

Bolivia: 2001 Article IV Consultation and Request for Third Annual Arrangement Under the Poverty Reduction and Growth Facility—Staff Report; Staff Statement; Public Information Notice and Press Release on the Executive Board Discussion; and Statement by the Authorities of Bolivia

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of a combined discussion of the 2001 Article IV consultation with Bolivia and request for third annual arrangement under the Poverty Reduction and Growth Facility, the following documents have been released and are included in this package:

- staff report for the combined 2001 Article IV consultation and request for third annual arrangement under the Poverty Reduction and Growth Facility, prepared by a staff team of the IMF, following discussions that ended on **April 6, 2001** with the officials of Bolivia on economic developments and policies. **Based on information available at the time of these discussions, the staff report was completed on May 25, 2001.** 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.
- a staff statement of **June 8, 2001**, updating information on recent economic developments.
- a Public Information Notice (PIN) and a Press Release, summarizing the **views of the Executive Board as expressed during its June 8, 2001, discussion** of the staff report on issues related to the Article IV consultation and the IMF arrangement, respectively.
- a statement by the authorities of Bolivia.
- corrections to the staff report were issued after the Board discussion on June 8.

The document(s) listed below have been or will be separately released.

Enhanced Initiative for Heavily Indebted Poor Countries—Completion Point Document
Joint Staff Assessment of the Poverty Reduction Strategy Paper
Letter of Intent by the authorities of Bolivia*
Memorandum of Economic and Financial Policies by the authorities of Bolivia*
Poverty Reduction Strategy Paper
Statistical Annex
Technical Memorandum of Understanding*
*May also be included in Staff Report.

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

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BOLIVIA

**Staff Report for the 2001 Article IV Consultation and Request for Third Annual
Arrangement Under the Poverty Reduction and Growth Facility**

Prepared by the Western Hemisphere Department

(In consultation with other departments)

Approved by Claudio M. Loser and Jesús Seade

May 25, 2001

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EXECUTIVE SUMMARY

Background

- Bolivia has a long track record of substantial progress in the areas of macroeconomic stability and structural adjustment; however, poverty remains widespread. In 2001 there were delays in implementing the structural program, but important advances were achieved in the areas of tax administration and budget management.
- The economic recovery in 2000, following a sharp slowdown in 1999, was weaker than expected, owing to weak domestic demand arising mainly from the aggressive coca eradication program that substantially reduced income in the informal sector. Still, virtually all the quantitative financial targets were met during the year. There is evidence of continued economic weakness in early 2001, as well as some deterioration of bank performance indicators.
- In September 1998 Bolivia reached the completion point under the original HIPC framework and received debt relief of US\$448 million. At its decision point under the enhanced framework in February 2000, Bolivia was found eligible for additional debt relief of US\$854 million, and conditions for a floating completion point were set.

Policy discussions

- The program for 2001 is based on the macroeconomic framework in the PRSP, and is designed to support a recovery in real GDP growth to 4 percent, while containing inflation at about 4 percent. The fiscal deficit is programmed to remain at 3.7 percent of GDP. The external current account deficit is expected to remain steady at about 5½ percent of GDP, and net international reserves would be allowed to fall moderately.
- The structural program is focused on several fiscal reforms: a new tax procedures code; reform of the domestic tax agency and ongoing customs reform; furthering decentralization through municipal adjustment programs and transfer of expenditure responsibilities for education and health; improved financial management and tracking of poverty-related expenditure. Also, financial sector reforms aim to strengthen bank resolution procedures and facilitate prompt corrective action for problem banks.
- The Bolivian poverty reduction strategy will guide the macro framework for the government's economic program, expenditure priorities for public investment, and the coordination of external assistance. The Board will consider whether Bolivia has met the conditions for reaching the completion point under the enhanced HIPC framework.
- To address a weakening in the banking system, measures were introduced in May 2001, providing credits from a public second-tier bank to encourage banks to reschedule loans, and providing subordinated credits to recapitalize banks.

I. INTRODUCTION

1. A staff mission visited La Paz and Santa Cruz during November 26–December 15, 2000 and February 12–22, 2001 to conduct the Article IV consultation discussions, collect information to update the debt sustainability analysis for the HIPC Initiative, and negotiate the program for the third annual PRGF arrangement (described in the attached Memorandum of Economic and Financial Policies). Discussions were concluded in meetings at headquarters with staff and management on April 6.¹

2. **At the conclusion of the last Article IV consultation** on February 7, 2000 (EBS/99/235), Directors commended the authorities for their solid track record since 1985, but noted that improvements in poverty and social indicators had been modest. They welcomed the authorities' commitment to maintaining the public sector finances on a sound basis, but underscored that the fiscal framework should incorporate the costs of needed social outlays. Bolivia has accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Fund's Articles of Agreement. Bolivia is on the 12-month consultation cycle.

3. **The current three-year PRGF arrangement**, in an amount of SDR 100.96 million (80 percent of quota), was approved by the Executive Board on September 18, 1998. The second annual arrangement was approved by the Executive Board on February 7, 2000, but neither of the reviews was completed before the arrangement expired, owing to delays in meeting prior actions in the areas of tax administration and financial sector legislation. As a consequence of the noncompletion of the reviews, the second and third loans provided under

¹ The mission met with the ministers of Finance, Agriculture, Economic Development, Sustainable Development and Planning, Justice, Health, Education, Labor, Trade and Industry, and Indigenous Affairs; the President of the Central Bank and Superintendent of Banks; representatives of subnational governments; representatives of donor countries, the private sector, and the banking community; and members of civil society, including officials of the Catholic Church and representatives of trade unions and nongovernmental organizations. The February mission, together with World Bank staff, also held background meetings with the authorities and civil society regarding the Bolivian poverty reduction strategy paper (PRSP). Observers from the Inter-American Development Bank (IDB) and donor countries attended these meetings. The Bolivian delegation in April was led by Vice President Quiroga. The staff team consisted of Messrs. Lewis (Head) and Dunn, Ms. González (all WHD), Mr. Ilahi (PDR), and Ms. Parry (FAD). Mr. Kreis, the Fund Senior Resident Representative in La Paz and Mr. Budnevich, MAE Consultant, assisted the December mission, and Mr. Peraza, the new Fund Resident Representative, assisted the February mission. Mr. Serrano (IDA), Mmes. Rubio, and Quintero (both IDB) overlapped with the missions. Ms. Carvalho (Research Assistant-PDR) and Mr. Alfandari (IDA) helped prepare the debt sustainability analysis.

the second annual arrangement were not disbursed; the authorities are requesting that they be rephased over the period of the third annual arrangement.

4. In February 2000, the Boards of the International Development Association (IDA) and the Fund agreed that Bolivia had reached the decision point for the enhanced HIPC Initiative (IDA/R 2000–7 and EBS/00/4), and would be eligible for debt relief of US\$854 million in net present value (NPV) terms at end-1998² on its stock of public and publicly guaranteed external debt. At that time, directors set conditions for Bolivia's reaching a floating completion point under the enhanced HIPC framework. The authorities have developed a long-term strategy for poverty reduction, incorporating a macro framework that provides a basis for a PRGF-supported program. The strategy will be supported by assistance under the HIPC Initiative, and will form the basis for coordinating external assistance and setting government spending priorities. The staffs of the Fund and the Bank have prepared a completion point document for consideration by the Executive Boards of the Fund and IDA.

II. BACKGROUND AND PERFORMANCE UNDER THE PROGRAM

5. **Bolivia has a long track record of substantial progress in the areas of macroeconomic stability and structural adjustment; however, poverty remains widespread.** Through sound fiscal, monetary, and exchange rate policies and a comprehensive program of structural reforms since 1985 (including extensive privatization, financial sector liberalization, central bank independence and recapitalization, fiscal decentralization, trade liberalization, and pension reform), real GDP growth averaged 4 percent a year during the 1990s, as inflation was reduced to low single digits. Foreign direct investment rose above 10 percent of GDP during the latter part of the decade, and gross international reserves rose to 7½ months of imports of goods and services. Despite the overall good performance of the 1990s, external shocks—notably the sharp depreciation of the Brazilian *real* in early 1999, and a drop in key export prices—and the negative impact on domestic demand of the successful coca eradication program, resulted in a sharp economic slowdown in 1999. Real GDP growth fell to 0.4 percent. Although there was some reduction in poverty during the 1990s, about two-thirds of the population were below the poverty line in 1999.

6. **The program for 2000, supported by the second annual arrangement under the PRGF, was designed to encourage an economic recovery, while maintaining a sound macroeconomic framework.** Real GDP growth was projected to recover to 4 percent, while inflation was to be contained at 4–4½ percent. The deficit of the combined public sector was programmed to narrow only slightly to 3.7 percent of GDP,³ while growth rates of broad

² It was subsequently agreed by creditors that the debt relief would be evaluated in NPV terms as of February 2000, the time of the decision point.

³ Using the new HIPC accounting conventions adopted in late 2000, the fiscal deficit was programmed to widen slightly from 3.4 percent of GDP in 1999 to 3.6 percent of GDP.

money and bank credit to the private sector were expected to recover in line with nominal GDP growth. The external current account deficit was expected to widen slightly to just over 6 percent of GDP, while net international reserves were expected to fall moderately (after adjusting for the overperformance during 1999).

7. **The economic recovery in 2000 was weaker than expected, owing to sluggish growth of domestic demand.** Real GDP grew by only 2.4 percent despite strong export volume growth, as real domestic demand is estimated to have grown by only 1.6 percent (Table 1). The continued success of the government's coca eradication program and the customs reform, which reduced commercial activity based on contraband imports, lowered incomes in the informal sector. The virtual elimination of illicit coca cultivation over the last two to three years may have lowered incomes by 3 percent or more of annual GDP. Periods of severe social unrest during 2000 also hindered real GDP growth, mainly by disrupting transportation. Inflation remained subdued during 2000, rising slightly to 3.4 percent, despite pressure on domestic fuel prices in the first half of the year from higher world oil prices. In July 2000 the government brokered an agreement among private distributors for a one-year freeze of fuel prices.

8. **The government twice approved plans to reactivate the economy during 2000, partly in response to social unrest.** The first economic stimulus package, approved by congress in April, contained several specific tax breaks and emergency spending measures, including a zero duty rate on imported capital goods⁴ and a labor-intensive public works program in the main municipalities. It also included a program to encourage commercial banks to reschedule outstanding loans. The stimulus package was enhanced in November, following a second episode of unrest, mainly by broadening incentives to banks to reschedule loans and expand their lending operations. The government engaged in negotiations with various groups during the year to address their specific concerns, including land and water rights in the countryside, teachers' salaries, military actions in the coca growing regions, and a strike by the national police (rank and file officers were granted a 50 percent wage increase).

9. **Fiscal discipline was generally maintained during 2000, even though government revenue shortfalls and measures to stimulate the economy led to a modest relaxation of the program's end-year fiscal limits.** In particular, an expected increase in tax revenues failed to materialize, reflecting the weak economy, delays in the implementation of various tax and tax administration measures, and lost revenue from the tax breaks in the first stimulus package (Tables 2 and 3). Nontax revenue fell by nearly a full percentage point of GDP, owing mainly to the end of the vehicle registration program early in the year. Fuel taxes were reduced in early 2000 to mitigate the pass-through of rising world prices, generating revenue losses that were only partly offset by increased excise taxes on other items. Current

⁴ Applicable to capital goods not produced within the Andean Community. For capital goods produced within the region, the duty rate remained at 5 percent.

government expenditures, including wages, were largely held in check but pension costs proved to be higher than expected. As part of the plan to stimulate the economy, capital spending, which had been sluggish for much of the year, was accelerated in the fourth quarter to meet original program targets. Under these budget pressures, the authorities reached agreement with staff in July to permit a modest relaxation (0.3 percent of GDP) of the end-year limits on the overall balance and domestic financing of the combined public sector. The modified program was not presented to the Board, because prior actions for completing the review program were not met.

