2001 Country Reports on Economic Policy and Trade Practices
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GUATEMALA

Key Economic Indicators

(Millions of U.S. dollars unless otherwise indicated)

	1999	2000	2001 1/
Income, Production and Employment:			
Nominal GDP 2/	18,072	18,415	18,860
Real GDP Growth (pct)	3.5	3.2	2.4
GDP by Sector (pct):			
Agriculture	23	23	22
Manufacturing	21	21	22
Services	47	47	47
Government	8	8	8
Per Capita GDP (US$)	1,635	1,636	1,630
Labor Force (000s) 3/	4,208	4,317	4,481
Unemployment Rate (pct) 4/	N/A	N/A	N/A
Money and Prices (annual percentage growth):			
Money Supply Growth (M2)	10.0	14.0	13.0
Consumer Price Inflation	5.2	5.1	10.0
Exchange Rate (Quetzal/US$ annual average)			
Financial Market Rate (2001 data is unofficial Embassy estimate)	7.40	7.77	8.1
Balance of Payments and Trade:			
Total Exports FOB 5/	2,493	2,708	2,440
Exports to United States	838	971	870
Total Imports CIF 5/	4,560	4,885	5,280
Imports from United States	1,851	1,957	2,110
Trade Balance 5/	-2,067	-2,177	-3,170
Balance with United States 5/	-1,013	-986	-1,240
External Public Debt 6/	2,600	2,600	2,700
Fiscal Deficit/GDP (pct) 6/	2.8	1.8	2.8
Current Account Deficit/GDP (pct) 6/	5.5	4.8	5.5
Debt Service Payments/GDP (pct) 6/	2.0	3.1	2.9
Gold and Foreign Exchange Reserves (Millions Net) 6/	1,100	1,800	1,900
Aid from United States	102	60.6	53.2

Aid from All Other Sources	N/A	N/A	N/A

1/ 2001 figures are all estimates based on available data in October.
2/ GDP expressed in millions of U.S. dollars.
3/ 1999 Labor Force Data: Secretariat for Economic Integration in Central America.
4/ Does not reflect estimated 40 to 50 percent underemployment.
5/ Merchandise trade data from Guatemalan customs and central bank. Trade data does not include approximately $250 million in value added by the apparel assembly industry. U.S. government data for U.S. imports from Guatemala were $2,265 million in 1999 and $2,072 million in 1998.
6/ Data from the Guatemalan government's preliminary 2001 budget projection and Guatemala's Central Bank.

1. General Policy Framework

Following the signing of the 1996 Peace Accords, which ended a 36-year armed internal conflict, Guatemala experienced a resurgence of civic participation culminating in the creation of a Fiscal Pact in 2000. The Fiscal Pact was designed to bring together various sectors to develop tax and other proposals that would help the government increase revenues from 8 percent of GDP to 12 percent, and therefore, to ensure implementation of social reforms promised in the Peace Accords. The Portillo administration did not accept some of the recommendations of the Fiscal Pact, and specifically rejected a proposed increase in the Value-Added Tax (VAT). However, in a July 2001 fiscal reform package, the government reversed its earlier position and increased the VAT from 10 percent to 12 percent.

Inconsistent policy messages and political infighting in the ruling party have created an uncertain investment climate. Increased polarization has characterized the relationship between the government and the private sector. A perception of official corruption and violent crime are two additional problems plaguing the current administration.

Guatemala's economy, the largest in Central America, is generally open, though the lack of transparency and bureaucratic complexity often make it difficult for foreigners to compete on equal footing. Real GDP growth has averaged above 3 percent and population growth about 2.9 percent annually for the last three years. Security concerns, as well as insufficient investment in education, health care, telecommunications, and transportation constrain the more rapid development of Guatemala's economy. The telecommunications sector and key elements of the electricity industry have been privatized, and the government has awarded concessions for the operation of the railroad and the postal service. Actions taken by the government during 2000 to investigate the legality of contracts signed by the previous administration cast a shadow over the investment climate, but the Government of Guatemala seems to have moved away from this policy. Guatemala has been a member of the WTO since 1995.

Agriculture and commerce are the dominant economic activities. Agriculture accounts for two thirds of exports and about 40 percent of employment, though there is much underemployment in all sectors. Activity in the agricultural sector is concentrated in production of the traditional products of coffee, sugar, and bananas**.** Dramatic declines in world prices for coffee have adversely affected the economy during 2000 and 2001. Nontraditional agricultural exports, e.g., specialty vegetables and fruits, berries, shrimp, and ornamental plants and flowers, account for an increasing share of export revenues. Other nontraditional industries that have experienced recent growth and have favorable prospects are apparel assembly for export and tourism. The textile sector expected significant increases in its exports to the United States as a result of enhanced benefits it receives under the Caribbean Basin Initiative since October 2000, but concerns that Guatemala would be disqualified over concerns for its respect for internationally recognized workers rights, along with a worldwide shakeout in the apparel industry due to slower world growth, has slowed foreign investment. Remittances from abroad are a significant source of foreign exchange.

