the importance of observing the evolution of the inflation risks balance in order to establish changes and orientation in the following month, so it is important to give close follow up to the main variables and macroeconomic indicators, internal as well as external, making it particularly relevant to monitor the inflation expectations, the inflation forecasts and the observed inflation, because if the levels continue to be high, in the opinion of the Committee, they could require gradual and successive adjustments in the following months in the leading interest rate.

SIXTH: Other Matters and Reports.

Not having other matters or reports to discuss, the session ended at sixteen hours, in the same place and on the same date indicated, the participants signed in agreement.