10. **All quantitative financial performance criteria and benchmarks for 2000 were met, except for the end-year financial benchmarks on the fiscal deficit and its domestic financing (Table 4).** In these latter two cases, the modified limits agreed with staff were met by a narrow margin. The target for net international reserves and the limit on net domestic assets of the central bank were met by a wide margin, mainly reflecting a substantial overperformance in 1999 that was carried over to the 2000 program.⁵

11. **Banking activity continued to contract during 2000, and there was some weakening of bank performance indicators, although banks' net external position improved sharply.** Slow economic growth contributed to a fall in both broad money and bank credit to the private sector in U.S. dollar terms⁶ (by 3 percent and 9 percent, respectively) during the year (Table 5). The fall in credit also was affected by the ongoing restructuring of the balance sheet of the country's largest bank, which was purchased by foreign investors in late 1998; more conservative lending practices encouraged by the phasing-in of stricter prudential norms, that require the categorization of new credits based on borrowers' cash flow, instead of collateral; and uncertainty created by social unrest. With the drop in lending, the share of banks' nonperforming loans doubled to 10.3 percent at end-2000, and rose further to 12.7 percent in March 2001 (Table 6). However, the net foreign asset position of the banks, including repayment of medium- and long-term external liabilities, improved by US\$365 million (11 percent of bank liabilities) during the year.

12. **In contrast to the program's projections, the external current account deficit narrowed in 2000, owing to the strong export growth.** Exports grew by 11 percent in real terms (17 percent in U.S. dollar terms), with natural gas and soybean export volumes rising by 75 percent and 24 percent, respectively. As a result, the current account deficit fell to 5.5 percent of GDP in 2000, despite unanticipated net imports of services (Table 7).⁷ Foreign

⁵ The program target for net international reserves permitted a decline of US\$85 million over the two-year period 1999–2000.

⁶ Over 90 percent of deposits and credits are denominated in U.S. dollars.

⁷ The balance of payments figures incorporate the new HIPC accounting based on the form in which debt relief is delivered. As a result, much of the HIPC relief, which was previously treated as exceptional financing, is now incorporated above the line.

direct investment fell to 8½ percent of GDP, reflecting the completion of the natural gas pipeline to Brazil, reduced privatization sales, and the continuing decline in investment commitments of capitalized enterprises.⁸ The unexpected improvement in banks' net foreign asset position, however, led to a sharp decline in the capital and financial account surplus. With a loss in net international reserves of US\$23 million, gross reserves declined to 6½ months of imports of goods and services at end-2000, but remained ample, and well above the program projection.

13. The economic slowdown appears to have persisted through the early months of 2001. Production indices for cement and electricity declined, and a localized drought in the soybean farming region damaged about 30 percent of the crop. Lower than expected revenue from taxes on imports suggests that domestic demand remains weak. Meanwhile, the 12-month inflation rate fell to 1.0 percent in April, and the 12-month growth rates of broad money and bank credit remain negative in U.S. dollar terms. Net international reserves have stabilized, following the expected unwinding of temporary factors that led to a surge in reserves in late 2000. In April, social unrest escalated again, and the government's ruling coalition continues to have difficulties pursuing its legislative agenda in congress. With national elections scheduled for June 2002, political opposition has intensified.

14. Although there were significant delays and setbacks in the execution of the structural adjustment program, some important advances were achieved, mainly in the area of tax administration and budget management (Table 8). In particular, progress was made with the institutional reforms of the customs agency and internal revenue service (SI), aimed at enhancing transparency and strengthening tax collections through the creation of autonomous, professionally staffed agencies. In April 2001, the senate approved a new tax procedures code, which is awaiting final approval by the lower chamber of congress. The tax code will strengthen the enforcement of taxes by requiring that contested tax obligations be paid before judicial review is pursued; making tax fraud a crime; and clarifying—in line with best-practice in tax systems—key issues regarding the use of sworn tax declarations and the application of the statute of limitations. In the area of budget management, the treasury began operating with a single treasury account in January 2001 and a new financial management information system (SIGMA) was implemented in all of the central government ministries. However, the tax policy reform, which was a performance criterion for end-2000, has been postponed for consideration until after the June 2002 elections and, as discussed below, congressional approval of a law to strengthen the financial system also has been delayed, because of changes in the approach taken to the introduction of limited deposit insurance.

15. While poverty incidence remains high, progress has been made in improving some social indicators in recent years. For example, in conjunction with the IDB's social

⁸ With the capitalization of public enterprises, private investors received 50 percent ownership and management control of a public enterprise, in exchange for a commitment to invest in the company. The remaining shares are held by two capitalization funds.

sector credit, nearly all targets for a selected set of social indicators developed under the original HIPC Initiative were met for 1999 and the first half of 2000 (Table 9). All spending targets for priority projects specified in the credit for the first half of 2000 were reached, and despite budgetary pressures, poverty-related expenditure as a whole increased relative to GDP in 2000 (Table 10).

III. POLICY DISCUSSIONS

16. **The Bolivian authorities have developed a comprehensive poverty reduction strategy, which provided the overall context for policy discussions with staff.** The strategy, which incorporates the main conclusions of the National Dialogue on poverty reduction held between June and August 2000 (Box 1) and was published in a PRSP in March 2001 and evaluated by Fund and Bank staffs in a joint staff assessment,⁹ aims to reduce the incidence of poverty and extreme poverty by about one-third and one-half, respectively, by 2015. With strong economic growth as a necessary condition for meeting these targets, the PRSP presents a sound macroeconomic framework that emphasizes medium- and long-term fiscal and external debt sustainability, and an extensive structural agenda. It also establishes indicators for monitoring progress with poverty reduction, and envisages oversight by civil society at the local, regional, and national levels on the use of HIPC resources, as discussed in the National Dialogue.

17. **The government's medium-term economic program in the PRSP is designed to raise output growth to 5 percent in 2003, and 5½ percent annually in 2008 and beyond, while maintaining inflation below 4 percent (Table 11).** Public and private sector investment are projected to rise gradually in relation to GDP over the medium term. With support from HIPC debt relief, public sector investment would focus on education, health, and rural development, in addition to a major expansion of the country's road system. While much of the private sector investment is expected to be directed toward the capital-intensive extractive industries (i.e., natural gas and mining), the PRSP calls for promoting investment in labor-intensive sectors (e.g., agriculture, manufacturing, and construction) through private sector participation in infrastructure investment, improved property rights and land titling, and efforts to open up foreign markets for Bolivian agricultural products and manufactures.

18. **The authorities agreed that the program for 2001 should be in line with the goals for achieving long-term fiscal and external debt sustainability but also should reflect the objectives of supporting an economic recovery and stepping-up pro-poor spending.** The program is based on real GDP growth of 4 percent, led by a further expansion of natural gas exports and a pickup in domestic demand. In particular, a substantial investment project in the mining sector, the distribution to the elderly of accumulated profits from the capitalization program, and stepped-up government spending associated with the

⁹ Issued as EBD/01/48 and Supplements 1 and 2, and EBD/01/49, respectively.

implementation of the PRSP in the second half of the year are expected to boost demand.¹⁰ The program projects a recovery in broad money and in banks' lending activity, and the external current account deficit is projected to be about unchanged in relation to GDP. Net international reserves would be allowed to decline by US\$100 million during the year, implying an increase of about US\$20 million over the last three quarters of the year.

Box 1. The National Dialogue 2000

Bolivia's second National Dialogue was held during the period June–August 2000. Through this participatory process, the civil society was engaged by the government to identify the obstacles to poverty reduction, and present proposals for the Bolivian Poverty Reduction Strategy, the *Estrategia Boliviana para la Reduccion de Pobreza* (EBRP).

The dialogue was organized through workshops starting at the municipal level, followed by meetings at the regional and national levels. In all three stages, participants included government delegates and representatives of various civil groups, such as NGOs (some of them sponsored by the Catholic Church), business sector, small producers, indigenous people, and miners. However, not all branches of society participated in these discussions. In particular, the political opposition did not attend.

The discussion focused on three agendas: social, economic and political. The Dialogue reached agreements in several areas: (i) the determination of priority policy areas (productive infrastructure, support to production, health, education, land tenure, environment, and gender and indigenous issues); (ii) the decentralized administration of the HIPC resources by municipal governments; (iii) the definition of a transparent mechanism for distributing HIPC resources to municipalities based on poverty indicators; and (iv) the need to establish social oversight and mechanisms for the monitoring of the HIPC funds.

The agreements of the National Dialogue are widely reflected throughout the EBRP. Further, the deepening of the decentralization process, the distribution mechanism for HIPC resources, and the design of social oversight mechanisms are expected to be implemented through the Law of the National Dialogue, which was before congress as of early May.

¹⁰ Disbursements of enhanced HIPC assistance during 2001 are projected to be nearly ½ percent of GDP.

A. Fiscal Policies

19. **The fiscal program for 2001 seeks to achieve a balance between the need for further fiscal consolidation over time, and the objective of avoiding a fiscal tightening during the present period of weak domestic demand.** The overall deficit of the combined public sector is programmed to remain unchanged at 3.7 percent of GDP, consistent with the macro framework in the PRSP. This deficit represents an underlying adjustment of 0.6 percent of GDP, since privatization revenue declines by 0.3 percentage point of GDP, and the change to the new accounting for HIPC relief disguises a 0.3 percentage point reduction in the deficit using the previous accounting conventions.¹¹ Revenue gains are expected to result from the impact of tax administration reforms on the efficiency of domestic tax collections, increased fuel taxes (once the current price freeze expires at midyear), and improved collections by customs as recent administrative measures take hold. The wage bill is expected to be held in line with nominal GDP growth, and a modest increase in public investment is targeted. About two-thirds of the deficit would be financed by concessional external credits, allowing for a reduction in the stock of nonconcessional debt during the year, while domestic financing would be reduced, permitting a modest decline in the borrowing from private pension funds and a settlement of arrears of the floating debt of the larger municipalities.

20. **The cost of the 1997 pension reform (4.3 percent of GDP in 2001) continues to place a heavy burden on the public sector finances,** with upward revisions stemming from the failure to close enrollment of new retirees under the old, unfunded system. To curb future costs, the authorities have committed to closing enrollment into the old pension system by end-2001.

21. **After the authorities and staff agreed on the fiscal program for 2001, a fiscal financing gap arose from a revenue shortfall in the first quarter of the year, and an agreement reached with pensioners in March 2001 that would provide for a 55 percent increase in the minimum pension, to be implemented in two steps.** The fiscal gap for the year is estimated at 1.1 percent of GDP, based on revised projections that assume a pickup in tax revenue will accompany a recovery of output and demand in the second half of the year (Box 2). Nearly half of the estimated revenue shortfall for the year took place in the first quarter, reflecting both a weaker tax base and lower efficiency than projected. To close the gap, the authorities have decided on a set of measures, consisting mainly of expenditure cuts in addition to the restraint of expenditure in the first quarter. The reductions in spending are being planned with a view to minimizing the impact on poverty-related expenditure; some impact may be unavoidable, however, in view of the large proportion of public investment that falls within the priority areas identified in the PRSP.

¹¹ Using previous accounting conventions for HIPC debt relief, and excluding the impact of enhanced HIPC assistance, the fiscal deficit would decline to 3.8 percent of GDP in 2001 from 4.1 percent of GDP in 2000.

Box 2. Bolivia: Fiscal Gap and Measures, 2001 ^{1/}

Fiscal program deficit	3.7	Measures	1.1
		Tax regularization	0.2
Fiscal gap	1.1	Spending cuts	
Lower revenues	0.6	Goods and services	0.3
Lower grants	0.1	Transfers	0.1
Pension increase	0.3	Investment	0.4

^{1/} Discrepancies between constituent figures and totals are due to rounding.

22. Some revenue gains are expected to result from a further “tax regularization,” which provides additional time for the payment of tax liabilities, but which also has elements of a tax amnesty, since interest and penalties could be reduced. Such programs can lower future tax collections owing to moral hazard, as they can weaken the discipline to pay taxes on time. The authorities have indicated that they would seek to minimize this risk by tightening up on tax enforcement procedures at the same time.

23. **The authorities’ economic program encompasses the following structural reforms in the fiscal area aimed at further enhancing transparency, strengthening tax administration, and improving the monitoring of expenditures and budget management at all levels of government:**

- **Customs reform.** Over the past year, Customs has recruited new staff through a series of hirings conducted under strict guidelines, and progress has been made toward installing modern control systems for processing taxes on imports. The reform will continue along these lines with completion of the installation of automated systems for transit and customs controls, and a system of a posteriori control of import duties. The government is committed to strengthening the Customs administration by assuring the full funding of the agency’s budget and by providing resources to double the Customs police to 100 full-time officers.
- **Reform of the internal revenue service (SI).** The important elements in the implementation of the new law on the SI are the appointment of an independent board of directors, exams for selecting professional staff on a competitive basis, and regulations aimed at the reform’s objectives for human resource management and the financial and operational autonomy of the SI. The appointment of the Board is an important next step, both because it should precede the issuance of regulations and extensive staffing changes, and for the effective implementation of the tax procedures code. Issuance of the

regulations by August 2001 is a structural benchmark. The SI is installing an automated system for filing tax returns and selecting cases for audit.