Though tax revenues have historically been less than 8 percent of GDP, the government is committed to increasing tax revenues to 12 percent of GDP by 2002 in order to fund social and economic development projects as set forth in the Peace Accords. However, tax revenues in 2001 are expected to be around 9.7 percent of GDP and the budget for 2002 estimates tax revenues of 11 percent of GDP. Beginning in 1994, the central bank (Bank of Guatemala) was prohibited from financing the government's budget deficit, forcing the government to issue treasury bonds, most of which were short-term. In 1996, the government began issuing securities for longer terms, up to 5 and 10 years, including several dollar indexed issues placed on the international market at lower rates of interest than offered on local currency denominated bonds.

In 1999, the Guatemalan currency experienced strong downward pressure in the foreign exchange market, leading the central bank to issue short-term notes to absorb excess liquidity and reduce consumption demand. Though the central bank achieved macroeconomic stability in 2000 and the first half of 2001, having curtailed capital flight and controlled inflation, its outstanding debt increased over 300 percent and has contributed to high domestic interest rates. High commercial bank lending rates continue to discourage productive investment and retard growth. Furthermore, the high volume of open market operations implies a large future cost to the central bank and has raised the question of whether the central bank can continue to maintain a relatively permissive monetary policy in the face of continued fiscal debt. Several placements of dollar-denominated government securities were issued in 1999 to finance part of the budget deficit, but the deficit remains problematic. Despite increased reliance upon dollar-denominated instruments that carry lower coupon rates than notes denominated in local currency, debt service costs will increase in 2001 as a result of both higher debt and the depreciation of the local currency.

2. Exchange Rate Policy

Guatemala pursues a "dirty float" exchange rate regime. Guatemala's trade deficit and capital flight in 1999 put pressure on the foreign exchange market. Though Guatemala sold an additional $400 million in foreign reserves in 1999, the local currency depreciated by approximately 13 percent. By issuing short-term notes to absorb the excess liquidity, the Central

Bank stabilized the exchange rate in 2000, while simultaneously managing to raise foreign reserves to approximately $1.8 billion. Access to foreign exchange is unrestricted and there are no reports of foreign exchange shortages. The exchange rate has been mostly stable in 2001 with the Central Bank only rarely intervening in the market.

In December 2000, Congress approved the Law of Free Negotiation of Currencies, which since May 2001 permits Guatemalan banks to offer different types of dollar-denominated accounts. In fact, accounts can be held in any currency, but in practice, the dollar is the only foreign currency used with any significance. The same bill legalized the dollar and other currencies for most real transactions. In June 2001, Guatemala also officially approved usage of non-Guatemalan currencies, and the dollar has quickly assumed an important, though, not dominant, role throughout the banking sector.

3. Structural Policies

The government is committed by the Peace Accords to increasing spending on social welfare programs, infrastructure expansion, and economic development programs. Much of the financing for this additional spending will come from grants and loans provided by the international donor community, but Guatemala is under pressure to generate significant internal resources to complement foreign grants and lending to fund these expenditures. The Fiscal Pact sought to address Guatemala's need for higher internal income by designing a new tax system. Among numerous other changes, the Fiscal Pact included a proposal to raise the nation's VAT from 10 to 12 percent, which was finally passed by Congress in July 2001. Together with the increase in the VAT, Congress also approved an increase on the Agricultural and Mercantile Industries Tax and a new Fiscal Stamp on Cigarettes, Sodas, and Alcoholic Beverages. The later three taxes were expected to yield an additional US$300 million, but the Constitutional Court is hearing a challenge to the Stamp Tax, and its future is in doubt. Measures to constrain public expenditures are still being considered, but have not been implemented. Fiscal reform will be addressed in a stand-by agreement under negotiation with the International Monetary Fund (IMF) and will likely be central to future World Bank and Inter-American Development Bank programs.

The Superintendency of Tax Administration, created in 1999 to improve compliance, reported revenue increases of 3.2 percent in the first seven months of 2001, as compared to the same period in 2000. Ninety percent of the government's current income is from taxes. Indirect taxes, primarily the VAT and duties, account for 80 percent of all tax revenues. Personal income taxes account for less than two percent of all tax revenues.