- **Tax procedures code.** As of mid-May 2001, the tax code had been approved in the first of two readings in the lower chamber of congress. To ensure early passage, the draft law has been given priority over other legislation to be considered by the chamber of deputies; if, by the end of the ordinary congress in early June, the tax code has not been finally approved, an extraordinary congress will be called in order to complete passage of the code. Full congressional approval of the tax code is a performance criterion for September 2001, and the implementing regulations are to be issued by the end of 2001.
- **Fiscal decentralization.** Congressional approval of the proposed national dialogue law will provide for a phased transfer of responsibilities for current spending on health and education from regional to municipal governments, to better coordinate needs and spending programs.
- **Municipal adjustment programs.** To address the problem of over-indebtedness in some of the major municipalities, the government has provided access to refinancing in return for commitments to improve fiscal sustainability. These agreements call for reforms to improve revenue collections and personnel reductions to reduce expenditures (Box 3).
- **Expenditure and financial management.** In 2001 the financial management information system (SIGMA) and the coverage of the single treasury account will be expanded to cover the rest of central government yielding greater expenditure control, more detailed data, and greater fiscal transparency. The government is committed to implementing SIGMA at the local government level with financing from the World Bank and the IDB.

24. **The government intends to prepare a proposal for a comprehensive tax reform, which would be ready for consideration by the next government.** Delays in proceeding with the tax reform in 2000 reflected the difficulty in establishing a consensus on its design. The proposal would be aimed at enhancing the efficiency and progressivity of the tax system, but it also would provide for a greater revenue-generating capacity. The authorities will base the proposal on previous FAD recommendations, possibly including the replacement of highly distortionary and regressive taxes with alternative revenue sources, such as a personal income tax.

Box 3. Municipal Adjustment Plans

Overindebted municipalities have begun to reach agreements with the central government on adjustment plans (PRF) that will permit a restructuring of their debts. The FPS and FNDR will require, as a condition of access to investment funds, that municipalities prepare and carry out an Institutional Reform Plan (PAI) that aims to improve the fiscal sustainability of municipalities by addressing issues in local revenue mobilization, recurrent expenditure levels, and financial management. The municipalities entering into these agreements are given access to refinancing in return for commitments to adopt fiscal policies aimed at achieving a fiscally sustainable position within five years. The PRFs also require implementation of a financial management information system (SIGMA) to improve fiscal data at the municipal level. Overindebted municipalities as of December 31, 2000 are eligible to sign PRF agreements, and 30-50 municipalities are expected to do so.

Each PRF plan sets fiscal targets for revenue, expenditure, the deficit and debt, and has incentives and penalties associated with the fulfillment of the agreed targets. The content may vary, but they tend to include the following indicators:

Financial performance targets will be based on the following indicators:

- Ratio of debt service to current income
- Ratio of present value of debt to current income
- Total income minus total expenditure and amortization
- Total income minus current expenditure and amortization
- Increase in current income

Structural indicators include:

- Tax revenue per capita
- Investment per 1000 inhabitants
- Public employees per 1000 inhabitants

Fiscal management indicators include:

- Tax evasion rates or effective tax rates
- Current expenditure
- Amount of expenditure arrears
- Debt service to current savings ratio

Possible elements of the adjustment strategy:

- Modernizing the tax and debt administration
- Improving the property tax registry
- Improving enforcement and audit
- Employment reductions
- Changes in the investment profile
- Debt refinancing plans

B. Monetary and Banking Policies

25. **Monetary policy will be guided by the inflation objective for 2001.** The central bank will manage liquidity mainly through open market operations. The monetary program assumes that the demand for money and credit will start to recover in the course of the year; also, the limits on the central bank's net domestic assets allow for a transfer of resources to the public sector second-tier banking institutions (about US\$60 million, or 0.7 percent of GDP), which will provide credit to financial institutions for new lending as well as lending to small and medium-sized enterprises, and to encourage loan rescheduling. As part of these operations, the central bank will transfer to the public sector second-tier bank, NAFIBO, the development credits and corresponding external liabilities remaining on its balance sheet, since such lending is no longer a central bank function. Currency issue is projected to grow slightly faster than nominal GDP, and in view of the ample stock of foreign reserves of the central bank, the program allows for a moderate decline in net international reserves (US\$100 million).

26. **Following a muted response to last year's measures to encourage banks' loan rescheduling and new lending, in May 2001 congress approved a new economic stimulus package with stronger incentives aimed at increasing credit growth (Box 4).** Under the latest package, NAFIBO would extend credit to banks that reschedule loans, including nonperforming loans, and it would secure funding for this program through bond sales. Staff expressed concern over the potential fiscal costs of this program, particularly to the extent that NAFIBO incurs losses that would be covered directly by the treasury. It will be important for the interest rate on NAFIBO's lending operations to fully cover the cost of its funding through the issuance of bonds. Also, staff noted that the provision of liquidity for new lending through this scheme does not seem to be needed, in view of the generally ample bank liquidity. The authorities explained that banks would retain the credit risk for the rescheduled loans, a feature of the program that would, in their view, limit the likelihood of fiscal costs.

27. **Measures to stimulate credit expansion have entailed regulatory forbearance, which may make it more difficult to detect bank weakness; early detection becomes increasingly important with the weakening of bank performance indicators.** The authorities regarded the measures taken over the last year as providing needed "breathing room" for well managed banks that have been adversely affected by a prolonged drop in profitability in the corporate sector. Staff pointed out that, as the regulatory forbearance may postpone both the detection of bank problems and the timely corrective action needed to address them, the proposed financial reforms in congress take on added importance. The authorities plan to amend the proposed law, or to resubmit a modified bill, that would postpone the introduction of an explicit ceiling on deposit insurance, while maintaining other important elements. In particular, the bill would enable the banking superintendency to more effectively utilize early warnings of bank weakness for taking timely corrective actions, and improve bank resolution procedures. Passage of a modified bill is expected by October 2001 (performance criterion for the first review of the program).

Box 4. Measures to Encourage Banks' Lending and Reprogramming in 2000-2001

First stimulus package (April 2000)

- **NAFIBO bond swap arrangement.** Banks may swap reprogrammed substandard loans (categories 2-4) to clients in the productive sector with the capacity to repay for zero-coupon nontransferable NAFIBO bonds, with a credit risk weight of 20 percent for capital adequacy requirements, compared with 100 percent for the original loan. Swaps are reversed by the amount of each loan repayment; if a repayment is late by 90 days, the swap is fully undone and the loan returns to its original classification. Repayment period of reprogrammed loans would be 5-10 years, including a grace period of up to 2 years. Total limit of program: US\$250 million.
- **Reprogramming with own resources.** Banks may reprogram any loan to clients in the productive sector with capacity to repay, including loans in default (category 5, the lowest category). Reprogrammed loans will not be subject to immediate downgrading. Total limit of program: US\$250 million.

Second stimulus package (November 2000)

- Reprogramming measures (above) are extended to clients in any sector (except consumer credits) with the capacity to repay, and the 5-year minimum repayment period is eliminated. The NAFIBO bond swap arrangement is extended to reprogramming of category 1 loans, which also had a risk weight of 100 percent.

Third stimulus package (May 2001)

- **Special Fund for Economic Reactivation (FERE).** The FERE will be financed through the emission of up to US\$250 million of bonds by NAFIBO, and will provide credits to banks that reprogram loans to clients with the capacity to repay. FERE credits to banks will have a minimum 12-year term, including a 2-year grace period; the interest rate will be established with each bank individually. Banks can receive credit from NAFIBO for 100 percent of reprogrammed loans, excluding consumer credits; and 50 percent of reprogrammed consumer credit. Except for consumer credits, reprogrammed loans will have a minimum term of 8 years; consumer credits will have a maximum term of 4 years.
- **NAFIBO bond swap arrangement.** The grace period for late debt service payments on reprogrammed loan is extended to 180 days, before the swap is undone.
- **Real estate collateral for provisioning.** Forty percent of the value of real estate collateral (up from 25 percent) can be applied to provisioning requirements on new loans.
- **Capitalization Program (PROFOP).** The PROFOP will provide one-time subordinated credits to capitalize banks, on terms to be determined. The maximum amount available will be US\$80 million, financed through the transfer to NAFIBO of the development portfolio (and corresponding liabilities) of the central bank.

28. **The weakened bank performance, evidenced by a rise in nonperforming loan ratios throughout much of the banking system, gives cause for concern but, at the same time, several developments have improved the banking system's ability to withstand stress:** the restructuring of the balance sheet of the largest bank in the system; a change in loan classification criteria that will improve the quality of bank loan portfolios; increases in provisioning requirements that are being phased in over the five years to 2004; a significant improvement in banks' net foreign asset position; and increases in bank capitalization in the latter part of the 1990s (see Figure 4). Increasing stress in the banking system has resulted from the economic slowdown in both the formal and informal sectors, the restructuring of the largest bank in the system following a change in ownership, and the adaptation to more stringent prudential regulations. The stress—unsurprising in view of the contraction of credit and lending rates that, at about 15 percent for U.S. dollar-denominated loans, are high in real terms—could increase further if the assumed economic recovery is slower or weaker than expected. These developments underline the importance of implementing without delay the financial sector reforms mentioned above, and exercising vigilance in bank supervision.

C. External and Exchange Rate Policies

29. **The external current account deficit in 2001 is projected to remain stable in relation to GDP,** with modest growth of export volumes and little change in the terms of trade (Table 12). Excluding natural gas, however, exports are projected to be stagnant in 2001. Foreign direct investment is projected to increase to 9 percent of GDP, owing mainly to a large investment project (San Cristóbal) in the mining sector. Gross official reserves would remain comfortable at just over 5½ months of imports.

30. **The authorities intend to continue with a de facto crawling peg exchange rate policy, with the aim of maintaining internal price stability and gradually improving their external competitiveness.**¹² The recent depreciation of the Brazilian *real* and continued strength of the U.S. dollar may create some temporary strain on competitiveness, particularly with regard to bilateral trade with Brazil, and the authorities will continue to monitor closely exchange rate developments. The authorities and staff agreed that the crawling peg system has served Bolivia well in helping the economy to adjust to terms of trade shocks, in the context of limited exposure to portfolio capital flows, while avoiding the volatility that could result from a freely floating exchange rate, and the adverse impact that this could have in the highly dollarized financial system. It is essential that monetary policy be consistent with this exchange rate framework.

31. **Bolivia maintains an open exchange and trade system.** Tariff rates are zero and 5 percent for capital goods and 10 percent on all other goods, and there are no major nontariff barriers. Based on the greater transparency and efficiency in customs procedures in recent

¹² The central bank manages the exchange rate in daily foreign exchange auctions; it does not pre-announce the rate of crawl.

years, arising from the ongoing reform of customs administration, Bolivia's rating on the Fund's Index of Aggregate Trade Restrictiveness has been revised to 1, the least restrictive rating.

D. Implementation of the Poverty Reduction Strategy

32. **The authorities will soon begin implementation of their comprehensive long-term strategy to reduce poverty, supported by assistance under the enhanced HIPC Initiative.** The strategy, mapped out in the PRSP that incorporates the conclusions of the National Dialogue 2000, identifies a comprehensive agenda for infrastructure projects, social expenditures, and institutional reforms aimed at reducing the incidence of poverty and extreme poverty in Bolivia by one third and one half, respectively, by 2015 (Table 13). The four main components of the strategy are to enhance employment and income opportunities for the poor; develop the productive capacities of the poor; provide greater security and protection; and increase social participation and integration. Together with these four components, the strategy incorporates three cross-sectoral issues—gender equity, interests of indigenous peoples, and the sustainable use of natural resources—and develops an institutional framework for its implementation. Upon reaching the completion point under the enhanced HIPC Initiative, the government will begin to direct the new flows of debt relief to municipalities for poverty reduction projects. As decided in the National Dialogue, this assistance will be distributed to municipalities using a formula developed during the National Dialogue that weights the allocations toward the poor.

33. **The program of social policies will be carried out in accordance with the strategy described in the PRSP.** Intermediate targets have been set for several social and economic indicators in order to evaluate the progress of the strategy in a timely manner, and provide a reference for the social monitoring mechanisms. In line with the PRSP, the public investment program will focus on roads, education (especially at the primary level), primary health care, basic sanitation (especially in rural areas), rural electrification, establishment of clear property rights for agricultural lands, and small scale irrigation.

34. **To complement the planned improvements in budget management, civil society will play an important role in monitoring the use of HIPC resources.** In conjunction with the Catholic Church and other civil groups, a network of social oversight committees will be established to monitor the use of HIPC resources and to provide feedback for setting future priorities. This network, which was discussed in the National Dialogue, will be formalized with congressional approval of the proposed National Dialogue Law. The government will issue norms that require municipalities to report on poverty-related and social-sector spending, showing separately the use of HIPC resources, as well as a breakdown between current and capital outlays.¹³ These data, which will be compiled on a quarterly basis by the

¹³ The current system and planned improvements for tracking poverty-related expenditure are described in the completion point document, EBS/01/78, Appendix I.

finance ministry's programming unit (UPF) for the 111 municipalities that report to it, will facilitate effective social oversight. In addition to the general requirement for local governments to report on poverty-related expenditure, the authorities also plan to conduct a tracking survey on a selective basis for an in-depth evaluation of the use of HIPC resources.

35. The PRSP provides a significant step toward a medium-term budget framework that will be further developed in the period ahead. It outlines poverty-related spending needs, which account for a major proportion of all public investment, and takes account of associated recurrent outlays, providing an accounting framework for ensuring that spending levels and financing needs are in line with the fiscal program. This will be expanded into a more comprehensive medium-term framework in order to improve the fiscal planning needed for the effective implementation of the antipoverty strategy. By the end of the first quarter of 2002, the ministry of finance will prepare the methodology and budget guidelines for the preparation of medium-term budget plans. For the 2003 budget, the line ministries will be required to submit three-year expenditure plans (subject to indicative ceilings prescribed by the ministry of finance) with their annual budget request. These plans would form the basis for future budget requests.

E. Other Structural Reforms

36. The authorities plan to complete by the end of 2001 the privatization program which has sharply reduced the role of public enterprises in the economy.¹⁴ Following the privatization in 1999–2000 of most of the state oil company's assets, the remaining gas networks and the LPG bottling plants are scheduled to be sold during the fourth quarter of 2001. The government also intends to offer for sale in 2001 the electricity distribution company of Tarija (SETAR), the electricity generation and distribution company of Potosí (SEPSA), and the electricity generation company of Trinidad (COSERELEC).

37. There is a need to reduce labor market rigidities through a modernization of labor legislation, but the needed consensus has not yet been achieved. Meanwhile, pilot programs to demonstrate the benefits that a modern labor law would permit are being implemented (for example, hourly work that is agreed upon by private firms and university students).

IV. MEDIUM-TERM OUTLOOK

38. The medium-term projections developed by the authorities for the PRSP are based on the faster growth that is needed to achieve significant reductions in poverty over the long term. The targeted path for real GDP growth (5–5½ percent over most of the period) is somewhat higher than the growth experienced in the 1990s, but staff agrees with the authorities that the growth targets are achievable, through increased investment, both

¹⁴ Sales by public enterprises in relation to GDP fell from over 15 percent in 1995 to less than 1 percent in 2000.

public and private, and greater efficiency of investment. However, this will require that the structural impediments to growth be addressed, including the weak public administration and related issues of governance, and labor market rigidities. Inflation is projected to remain contained at 3½–4 percent over the medium and long run, and the crawling peg exchange rate policy would be implemented over the foreseeable future. The framework is dependent upon a planned reduction of the overall deficit of the combined public sector from 3.7 percent of GDP in 2000 to 1.3 percent of GDP in 2008 and beyond. This fiscal adjustment would help to free up domestic financial resources for private investment. Reducing pressures on domestic financing will also facilitate stable monetary and exchange rate policies. Tax policy reform will be crucial for achieving the projected increase in tax revenue from 18.5 percent of GDP in 2000 to 21.8 percent of GDP in 2008, necessary to support increased public investment in the medium term.

39. **Over the medium and long term, the external current account deficit is projected to be in the range of 4½–5 percent of GDP**, as strong export growth, particularly in the hydrocarbons and mining sectors, would match growth in imports and a rising deficit on interest and dividends. This deficit would be fully covered by foreign direct investment (FDI) flows. The projected decline in FDI to 5–6 percent of GDP over the longer term assumes no major new investment projects for natural gas, despite recent large increases in proven reserves. Net international reserves are projected to decline until 2003, before achieving a steady annual accumulation, as gross reserve coverage falls to about 5 months of imports of goods and services in 2003, before leveling off.

40. **Debt relief to be provided under the enhanced HIPC Initiative would reduce Bolivia's outstanding debt by nearly 30 percent in NPV terms.** An updated debt sustainability analysis, based on end-2000 data, shows that the NPV of debt would fall to 138 percent of exports at end-2001 after enhanced HIPC assistance (Table 14), compared with the enhanced HIPC target of 150 percent of exports. Moreover, additional bilateral debt relief by Paris Club members beyond that provided under the HIPC Initiative would reduce this indicator another 24 percentage points.¹⁵ The flow of enhanced HIPC relief is projected to average about US\$100 million a year through 2005 (Table 15).

41. Given the outlook for the external sector and the authorities' commitment to maintaining prudent financial and macroeconomic policies, **Bolivia should be able to meet its obligations to the Fund in a timely manner.** Gross financing from the Fund would cover about 3 percent of Bolivia's foreign financing needs over the remainder of the arrangement. Debt service due to the Fund would constitute a small proportion of Bolivia's exports of goods and services and gross official reserves (Table 16).

¹⁵ See EBS/01/78, Table 18.

V. OTHER ISSUES

A. Data and Technical Assistance Issues

42. The timeliness and coverage of the economic database is generally adequate for monitoring purposes, but **there are long delays in the publication of the quarterly and annual national accounts, and the coverage of labor market statistics is weak. The authorities have been participating in the GDDS since September 2000.**

43. **In recent years, the Fund has provided considerable technical assistance to Bolivia**, including an MAE project funded by Switzerland for the modernization of central bank accounting and payment systems; FAD support for the reform of customs administration and the internal revenue service; and FAD advice on fiscal decentralization issues. With respect to future needs, the authorities saw the key priorities as follow-up assistance from FAD on tax and customs administration, and from STA on banking statistics.

B. Performance Criteria and Reviews

44. The third annual arrangement includes quarterly financial benchmarks through end-2001 (with the financial benchmarks for June and December being performance criteria) and indicative financial benchmarks for end-September 2001. The definitions and adjusters for the financial benchmarks and performance criteria, described in the tables attached to the Memorandum of Economic and Financial Policies, will apply to the same variables as in the first and second annual arrangements.¹⁶ The program provides for a downward adjustment in the targets for net international reserves if currency issue is lower than envisaged under the program, and an upward adjustment to the limits on domestic financing of the fiscal deficit in the event of shortfalls in external financing. Two structural performance criteria have been defined, one on passage by congress of the draft tax code (by September 2001), and one on passage of a financial sector reform by October 2001 that would strengthen the financial system. There are structural benchmarks in the area of public sector institutional reform.

45. There will be two reviews, the first to be completed by October 2001. The first of three disbursements is to be made available after approval of the arrangement, the second upon completion of the first program review and observance of performance criteria for end-June 2001 (SDR 19 million each), and a third disbursement (SDR 18.1 million) upon completion of the second review and observance of performance criteria for end-December 2001.

¹⁶ Financial benchmarks include limits on the deficit of the combined public sector with sublimits on domestic financing; limits on the net domestic assets and ceilings on the net international reserves of the central bank; and limits on the changes in nonconcessional external public debt with subceilings on borrowing of less than one year.

C. Streamlining Structural Conditionality

46. Structural conditionality in the program for 2001 is substantially more streamlined than the year before, focused primarily in the core areas of fiscal and financial sector reforms. Fiscal reforms to improve customs and domestic tax administration and financial management should improve the efficiency and equity of the tax system as well as its yield, and should serve to enhance transparency and governance. The reforms also are designed to improve the tracking of government spending at all levels of government, notably the pro-poor spending by municipalities that would be supported by HIPC assistance. A sound banking system, which is a key objective of the financial sector reforms that are planned, is crucial for good macroeconomic performance under the program. Many of the measures included in the previous PRGF-supported program will be covered under the lending programs and conditionality of the World Bank (Box 5).

D. Safeguards Assessment

47. Under its current arrangements with the Fund, Bolivia is subject to the transitional procedures governing safeguards assessments. These procedures require the Banco Central de Bolivia to demonstrate, by providing certain documentation to Fund staff, that it publishes annual financial statements that are independently audited in accordance with internationally accepted standards (the "external audit mechanism"). The Banco Central de Bolivia cooperated fully in providing Fund staff with the required documentation.

48. The staff has reviewed the documentation and noted that the Banco Central de Bolivia publishes, within three months of the financial year-end, annual financial statements that are audited by PriceWaterhouseCoopers. Based on the review, **the staff concluded that the Banco Central de Bolivia's external audit mechanism meets internationally accepted standards.**

VI. STAFF APPRAISAL

49. The Bolivian economy has grown at a moderate pace over the last decade, supported by structural reforms to improve the efficiency of the economy. However, despite improvements since 1985, progress in reducing poverty during this period has been limited. The staff welcomes the authorities' decision to give priority to poverty reduction through the adoption of a comprehensive poverty reduction strategy, which was developed through a broadly participatory process. The macro framework of the PRSP is sound, and provides a good, consistent basis for the government's annual economic programs.

50. The weakness of the economy has been greater and has lasted longer than had been anticipated at the time of the last Article IV consultation, owing to the adverse effects on the informal sector of an impressive coca eradication effort and of customs reform that has slowed contraband-based commerce; episodes of social unrest; weakness in the regional economy; and structural changes in the banking system that have exacerbated the slowdown in bank lending. The staff commends the authorities for a prudent management of many

Box 5. Bolivia—Structural Conditionality Streamlining Assessment

1. Coverage of Structural Conditionality in the Current Program

- **Fiscal sector reforms are critical for the program's success.** The reform of the Customs administration and the domestic tax agency and a new tax procedures code are expected to improve governance and increase the efficiency and yield of the tax system. Improvements in the financial management systems at all levels of government and in expenditure-tracking capabilities will enhance governance and facilitate monitoring and evaluation of the PRSP.
- **Financial sector reforms should promote the soundness of the banking system.** The proposed financial sector reforms encompass improved bank resolution procedures, and rules to allow prompt corrective actions by the banking superintendency. Approval and implementation of these reforms is needed, as these measures are central to a healthy financial system, and aim to reduce the duration and cost of bank problems.

2. Relevant Structural Conditions not Included in Current Program

- Tax policy reform and labor market reform are examples of macro-relevant measures that are important in the long run, but not crucial in the short run, and are in various stages of implementation. Tax policy reform is needed to increase the progressivity of the tax system and increase revenue-generating capacity, but it is delayed by political opposition; a tax reform proposal will be prepared. Modern labor legislation has been delayed for political reasons. Reforms permitting more flexible labor markets would help reduce unemployment and poverty over time, as noted in the PRSP.
- Some relevant structural measures are covered by World Bank loans for the education and health sectors, decentralization, and the reform of public sector institutions, including the judiciary, the National Road Service, and the Superintendency of Basic Sanitation. Completion of the privatization program is a loan condition; privatization measures were formerly structural benchmarks under the PRGF-supported program.
- Other relevant measures are supported by the IDB, including road infrastructure, public sector institutional reform, rural development, and investment in the social sectors.

3. Status of Structural Conditionality from Earlier Programs

See Table 8.

4. Structural Areas Covered by Bank Lending and Conditionality

World Bank lending and conditionality cover the following sectors and programs: education, roads, rural development, health care, integrated child development, regulatory reform, decentralization, other institutional reform in the public sector.

elements of economic policy in difficult circumstances. At the same time, the pace of structural reforms has been slow over the last one to two years, thus delaying the efficiency gains that the reforms are expected to bring. The authorities' commitment to the economic program will be measured not only by their performance under the financial program, but also by their success in implementing key fiscal and financial sector reforms.