4. Debt Management Policies

The projected deficit for the FY 2001 budget was originally of 1.7 percent of GDP. A combination of lower tax revenues during the first seven months of 2001 have forced the government to increase that estimate to 2.8 percent of GDP. The FY 2002 budget, though not yet approved, projects a deficit of US$457 million, about two percent of GDP. In the absence of firm policies designed to increase revenues and political commitments to fund the peace accords, many experts expect higher fiscal deficits than those forecast by the government. This deficit will be financed through a combination of internal borrowing, foreign borrowing, and loans from foreign governments and international lending agencies. Guatemala's total public debt at the end of 2000 was approximately $3.7 billion, of which $1 billion is internally held and $2.7 billion is foreign debt.

Guatemala has successfully converted some domestic debt from short term, high-interest instruments to longer-term, lower interest debt, including dollar-denominated commercial debt. The FY 2001 budget calls for appropriation of $452 million for debt service. Guatemala is current in its payments on both U.S. and other foreign debt.

5. Significant Barriers to U.S. Exports

Guatemala applies the common external tariff schedule of the Central American Common Market, which ranges from zero to fifteen percent for most agricultural and industrial goods. Exceptions include agricultural commodity imports in excess of the Tariff Rate Quotas (TRQ).

The TRQ for beef is suspended for 2001 and there is no quota assignment this year nor is there an import license required. All imported beef pays a 15 percent tariff, and the importation is open without limit. However, the Government of Guatemala reserves the right to implement the TRQ if the need arises.

This year, the importation of three products, poultry, wheat and wheat flour, was liberalized, and quota assignments are no longer needed. Furthermore, tariffs were reduced for these products. The poultry tariff was completely eliminated. Wheat and wheat flour tariffs were lowered to 2 percent and 4 percent respectively. Guatemala’s current import tariff rates for agricultural products are below WTO tariff binding rates, and the changes that occurred earlier this year have simplified entry.

Imported processed foods must be registered with the Ministry of Health by each individual importer. However, importers have the option of joining an association of importers and paying a fee for the use of the association’s registrations. Processed foods must be labeled in Spanish, however a stick-on label is permitted. While, enforcement of this requirement has been lax, compliance is increasing. Importers should be aware that the Ministry of Health requires a Free Sale Certificate for imports of all processed food products.

Phytosanitary and Zoosanitary licenses are required for all imports of plant and animal origin. Inspection of the processing plant in the country of origin, at the importers’ expense, is technically required for the license; however, implementation has been uneven, and trade disruption limited.

Imports are not generally subject to non-tariff trade barriers, though excessive bureaucracy occasionally creates delays and complicates the import process.

Some restrictions remain on foreign investment, but foreign investors generally receive national treatment. However, recent attempts by the government to renegotiate existing investment terms have negatively affected some foreign investments. Subsurface minerals, petroleum, and other resources are property of the state, and concessions are typically granted in the form of production-sharing contracts.

Surface transportation is limited to companies with at least 51 percent Guatemalan ownership. Foreign firms are barred from directly selling insurance or providing legal, accounting or other licensed professional services. This hurdle can be overcome by establishing a locally incorporated subsidiary or through a correspondent relationship with a local firm. Most of the major U.S. accounting firms, for example, are represented through one of these methods.

6. Export Subsidies Policies

Guatemala offers duty drawback and deferral programs based on Decree 65-89, Law of Free Trade Zones (FTZs), and Decree 29-89, Law of Promotion and Development of Export Activities and Drawback (Maquila). According to Ministry of Economy statistics, at the end of 2000, a total of 866 companies had qualified for maquila status and 294 that had been qualified since lost their license for various reasons, leaving 572 operating maquilas. 16 areas have qualified as Free Trade Zones and 80 companies are operating in the FTZs. Together, Maquilas and FTZs employ 148,437 workers.

7. Protection of U.S. Intellectual Property

Guatemala belongs to the World Trade Organization (WTO) and the World Intellectual Property Organization (WIPO). It is also a signatory to the Paris Convention, Berne Convention, Rome Convention, Phonograms Convention, and the Nairobi Treaty.

In August 2000, the Guatemalan Congress passed legislation that should increase the protection afforded to the holders of intellectual property rights. Effective November 1, 2000, IPR violations became criminal, as opposed to civil, offenses. In July 2001, the government named a special prosecutor for IPR. In recognition of this progress, the U.S. Trade Representative removed Guatemala from the “Special 301” Priority Watch List and placed it on the Watch List.