51. The authorities' macroeconomic strategy for 2001 is appropriate. Many of the factors that led to the current slowdown are transitory, and the decision to avoid a large fiscal stimulus merits support. The planned fiscal stance reflects a balance between the need for economic recovery and higher levels of poverty-related spending, on the one hand, and further progress in ensuring fiscal and external sustainability, on the other.

52. The weakening of bank performance indicators gives cause for concerns that are, however, mitigated by developments that have improved the banking system's ability to withstand stress in the banking system that has increased since the last Article IV consultation. These include increases in capital and in loan-loss provisions, a reduction in short-term foreign debt, and a restructuring of the balance sheet of the largest bank in the system. The stress could increase further if the economic recovery is slower or weaker than expected. In the meantime, close monitoring by the supervisory authorities of the situation in the banking system is warranted. In this regard, it will be important to approve, and begin to implement, financial sector reforms now before congress, including those related to more adequate prompt corrective action for problem banks, and strengthened bank resolution procedures. The authorities' decision to postpone the introduction of an explicit limit to the guarantee of bank deposits is appropriate. The staff cautions against measures for the banking system that entail regulatory forbearance, as they may obscure the diagnosis of the soundness of a bank or its borrowers.

53. Implementation of the authorities' plans for structural reform in the fiscal area is important for improving the efficiency and equity of fiscal operations, and for meeting revenue targets, hence also for the success of the program. These include: rapid passage and implementation of the tax procedures code, the restructuring of the internal revenue service, continued progress in implementing the customs reform, and the careful monitoring of the municipal adjustment programs for overindebted municipalities.

54. Staff welcomes Bolivia's open trade and payments system, particularly the improvements in customs procedures that raised Bolivia to the top ranking in the index with respect to being free from restrictive trade policies. The staff supports the authorities' intention to continue the crawling peg exchange rate system, which has served Bolivia well, permitting adjustment to terms of trade shocks, while limiting exchange rate volatility that could be costly in the highly dollarized financial system. If a modestly faster rate of crawl of the nominal exchange rate becomes an appropriate response to changes in Bolivia's competitive position within the region, it could be accommodated without causing significant pressure on inflation.

55. The staff is of the view that the authorities' program is consistent with continued progress toward external viability, while fostering growth and advancing structural reforms. There are risks to the program in the form of a possibly slower-than-expected recovery, with its attendant fiscal consequences; pressure for further support for the banking system in the event of continued stagnation of bank lending; and uncertain prospects in the regional economy. There also are political risks, as future disruptive episodes of social unrest cannot be ruled out. However, the staff notes the authorities' record of prudent financial management and considers the risks to be of a manageable magnitude. **The staff therefore supports Bolivia's request for the third annual arrangement under the current three-year PRGF arrangement, for the extension of the commitment period through June 7, 2002, and for the rephasing of the undisbursed loans under the second annual arrangement during the period of the third annual arrangement.**

56. It is recommended that the next Article IV consultation be held on the standard 12-month cycle.

Table 1. Bolivia: Selected Economic and Financial Indicators

	Average	1998	Prel.	2000		Prog.
	1990-97		1999	Prog.	Prel.	2001
(Annual percentage change)						
Income and prices						
Real GDP	4.3	5.2	0.4	4.0	2.4	4.0
Real domestic demand	4.7	6.6	-1.8	4.4	1.6	2.5
GDP deflator	11.3	7.3	3.0	4.8	5.5	4.3
CPI inflation (period average)	11.9	7.7	2.2	4.2	4.6	3.7
CPI inflation (end-of-period)	11.1	4.4	3.1	4.0-4.5	3.4	4.0-4.5
(In percent of GDP)						
Investment and savings						
Gross domestic investment	15.9	23.1	18.9	19.7	18.8	19.5
Public	8.4	7.0	7.1	6.9	7.0	7.1
Private, including stockbuilding	7.4	16.1	11.8	12.8	11.8	12.4
Gross national savings 1/	10.3	15.3	13.0	13.6	13.3	14.0
Public	4.6	1.7	2.8	2.7	2.7	3.1
Private	5.7	13.6	10.2	11.0	10.6	10.9
Combined public sector 1/						
Nonpension balance	-2.9	-0.7	0.6	0.4	0.7	0.6
Pension-related balance	-0.7	-4.0	-4.1	-3.9	-4.4	-4.3
Overall balance	-3.6	-4.6	-3.4	-3.6	-3.7	-3.7
Foreign financing	3.4	2.7	1.9	2.2	1.9	2.5
Domestic financing	0.2	1.9	1.5	1.3	1.7	1.2
(Annual percentage change, unless otherwise stated)						
Money and credit						
Broad money (at current exchange rates)	31.3	13.7	4.2	10.6	3.4	7.7
Credit to private sector (at current exchange rates)	30.4	23.8	4.1	9.3	-2.6	7.9
Interest rates (percent, end-of-period)						
Lending rate in U.S. dollars	16.5	15.6	16.3	...	15.3	...
Yield on treasury bills in local currency	19.7	12.2	12.2	...	13.2	...
Yield on treasury bills in U.S. dollars	9.1	8.6	8.6	...	8.8	...
External sector (US\$ million) 1/ 2/						
Current account	-349	-667	-488	-522	-464	-469
(Percent of GDP)	-5.5	-7.8	-5.9	-6.1	-5.5	-5.4
Capital and financial account	354	792	515	522	425	313
<i>Of which:</i> foreign direct investment	198	955	1,014	785	731	778
Overall balance	5	125	26	0	-39	-155
Exceptional financing 3/	138	3	16	16	16	10
Financing gap	...	...	...	...	...	45
Merchandise export volume, percent change	6.3	4.1	-1.8	7.2	11.4	4.2
Merchandise import volume, percent change	9.0	16.0	-8.8	6.4	-0.1	0.0
Terms of trade, percent change (deterioration -)	-0.9	-1.6	-0.2	0.9	0.6	0.1
Gross official reserves 4/						
(Months of imports of goods and services)	5.0	7.2	7.0	6.1	6.6	5.6
(In percent of broad money)	29.8	31.3	32.5	27.7	32.2	28.5
Public sector external debt (US\$ billion) 5/ 6/	4.4	4.7	4.6	4.9	4.4	4.5
(Percent of GDP) 5/ 6/	71.2	54.7	54.9	55.7	51.8	52.2
Debt-service ratio 5/ 6/ 7/	38.0	28.6	19.0	23.6	18.4	16.7
End-of-period exchange rates						
Bolivianos/U.S. dollar	4.47	5.65	6.00	...	6.38	...
Nominal effective rate (percentage change) 8/	19.4	-0.5	1.5	...	-1.9	...
Real effective rate (percentage change) 8/	-1.8	3.8	1.4	...	-1.5	-3.0
Memorandum items						
Overall fiscal balance (in percent of GDP) 9/	-3.6	-4.7	-3.8	-3.7	-4.1	-3.8
External current account balance (in percent of GDP) 9/	-5.5	-8.0	-6.7	-6.8	-6.2	-5.9

Sources: Central Bank of Bolivia; ministry of finance; and Bank/Fund staff estimates and projections.

1/ Includes actual and anticipated assistance under the HIPC Initiative, using the new HIPC accounting conventions.

2/ For the 2001 external sector figures, enhanced HIPC assistance is presented as closing the financing gap.

3/ Includes grants for debt-reduction operations in effect prior to July 2000 and rescheduling operations under the original HIPC framework.

4/ Does not include Bolivia's capital contribution to the Latin American Reserve Fund. Import coverage for the following year.

5/ Debt and debt service reflect assistance under the HIPC Initiative, of which the original became available after September 1998.

6/ Includes obligations to the Fund and debt with public guarantee.

7/ On public sector medium- and long-term external debt (including payments to the Fund) in percent of exports of goods and services.

8/ Weights based on average trade, excluding trade related to natural gas, in 1996-97.

9/ According to previous accounting conventions.

Table 2. Bolivia: Operations of the Combined Public Sector 1/
(In percent of GDP)

	1997	1998	Prel. 1999	2000		Prog. 2001
				Prog.	Est.	
Balance excluding pensions (deficit -)	-0.8	-0.7	0.6	0.4	0.7	0.6
Current revenue	21.6	22.9	23.0	23.2	22.5	23.1
General government	20.3	22.8	22.9	22.8	22.1	22.7
Taxes	17.6	19.6	18.4	19.4	18.5	19.3
Hydrocarbons	4.4	5.4	5.2	5.3	5.0	5.5
Other	13.2	14.2	13.2	14.1	13.4	13.9
Nontax revenue	2.7	3.2	4.5	3.4	3.6	3.4
Public enterprise operating balance	0.7	-0.6	-0.3	0.2	0.0	0.1
Central bank operating balance	0.7	0.7	0.4	0.2	0.5	0.3
Current expenditure of general government	17.6	18.7	18.0	18.4	17.6	18.0
Wages	8.3	8.3	8.5	8.1	8.2	8.3
Interest 2/	2.3	2.1	2.0	2.2	2.3	2.6
Other	7.1	8.3	7.5	8.1	7.1	7.1
Official grants	1.4	1.4	1.8	2.0	2.2	2.4
Of which: HIPC assistance from grants	0.0	0.1	0.7	0.5	0.7	0.8
Capital revenue	1.0	0.7	0.8	0.5	0.6	0.3
Capital expenditure	7.2	7.0	7.1	6.9	7.0	7.1
General government	6.6	6.7	6.9	6.8	6.8	7.0
Central government	2.7	2.0	2.9	3.4	3.2	...
Local governments	3.9	4.7	3.9	3.4	3.6	...
Public enterprises	0.7	0.3	0.2	0.2	0.2	0.1
Pension-related balance (deficit -)	-2.5	-4.0	-4.1	-3.9	-4.4	-4.3
Revenue	1.0	0.0	0.0	0.0	0.0	0.0
Expenditure	3.4	4.0	4.1	3.9	4.4	4.3
Pensions	3.2	3.6	3.7	3.6	4.1	4.0
General government employer contributions	0.2	0.4	0.4	0.3	0.3	0.3
Overall balance (deficit -)	-3.3	-4.6	-3.4	-3.6	-3.7	-3.7
Financing	3.3	4.6	3.4	3.6	3.7	3.7
External 2/	2.7	2.7	1.9	2.2	1.9	2.5
Of which: HIPC assistance from refinancing	0.0	0.0	0.2	0.2	0.2	0.2
Domestic	0.5	1.9	1.5	1.3	1.7	1.2
Central bank	-0.9	-0.6	-1.4	0.1	0.4	0.1
Commercial banks	0.8	-0.8	-0.2	0.0	0.4	0.0
Pension funds	0.9	1.7	1.9	1.2	1.7	1.4
Other	-0.2	1.7	1.3	0.0	-0.7	-0.2
Memorandum items:						
Overall balance before grants (deficit -)	-4.7	-6.0	-5.3	-5.6	-5.9	-6.1
Primary deficit (-)	-1.0	-2.5	-1.5	-1.4	-1.4	-1.1
Savings	3.0	1.7	2.8	2.8	2.7	3.1
Military expenditure	2.2	2.3	1.9	...	1.9	...
Overall balance before enhanced HIPC Initiative 3/	-3.3	-4.7	-3.8	-3.7	-4.1	-3.8
Total assistance under the HIPC Initiative	0.0	0.3	1.0	0.8	0.9	1.2
Original HIPC	0.0	0.3	1.0	0.8	0.9	0.8
Enhanced HIPC	...	...	...	...	...	0.4
HIPC assistance from stock-of-debt reduction	0.0	0.2	0.1	0.1	0.1	0.2
On interest	0.0	0.0	0.1	0.1	0.1	0.1
On amortization	0.0	0.2	0.0	0.0	0.0	0.1
GDP (in billions of bolivianos)	41.6	47.0	48.6	54.2	52.5	57.0

Sources: Ministry of finance; Central Bank of Bolivia; and Fund staff estimates.

1/ This table is based on HIPC relief projections in the Poverty Reduction Strategy Paper. The program for 2001 has adjusters for HIPC relief as described in Table 1 of the MEFF. In January 1998, coverage was extended to include 65 provincial municipalities (the 10 largest cities had already been included) and the operating outlays of Fondo Nacional de Desarrollo Regional and the Vice Ministry for Public Investment. In January 1999, coverage was extended to include 111 municipalities.

2/ Reflects lower scheduled debt service, starting in 1998, owing to HIPC assistance in the form of stock-of-debt reduction.

3/ Reflects previous accounting of assistance under the original HIPC Initiative. Under this method, all relief on interest owed by the general government was subtracted from scheduled interest payments, while the remaining debt relief was treated as exceptional external financing.

Table 3. Bolivia: The Fiscal Impact of the HIPC Initiative

(In percent of GDP, unless otherwise indicated)

	1999	Prel. 2000	Projections			
			2001	2002	2003	2004
1. HIPC assistance given 1/	1.0	0.9	1.2	1.8	1.5	1.4
A. Interest due before HIPC assistance 2/	1.2	1.3	1.3	1.2	1.2	1.2
B. Interest paid before HIPC assistance 2/	1.2	1.3	1.3	1.2	1.2	1.2
C. HIPC assistance on interest (as a result of stock-of-debt operation only)	0.1	0.1	0.0	0.1	0.1	0.1
D. Interest due after HIPC assistance 2/	1.1	1.2	1.3	1.1	1.1	1.1
E. Amortization due before HIPC assistance	1.4	1.5	1.6	1.7	1.8	1.7
F. Amortization paid before HIPC assistance	1.4	1.5	1.6	1.7	1.8	1.7
G. HIPC assistance on amortization (as a result of stock-of-debt operation only)	0.0	0.0	0.2	0.4	0.5	0.4
H. Amortization due after HIPC assistance	1.3	1.4	1.4	1.3	1.3	1.3
I. HIPC assistance provided as grants (to cover debt service due)	0.7	0.7	0.8	1.0	0.8	0.8
J. HIPC assistance provided as exceptional financing (to cover debt service due)	0.2	0.2	0.1	0.2	0.2	0.1
Total HIPC assistance (C+G+I+J)	1.0	0.9	1.2	1.8	1.5	1.4
Total HIPC assistance (in millions of U.S. dollars)	84.7	79.0	104.9	159.1	144.0	142.2
Net cash flow to the budget from HIPC assistance B+F-(D+H-I-J)	1.0	0.9	1.2	1.8	1.5	1.4
2. Poverty-related government expenditure 3/						
Before enhanced HIPC relief 4/	10.6	10.9	10.7	11.0	11.1	11.4
After enhanced HIPC relief	...	...	11.2	12.2	12.2	12.4
Memorandum items:						
Other donor inflows (disbursements plus grants excl. HIPC assistance)	4.2	4.8	5.4	5.1	5.2	4.9
Total net external flows (HIPC and other donor flows less debt service due)	2.6	2.9	3.5	3.9	3.8	3.4
Total assistance under the enhanced HIPC framework	0.0	0.0	0.4	1.2	1.1	1.0
Tax revenue	18.4	18.5	19.3	19.6	19.7	20.1
Domestic debt	3.1	3.3	3.2	3.1	3.0	2.8
Overall fiscal balance after HIPC assistance	-3.4	-3.7	-3.7	-3.5	-3.2	-3.0

Sources: Ministry of finance; Central Bank of Bolivia; and Fund staff estimates and projections.

1/ Total assistance under both the original and enhanced frameworks.

2/ External interest of the non-financial public sector (excluding liabilities of capitalized enterprises).

3/ Expenditures on health, education, basic sanitation, urban and rural development.

4/ Equal to the authorities' actual and projected poverty-related expenditure less enhanced HIPC assistance (all of which is expected to be used for poverty-related expenditure).

Table 4. Bolivia: Financial Benchmarks and Performance Criteria - First and Second Annual Arrangements Under the Current PRGF 1/

	1999	2000				
	Dec.	Jan. 2/	Mar. 3/	Jun. 4/	Sep. 3/	Dec. 4/
(In millions of bolivianos)						
Deficit of the combined public sector						
Unadjusted limit	2,066	...	312	475	1,040	2,066
Adjusted limit	1,999	...	312	475	1,040	2,048
Actual	1,892	...	125	324	936	2,126
Margin	107	...	186	152	104	-78
Domestic financing of the combined public sector						
Unadjusted limit	821	...	138	-28	231	821
Adjusted limit	754	...	222	117	391	900
Actual	749	...	36	-35	325	917
Margin	5	...	186	152	66	-17
Net domestic assets of the central bank 5/						
Unadjusted limit	495	482	639	653	488	629
Adjusted limit	...	414	572	586	421	544
Actual	...	-583	-301	-326	96	-95
Margin	...	998	873	912	324	639
(In millions of U.S. dollars)						
Net international reserves of the central bank 5/						
Target	-100	-146	-185	-155	-120	-85
Adjusted target	...	-134	-195	-178	-143	-106
Actual	...	30	-32	-22	-86	19
Margin	...	164	163	156	58	124
Nonconcessional external debt 6/						
Limit	0	...	10	10	10	0
Actual	-38	...	-42	-40	-50	-29
Margin	38	...	52	50	60	29
External debt with maturities up to one year 6/						
Limit	0	...	10	10	10	0
Actual	0	...	0	0	0	0
Margin	0	...	10	10	10	0
(In millions of bolivianos)						
Memorandum items:						
Adjuster for:						
Net proceeds from sale of assets 7/						
For deficit and domestic financing of combined public sector	67	67	0	0	0	18
For NIR and net domestic assets of the central bank	...	67	67	67	67	85
Severance payments 8/	0	0	...	...	...	...
External disbursements shortfall 9/	...	...	84	145	160	97
Debt relief HIPC 7/	0	0	...	...	...	...
Shortfall in currency issue 8/	...	...	135	218	218	218

Source: Data provided by the Bolivian authorities.

1/ Program limits and targets adjustable for net proceeds from the sale of assets in excess of US\$45 million in 1999 and in 2000, for the difference between programmed cash outlays for severance payments and actual cash outlays, for any overdue obligations to foreign official creditors, for the difference between actual interest relief from HIPC over projected interest relief during 1999, and for the difference between projected cumulative currency issue and actual cumulative currency issue in 2000 up to a maximum equivalent to US\$35 million.

2/ Target evaluated at the end of January because of the expected increase in the demand for foreign currency banknotes associated with the year 2000 problem at the end of December 1999.

3/ Performance criteria.

4/ Benchmarks.

5/ Cumulative flows from January 1, 1999.

6/ Net disbursements of public and publicly guaranteed external debt.

7/ In excess of programmed amount.

8/ Less than programmed amount.

9/ Shortfall of net external disbursements in relation to programmed amounts, maximum of Bs160 million in 2000.

Table 5. Bolivia: Monetary Survey 1/

	1997	1998	1999	2000		Prel.	Prog. 2001
				Orig. Prog.	Adj. Prog.2/		
I. Central Bank							
(In percent of currency issue at beginning of period)							
Net international reserves	28.9	-53.9	10.2	4.0	-35.0	-6.0	-27.1
(Flow in millions of U.S. dollars)	102.7	-211.5	42.3	15.0	-115.8	-23.4	-100.0
Net domestic assets	-14.3	66.0	-10.2	5.7	38.8	6.2	36.6
Net credit to nonfinancial public sector	-20.1	-13.0	-28.0	3.0	3.6	8.5	1.6
Net credit to financial intermediaries	-2.3	59.0	6.4	-17.8	13.9	-20.6	10.0
<i>Of which: open market operations</i>	19.4	-3.0	-2.1	-16.2	9.8	16.0	-10.2
Medium- and long-term net foreign liabilities	2.4	27.1	8.1	12.0	20.1	8.4	20.7
(Flow in millions of U.S. dollars, increase -)	8.7	106.1	33.3	-44.8	-77.9	32.7	-76.4
Other	5.7	-7.1	3.4	8.6	1.3	9.9	4.2
Currency issue	14.6	12.1	0.0	9.7	3.8	0.2	9.4
II. Banking System							
(In percent of broad money at beginning of period)							
Net short-term foreign assets	1.1	-0.8	5.9	-0.1	-3.1	6.6	-0.7
(Flow in millions of U.S. dollars)	33.3	-29.7	221.5	-5.0	-117.1	244.4	-24.1
Net domestic assets	13.0	9.9	-6.6	4.7	2.0	-8.6	3.8
Net credit to the public sector	-0.4	-3.5	-3.5	0.3	1.0	1.7	0.2
Credit to the private sector	17.0	19.9	-1.9	3.3	-1.6	-10.7	3.3
Medium- and long-term net foreign liabilities	-2.6	0.1	0.7	0.6	3.0	3.4	0.8
(Flow in millions of U.S. dollars, increase -)	-79.0	3.0	27.1	20.4	112.3	126.1	27.4
Other	-1.0	-6.6	-1.9	0.6	-0.4	-3.0	-0.5
Broad money	14.1	9.0	-0.7	4.6	-1.1	-2.0	3.1
(12-month percentage change)							
Currency in circulation	14.4	6.4	-0.9	9.6	3.8	0.8	9.8
Broad money 3/	14.1	9.0	-0.7	4.7	-1.1	-2.0	3.1
Liabilities in bolivianos (M2)	16.9	8.0	-2.5	9.8	0.5	3.8	4.9
Foreign currency deposits 4/	13.5	8.3	-0.9	3.5	-1.4	-2.6	2.8
Credit to private sector	15.5	17.8	-1.6	2.6	-1.3	-8.8	2.9
Credit in bolivianos	39.8	29.6	-3.4	8.3	5.7	-2.3	8.1
Foreign currency credit 4/	14.7	17.3	-1.5	2.6	-1.6	-9.0	2.7
Memorandum items:							
(Average stock in percent of GDP)							
Currency issue	4.3	4.4	4.2	4.3	3.9	3.8	3.9
Broad money 3/	41.5	42.4	44.7	45.4	43.2	42.8	40.7
Credit to private sector	45.8	49.4	48.4	48.5	47.1	51.8	49.1
(In percent of total deposits for credit at current exchange rates)							
Dollarization (end-period stocks)							
Foreign currency deposits 4/	91.9	92.2	92.9	92.6	93.5	92.6	93.2
Foreign currency credit 4/	96.2	96.0	96.3	92.3	96.3	96.3	96.3
(12-month percentage change at current exchange rates)							
Broad money 3/	17.3	13.7	4.2	10.6	5.0	3.4	7.7
Credit to private sector	19.2	23.8	4.1	9.3	5.7	-2.6	7.9
(12-month percentage change in U.S. dollars at current exchange rates)							
Broad money 3/	13.4	7.9	-1.8	3.4	-1.9	-3.0	2.6
Credit to private sector	15.2	17.5	-2.0	2.1	-1.2	-8.7	2.8

Sources: Central Bank of Bolivia; and Fund staff estimates and projections.

1/ Flows in foreign currency are valued at the accounting exchange rate for the corresponding period. The banking system comprises the central banks, and the National Financial Institution of Bolivia, a state-owned second-tier bank.

2/ Original program adjusted for overperformance of the program in 1999.

3/ Includes special certificates of deposits (CDDs) issued by the central bank during the liquidation of failed banks.

4/ Includes deposits and credits in bolivianos that are indexed to the U.S. dollar.

Table 6. Bolivia: Commercial Bank Performance Indicators

(In percent)

	1997	1998	1999	2000												2001		
				Jan.	Feb.	Mar.	Apr.	May.	Jun.	Jul.	Aug.	Sep.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.
Profitability																		
<i>Ratios to total assets (period average) 1/</i>																		
Operating income	4.5	5.3	4.8	3.9	4.1	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.1	4.1	4.0	4.1	4.2	4.2
Profit before tax	0.9	1.5	1.2	0.4	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.5	0.5	0.4	0.3	0.4	0.5	0.5
<i>Ratios to equity capital (period average) 1/</i>																		
Profit before tax	13.3	20.9	13.0	4.1	6.0	6.5	6.4	6.3	6.5	6.2	6.0	5.3	4.8	4.1	3.4	3.6	5.1	4.6
Profit after tax	6.4	14.5	8.3	-0.6	1.4	1.9	1.8	1.7	1.9	1.6	1.4	0.7	0.2	-0.4	-1.1	-0.5	1.1	0.5
Asset quality																		
<i>Ratios to total loans (end-of-period)</i>																		
Past due loans up to 30 days	...	...	...	2.4	1.7	1.5	1.9	1.6	1.2	2.2	2.2	2.4	2.4	2.7	1.3	3.0	2.8	2.7
Nonperforming loans 2/	3.6	3.7	5.3	6.3	7.1	7.4	7.7	8.4	7.7	8.3	9.3	10.0	10.9	11.5	10.3	10.7	12.1	12.7
Nonperforming loans net of provisions 2/	1.6	1.1	1.6	4.9	4.9	4.7	5.2	5.4	4.2	5.3	6.2	6.6	7.2	7.7	5.2	7.2	8.4	8.7
Liquidity																		
<i>Ratios to total deposits (end-of-period)</i>																		
Total loans	110.9	119.4	112.7	110.1	109.7	109.1	108.7	108.5	109.3	108.2	106.9	106.2	106.8	105.5	102.4	101.1	99.8	98.9
Total liquid assets	33.5	25.5	29.7	28.4	27.9	28.6	28.8	27.7	25.7	26.2	24.7	23.9	23.5	23.4	27.2	24.7	25.3	26.9
Capital adequacy																		
<i>Ratio of qualifying capital to total risk-weighted assets (end-of-period)</i>																		
	10.9	11.6	12.2	12.7	12.6	12.7	12.7	12.9	13.0	13.3	13.2	13.3	13.3	...	13.5	13.5	13.7	...