8. Worker Rights

The Guatemalan Constitution and the country's labor code guarantee a progressive range of internationally recognized worker rights. Exercise of these rights, however, is not effectively secured by the institutions charged with doing so. Guatemalan labor activists persistently complain that, when their labor and civil rights are violated, at times egregiously, the justice system fails to redress the injury and the perpetrators benefit from impunity. Labor Code reforms were approved by Congress in April and May 2001, implementing Guatemala's commitments to the ILO and under the 1996 Peace Accords. Guatemala's beneficiary status under the Caribbean Basin Trade Preference Act (CBTPA) and the General System of Preferences (GSP) were reviewed with a focus on labor rights in April. Guatemala was found to be eligible under both programs in May.

a. *The Right of Association* and b. *The Right to Organize and Bargain Collectively:* The Guatemalan Constitution guarantees the right of association. The constitution also specifically guarantees workers the right to unionize. Furthermore, the constitution stipulates that "what is established in treaties and conventions to which the state is party is to be considered part of the basic rights enjoyed by Guatemalan workers." Guatemala is one of only 27 countries to have ratified all of the ILO's "core" conventions, including Convention 87 (Freedom of Association and Protection of Right to Organize), Convention 98 (Right to Organize and Collective Bargaining), and, in September, Convention 182 (Worst Forms of Child Labor). Labor Code reforms approved by Congress in May implemented Guatemalan commitments under several of these conventions.

In practice, workers who exercise the right of association and try to organize unions are often fired for doing so. The law fully protects workers from retribution for forming and participating in trade union activities, but effective enforcement of these provisions is the exception rather than the rule. Less than 3 percent of the country's workforce of 4.3 million is organized. Most of these workers belong to private sector unions. Public sector employers are among the worst violators of the right of association, according to a September United States Verification Mission in Guatemala (MINUGUA) report. Under the Portillo administration, the Labor Ministry has attempted to improve the labor inspection function.

The Labor Code allows collective bargaining if at least 25 percent of a company's employees are union members. Many employers routinely seek to circumvent labor code provisions in order to resist union activities, which they view as disruptive and as a challenge to their full control of the workplace. An ineffective legal system and inadequate penalties for violations have hindered enforcement of the right to form unions and participate in trade union activities. Although the Labor Code provides that workers illegally fired for union activity should be reinstated within 24 hours, in practice employers often file a series of appeals, or simply defy judicial orders of reinstatement. Penalties for defying such orders were increased somewhat in the 1992 labor code reform and again in June 1998. Labor Code reforms enacted in May increased Labor Ministry discretion to levy fines on employers for noncompliance, and increased existing fines substantially. However, fines can be appealed in the courts, causing long delays in the administration of justice.

c. *Prohibition of Forced or Compulsory Labor:* The constitution bars forced or compulsory labor.

d. *Minimum Age for Employment of Children:* The constitution bars employment of minors under the age of 14 except as authorized by law. In addition, the constitution prohibits "employing minors in work that is incompatible with their physical ability or that puts at risk their moral development." Employment of minors requires written permission from the Ministry of Labor. There are fewer than 5,000 such permits in effect, the majority of them for work in the in-bond processing for export, or maquila, sector. The Ministry of Labor is engaged actively in reducing the number of these permits and issued less than 1,500 in 1999. However, many children under the age of 14 are employed without legal permission. They generally receive no social benefits, social insurance, vacations, or severance pay, and earn below-minimum salaries. The Labor Ministry has a program to educate minors, their parents, and employers on the rights of minors in the labor market. In 1992 the government formed the Child Worker Protection Unit within the Ministry of Labor. The Labor Ministry administers a "National Program for the Prevention and Eradication of Child Labor and Protection of Adolescent Workers" and cooperates with NGO programs to combat child labor.

e. *Acceptable Conditions of Work:* The constitution provides for a 44-hour normal workweek and the average number of hours worked is 42.5. Occupational safety and health regulations exist but often are not strictly enforced. The minimum wage is far below the level necessary to support an urban family of four, though many urban workers earn two or three times this amount; however, not all workers are paid the legally-mandated minimum wage.

f. *Rights in Sectors with U.S. Investment:* With few exceptions, international corporations adhere to the labor code and respect worker rights. There have been some credible complaints about failure to respect the right of association in the construction phase of power generating plants and in the maquila sector. U.S. companies are among the leaders in requiring that maquilas that produce garments for them adhere to codes of conduct with respect to working conditions and worker rights. Many coffee plantations also violate labor rights, particularly by often failing to pay workers the national minimum wage.

Extent of U.S. Investment in Selected Industries—U.S. Direct Investment Position Abroad on an Historical Cost Basis—2000

(Millions of U.S. dollars)

Category		Amount
Petroleum		474
Total Manufacturing		230
Food & Kindred Products	103	
Chemicals & Allied Products	61	
Primary & Fabricated Metals	2	
Industrial Machinery and Equipment	0	
Electric & Electronic Equipment	0	
Transportation Equipment	0	

Other Manufacturing	64	
Wholesale Trade		34
Banking		(D)
Finance/Insurance/Real Estate		123
Services		3
Other Industries		(D)
TOTAL ALL INDUSTRIES		904

(D) Suppressed to avoid disclosing data of individual companies.
Source: U.S. Department of Commerce, Bureau of Economic Analysis.