Source: Superintendency of Banks; and Fund staff estimates.

1/ Averages in 2000 and 2001 are cumulative from January of each year.

2/ Adjusted to exclude the estimated share of loans overdue by less than one month, which were included in official statistics of nonperforming loans prior to January 2000.

Table 7. Bolivia: Summary Balance of Payments, 1997-2001

(In millions of U.S. dollars, unless otherwise noted)

	1997	1998	Prel. 1999	2000		Prog. 2001
				Prog.	Prel.	
Current account	-553	-667	-488	-527	-464	-469
Trade balance	-684	-879	-704	-671	-600	-554
Exports, f.o.b.	1,167	1,104	1,051	1,120	1,230	1,302
<i>Of which: gas</i>	69	57	36	90	122	212
Imports, c.i.f.	-1,851	-1,983	-1,755	-1,790	-1,830	-1,857
<i>Of which: capitalization and pipeline</i>	-349	-510	-405	-257	-243	-134
Services (net)	36	34	26	34	-24	6
Income (net)	-196	-162	-196	-260	-225	-282
<i>Of which: interest due on external public sector debt 1/</i>	-155	-144	-126	-148	-129	-131
<i>Of which: investment income (net)</i>	-56	-44	-52	-105	-80	-131
Transfers (net)	292	340	386	369	385	361
<i>Of which: original HIPC assistance from grants</i>	0	11	62	59	55	39
Capital account	656	792	515	395	425	313
Capital transfers	25	10	0	0	0	0
Direct investment (net)	876	955	1,014	785	731	778
<i>Of which: from capitalization</i>	570	638	506	322	297	168
Portfolio investment (net)	-53	-75	-61	-115	55	-135
Public sector loans	205	104	113	126	112	154
Disbursements	371	320	280	322	290	347
Amortization 1/	-166	-216	-167	-195	-178	-194
Other, including errors and omissions	-398	-202	-551	-402	-473	-483
Overall balance	103	125	26	-133	-39	-155
Exceptional financing	0	3	16	17	16	10
<i>Of which: original HIPC assistance from rescheduling</i>	0	3	16	17	16	10
Net international reserves (increase -)	-103	-128	-42	116	23	100
Financing gap 2/	...	...	...	...	...	45
Memorandum items:						
Gross reserves (end-of-period)	1,403	1,189	1,211	1,088	1,164	1,059
(In months of imports of goods and services) 3/	7.6	7.2	7.0	6.1	6.6	5.6
Total assistance under the HIPC Initiative	...	27	85	85	79	105
Original framework	...	27	85	85	78	60
<i>Of which: assistance from debt reduction</i>	...	13	7	8	7	10
Enhanced framework	...	...	...	...	1	45
<i>Of which: assistance from debt reduction</i>	...	...	...	...	1	11
(In percent)						
Export volume growth	4.3	4.1	-1.8	7.2	11.4	4.2
Import volume growth	25.5	16.0	-8.8	6.4	-0.1	0.0
Terms of trade change	2.9	-1.6	-0.2	0.9	0.6	0.1
(In percent of GDP)						
Current account	-7.0	-7.8	-5.9	-6.1	-5.5	-5.4
Current account before HIPC assistance 4/	-7.0	-8.0	-6.7	-6.8	-6.2	-5.9
Merchandise exports	14.7	13.0	12.6	12.8	14.5	15.0
Merchandise imports	23.4	23.3	21.1	20.5	21.6	21.4
<i>Of which: capitalization and pipeline</i>	4.4	6.0	4.9	3.0	2.9	1.6
Direct investment (net)	11.1	11.2	12.2	9.0	8.6	9.0
Grants and loans 5/	7.0	6.1	5.5	5.5	5.6	5.9

Sources: Central Bank of Bolivia; and Fund staff estimates and projections.

1/ Reflects lower scheduled debt service, starting in 1998, owing to original HIPC assistance in the form of stock-of-debt reduction.

2/ To be filled by debt relief under the enhanced HIPC framework.

3/ In months of imports of goods and services in the following year.

4/ Before any assistance under the HIPC Initiative.

5/ Official transfers and loans to the public sector, excluding HIPC debt relief.

Table 8. Structural Benchmarks: Status of Implementation, 2000

Performance Criteria/Benchmark	Policy Measure	Timetable for Implementation	Progress to Date	Measure Completed
<i>Public Sector Institutional Reform</i>				
Performance criterion	Submit to congress draft amendments to the tax code that will strengthen the tax authorities' ability to enforce tax laws.	March 2000	Tax code initially submitted in April 2000 but subsequently withdrawn and modified. As of end-2000, draft tax procedures had been resubmitted, and was before the Senate. Full passage to be made part of the program for 2001.	Partly
Benchmark	Submit to congress the new draft tax administration law that will restructure the Internal Revenue Service, giving it more autonomy.	April 2000	Law was approved in December 2000	Yes
Benchmark	Enactment of tax code and tax administration laws.	June 2000	Issuance of implementing regulations for the new tax procedures code and the Internal Revenue Service to be made structural benchmarks under third annual arrangement.	No
Benchmark	Reach decision on new computerized control system to be adopted by customs and begin implementation.	December 1999	Contract was signed in March 2000, full implementation expected in October 2001.	Yes
Benchmark	Issue implementing decrees on customs procedures and penalties.	February 2000	Issued in August 2000.	Yes
Benchmark	Automated international customs transit control system to be fully operational.	July 2000	The automated system has been implemented in three customs offices as a pilot program since February 2001. Full implementation is expected by end-June 2001.	Partly
Benchmark	Establishment of controls a posteriori in the Customs Administration.	September 2000	World Trade Organization will provide TA for implementation. Private consultants are designing software. Implementation expected to begin June 2001.	Partly

Table 8. Structural Benchmarks: Status of Implementation, 2000

Performance Criteria/Benchmark	Policy Measure	Timetable for Implementation	Progress to Date	Measure Completed
<i>Privatization</i>				
Prior action	Offer the state smelting company Vinto for sale.	December 1999	Implemented in December 1999.	Yes
Prior action	Complete the bidding process for the privatization of the refineries of YPFB.	November 1999	Implemented in November 1999.	Yes
Benchmark	Complete privatization of the residual assets of YPFB, including the natural gas network, jet fuel stations, and natural gas bottling plants.	June 2000	Storage facilities and jet fuel stations sold in December 2000. Sale of gas networks and bottling plants has been delayed to 2001.	Partly
Benchmark	Complete the privatization process fully, including the dairy product company Milka, the electricity companies SEPSA, SETAR, and the electricity generation of Trinidad (COSERELEC).	December 2000	Milka was privatized in December 1999. SETAR and COSERELEC to be privatized in 2001.	Partly
<i>Tax System Reform</i>				
Benchmark	Modify the simplified and integrated tax regimes (involving tax exemption of small traders and inclusion of the largest ones in the general tax regime).	December 31, 2000	Currently under revision by the Finance Ministry. Approval delayed indefinitely.	No
Benchmark	Elaborate and implement a comprehensive reform of the tax system in several steps with the objective of making the tax system more progressive and fair.	During 2000	Authorities will prepare a proposal for consideration by the next government following national elections in June 2002.	No
Performance criterion	Submit to congress the draft legislation for the reform of the tax system.	October 2000	Postponed until the next government takes office following national elections in June 2002.	No
<i>Labor Market Modernization</i>				
Benchmark	Initiate consultation on labor reform.	January 2000	Implemented February 2000.	Yes
Benchmark	Submit to congress a new draft labor legislation.	October 2000	Postponed until the next government takes office following national elections in June 2002.	No

Table 8. Structural Benchmarks: Status of Implementation, 2000

Performance Criteria/Benchmark	Policy Measure	Timetable for Implementation	Progress to Date	Measure Completed
<i>Financial Sector and Capital Markets</i>				
Performance criterion	Publication of the law establishing a comprehensive bank resolution framework, including a deposit insurance scheme.	March 2000	Stalled in congress due to concerns about the deposit insurance scheme. Congressional approval of amended bill to be a performance criterion for October 2001 under the third annual arrangement.	No
Benchmark	Issue norms for consolidated supervision of financial conglomerates, in line with the core principles established by the Basle Committee on Banking Supervision.	June 2000	Pending congressional approval of the law.	Partly
Benchmark	Issue norms on credit risk to ensure a more precise definition of risk weights for mortgages and on the strengthening of internal and external audits.	June 2000	Pending congressional approval of the law.	Partly
Benchmark	Complete and implement new regulations on securitization and develop plans for the establishment of a secondary housing mortgage market.	March 2000	General regulations on securitization were approved in April 2000.	Yes
<i>Social Reforms</i>				
Benchmark	Health: Implement the basic Health Insurance System, designed to provide a basket of basic health services free to the entire population.	October 2000	In the process of implementation. The consolidation of the basic Health Insurance System is now a strategic action in Bolivia's Poverty Reduction Strategy Paper.	Partly
Benchmark	Education: Develop a reform proposal for higher education in order to reduce the share of public resources for higher education.	September 2000	Final Document presented to the World Bank. Financing was approved.	Partly
<i>Legal and Judicial Reforms</i>				
Benchmark	Submit to congress revisions to the civil code procedures.	October 2000	Approval of the new Civil Code will make this measure obsolete. The draft will be submitted to the senate by June 2001.	No
Benchmark	Submit to congress revisions to the commercial code.	December 2000	Revisions are in progress; expected to be completed in first half of 2001.	No
<i>Roads and Transportation</i>				
Benchmark	Submit a new transport law, with corresponding regulation, to promote competition in the transport sector.	June 2000	Draft of the law will be officially presented to congress by June 2001.	No

Table 9. Bolivia: Selected Social Policy Actions and Outcome Indicators, 1996-2000

(In percent, unless otherwise indicated)

	1996	1997	1998	1999		2000			Targets Met	
				Target	Outturn	Annual Target	Jan.-June		1999	2000 Jan.-June
							Target	Outturn		
Education										
Total expenditures on primary and secondary education 1/ (in percent of GDP)	3.1	3.3	3.3	3.3	3.6	3.3	1.4	1.6	√	√
Rural coverage--males	66.0	68.0	81.0	72.0	82.7	74.0	80.0	83.0	√	√
Rural coverage--females	54.0	56.7	77.0	64.0	78.9	68.0	75.0	76.9	√	√
Number of children completing 5th grade										
In urban areas	86,000	87,000	92,000	94,000	101,200	98,000	111,400	115,100	√	√
In rural areas	60,000	63,000	68,000	70,000	70,400	75,000	81,100	85,100	√	√
Number of girls completing 5th grade										
In urban areas	41,000	43,000	46,000	47,000	50,600	47,000	53,800	57,100	√	√
In rural areas	29,000	30,000	31,000	34,000	32,600	36,000	37,500	39,500		√
Cumulative number of beneficiary schools in quality improvement programs (such as PASE, PIME, and PIE) 2/	...	...	...	96	96	250	125	154	√	√
Number of children (age 6 or under) enrolled in early childhood development programs	43,667	43,013	47,051	58,700	58,700	70,000	62,700	68,870	√	√
Health										
Share of births attended by health professionals 3/	30.0	43.8	49.0	46.0	47.0	49.0	21.0	24.0	√	√
Share of children (age 5 or under)										
Treated for										
Acute respiratory infections (IRA) 3/	25.0	69.0	69.0	69.0	75.0	69.0	32.0	42.0	√	√
Acute diarrhea (EDA) 3/	25.0	26.2	29.0	42.0	44.0	45.0	19.0	26.0	√	√
Receiving complete vaccinations 4/	78.0	86.5	80.0	82.0	92.0	85.0	37.0	39.0	√	√
In endemic areas										
Share of households protected from Chagas	8.0	13.4	16.0	17.0	19.0	22.0	7.0	7.3	√	√
Inhabitants, in areas with malaria, participating in the annual parasite index (IPA)	...	15.3	21.7	5.0	4.0	5.0	2.0	2.0		√
Rural development and poverty alleviation										
Number of new beneficiaries of basic water and sanitation projects in rural and peri-urban areas	132,000	186,052	216,662	132,000	214,577	132,000	132,000	73,404	√	
Investment in rural road improvement/rehabilitation (in millions of US dollars)	32.0	39.4	33.0	33.6	34.3	38.5	11.0	11.9	√	√
Number of hectares subject to cadastre and titling regulations during the period (in millions)	0.3	1.6	3.5	4.0	4.4	4.0	1.9	2.7	√	√

Sources: Bolivian authorities, *Economic Policy Analysis Unit* (UDAPE); and Fund staff estimates.

1/ Does not include spending in alternative education and training programs.

2/ In 1999 and 2000, the targets were modified to reflect the new units in which the implemented programs in education are measured.

3/ In the framework of the Mother and Childhood National Insurance Program (SNMN).

4/ Such as vaccinations for polio, DPT, measles, and BCG.

Table 10. Bolivia: Poverty-Related Expenditure

	1995	1996	1997	1998	1999	Prel. 2000	Prog. 2001	Proj. 2002	Proj. 2003
(In millions of bolivianos)									
Current expenditure	1,820	2,212	2,537	2,933	3,027	3,282	3,576	4,153	4,571
Health 1/	692	872	1,000	1,172	1,192	1,298	1,418	1,652	1,825
Education (excluding university level) 1/	1,128	1,340	1,537	1,752	1,828	1,975	2,149	2,491	2,735
<i>Of which: primary education wages</i>	...	906	974	1,050	1,187	...	...	...	...
Other social expenditure 2/	...	...	...	9	7	9	9	10	11
Capital expenditure	1,119	1,474	1,628	1,892	2,125	2,458	2,767	3,256	3,572
Health	126	160	174	192	241	380	428	503	553
Education	179	325	405	353	446	521	687	831	911
Basic sanitation	222	430	423	454	577	568	437	492	540
Urban development	367	310	307	350	283	309	425	464	508
Rural development	225	249	319	543	578	680	790	966	1,060
<i>Of which: rural roads</i>	58	100	123	183	266	269	275	361	399
Adjustment for revised HIPC projections 3/	...	...	...	...	...	...	57	196	186
Total poverty-related expenditure	2,939	3,686	4,165	4,825	5,152	5,740	6,400	7,605	8,329
(In percent of total expenditure)	32.9	35.5	35.6	34.7	36.5	37.8	38.3	42.5	43.6
(In percent of GDP)									
Current expenditure	5.6	5.9	6.1	6.2	6.2	6.3	6.3	6.7	6.7
Health 1/	2.1	2.3	2.4	2.5	2.5	2.5	2.5	2.7	2.7
Education (excluding university level) 1/	3.5	3.6	3.7	3.7	3.8	3.8	3.8	4.0	4.0
<i>Of which: primary education wages</i>	...	2.4	2.3	2.2	2.4	...	...	...	...
Other social expenditure 2/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Capital expenditure	3.5	3.9	3.9	4.0	4.4	4.7	4.9	5.2	5.2
Health	0.4	0.4	0.4	0.4	0.5	0.7	0.8	0.8	0.8
Education	0.6	0.9	1.0	0.8	0.9	1.0	1.2	1.3	1.3
Basic sanitation	0.7	1.1	1.0	1.0	1.2	1.1	0.8	0.8	0.8
Urban development	1.1	0.8	0.7	0.7	0.6	0.6	0.7	0.7	0.7
Rural development	0.7	0.7	0.8	1.2	1.2	1.3	1.4	1.6	1.6
<i>Of which: rural roads</i>	0.2	0.3	0.3	0.4	0.5	0.5	0.5	0.6	0.6
Adjustment for revised HIPC projections 3/	...	...	...	...	...	...	0.1	0.3	0.3
Total poverty-related expenditure	9.1	9.8	10.0	10.3	10.6	10.9	11.2	12.2	12.2
Memorandum items:									
Baseline poverty-related expenditures 4/	9.1	9.8	10.0	10.3	10.6	10.9	10.7	11.0	11.1
HIPC assistance	...	...	...	0.3	1.0	0.9	1.2	1.8	1.5
<i>Of which: under the enhanced framework</i>	...	...	...	...	...	...	0.5	1.2	1.1
Total social expenditure 5/	8.5	9.6	9.9	9.6	10.4	10.6	10.5	11.1	11.2
Current	6.9	7.2	7.4	7.4	7.8	7.8	7.8	8.2	8.2
Capital	1.6	2.4	2.4	2.1	2.6	2.8	2.7	2.9	2.9
General government expenditure (millions of bolivianos)	8,925	10,383	11,686	13,905	14,117	15,174	16,697	17,907	19,094
Total social expenditure (millions of bolivianos) 5/	2,747	3,602	4,102	4,495	5,033	5,561	6,002	6,927	7,609

Sources: Ministry of finance; ministry of education; and Bank/Fund staff.

1/ Does not include spending on health and education by the ministry of defense.

2/ Social spending by *prefecturas*.

3/ Reflects revisions to projections of enhanced HIPC assistance since the publication of the PRSP. The upward revision is expected to result in a commensurate increase in poverty-related spending.

4/ Bank/Fund staff estimated series equal to the authorities' actual and projected poverty-related expenditure less enhanced HIPC assistance.

5/ Health and education expenditures, including universities, and basic sanitation expenditures.

Table 11. Bolivia: Medium-Term Macroeconomic Framework

	Prel.		Prog.	Projections						Average
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008-15
(Annual percentage change)										
Economic growth and prices										
Real GDP at market prices	0.4	2.4	4.0	4.5	5.0	5.0	5.0	5.2	5.4	5.5
Real domestic demand 1/	-1.8	1.6	2.5	3.0	3.8	4.3	4.6	4.5	5.3	5.5
GDP deflator	3.0	5.5	4.3	3.1	3.5	3.5	3.6	3.3	3.4	3.5
CPI (period average)	2.2	4.6	3.7	3.9	3.8	3.7	3.6	3.5	3.5	3.5
CPI (end of period)	3.1	3.4	4.0	3.9	3.8	3.7	3.6	3.5	3.5	3.5
(In percent of nominal GDP)										
Gross investment										
Public investment 2/	7.1	7.0	7.1	7.3	7.4	7.7	8.0	8.2	8.3	8.3
Private investment, including stockbuilding	11.8	11.8	12.4	12.2	12.7	13.2	13.5	13.6	14.3	14.8
Savings										
Gross national savings	13.0	13.3	14.4	14.7	15.1	16.1	16.6	16.9	17.7	18.4
Public savings	2.8	2.7	3.1	3.8	4.1	4.7	5.4	5.9	6.5	7.0
Private savings	10.2	10.6	11.2	10.8	11.0	11.4	11.2	11.0	11.2	11.3
External savings	5.9	5.5	5.1	4.9	4.9	4.8	4.9	4.9	4.9	4.8
Consolidated public sector										
Non-pension balance	0.6	0.7	0.6	1.0	1.1	1.2	1.4	1.5	1.8	1.8
Pension-related balance	-4.1	-4.4	-4.3	-4.5	-4.3	-4.2	-4.0	-3.7	-3.7	-3.1
Overall balance	-3.4	-3.7	-3.7	-3.5	-3.2	-3.0	-2.6	-2.2	-1.8	-1.3
Net domestic financing	1.5	1.7	1.2	1.0	0.5	0.3	0.2	0.1	0.0	-0.3
Net external financing	1.9	1.9	2.5	2.5	2.7	2.7	2.5	2.2	1.8	1.6
External sector										
Current account balance	-5.9	-5.5	-5.1	-4.9	-4.9	-4.8	-4.9	-4.9	-4.9	-4.8
Net foreign direct investment	12.2	8.6	9.0	8.3	6.8	6.4	5.9	5.9	5.9	5.3
Memorandum items:										
Nominal GDP (millions of US dollars)	8,326	8,457	8,660	9,006	9,519	10,097	10,777	11,560	12,470	...

Sources: Bolivian Central Bank, Bolivia's Poverty Reduction Strategy Paper (EBRP); and Fund staff estimates and projections.

1/ Based on balance of payments figures from the Central Bank of Bolivia.

2/ Based on information from the ministry of finance.

Table 12. Bolivia: Medium-Term Balance of Payments, 1999-2007

(In millions of U.S. dollars, unless otherwise noted)

	Prel. 1999	Est. 2000	Prog. 2001	Projections					
				2002	2003	2004	2005	2006	2007
Current account	-488	-464	-439	-439	-466	-484	-523	-562	-614
Trade balance	-704	-600	-554	-540	-501	-503	-507	-505	-555
Exports, f.o.b.	1,051	1,230	1,302	1,463	1,664	1,826	1,996	2,206	2,358
<i>Of which:</i> gas	36	122	212	291	346	384	427	491	506
Imports, c.i.f.	-1,755	-1,830	-1,857	-2,003	-2,165	-2,329	-2,504	-2,712	-2,913
<i>Of which:</i> capitalization and pipeline	-405	-243	-134	-94	-64	-8	0	0	0
Services (net)	26	-24	6	10	14	21	29	35	42
Income (net)	-196	-225	-285	-305	-330	-359	-391	-436	-473
<i>Of which:</i> interest due on external public sector debt	-126	-129	-134	-122	-120	-121	-125	-134	-142
<i>Of which:</i> investment income (net)	-52	-80	-131	-153	-176	-197	-219	-244	-268
Transfers (net)	386	385	394	396	351	357	347	344	372
<i>Of which:</i> HIPC assistance from grants	62	55	72	91	75	79	73	61	54
Capital and financial account	515	425	327	439	584	619	672	698	758
Direct investment (net)	1,014	731	778	748	648	648	640	677	735
<i>Of which:</i> from capitalization	506	297	168	118	80	10	0	0	0
Portfolio investment (net)	-61	55	-135	-135	-135	-150	-150	-150	-150
Public sector loans	113	112	167	175	228	241	245	233	218
Disbursements	280	290	347	360	411	412	404	395	383
Amortization 1/	-167	-178	-180	-185	-182	-171	-159	-162	-165
Other, including errors and omissions	-551	-473	-483	-348	-156	-120	-62	-61	-45
Overall balance	26	-39	-112	1	118	134	150	136	144
Exceptional financing	16	16	12	20	18	14	10	7	7
<i>Of which:</i> HIPC assistance from refinancing	16	16	12	20	18	14	10	7	7
Net international reserves (increase -)	-42	23	100	-20	-135	-149	-159	-143	-151
Memorandum items:									
Gross reserves (end-of-period)	1,211	1,164	1,059	1,053	1,135	1,219	1,345	1,458	1,575
(In months of imports of goods and services) 2/	7.0	6.6	5.6	5.2	5.2	5.3	5.4	5.5	5.5
Total assistance under the HIPC Initiative	85	79	105	159	144	142	130	118	109
Original framework	85	78	60	51	40	36	30	26	25
<i>Of which:</i> assistance from debt reduction	7	7	10	10	10	10	10	10	10
Enhanced framework	...	...	45	108	104	106	100	92	84
<i>Of which:</i> assistance from debt reduction	...	...	11	38	41	38	37	40	38
	(In percent)								
Export volume growth	-1.8	11.4	4.2	12.6	12.1	7.3	7.3	8.5	4.9
Import volume growth	-8.8	-0.1	0.0	5.8	5.3	5.2	5.5	6.3	5.4
Terms of trade change	-0.2	0.6	0.1	-2.2	-1.1	0.0	0.0	0.0	0.0
	(In percent of GDP)								
Current account	-5.9	-5.5	-5.1	-4.9	-4.9	-4.8	-4.9	-4.9	-4.9
Current account excluding HIPC assistance 3/	-6.7	-6.2	-5.9	-6.0	-5.8	-5.7	-5.6	-5.4	-5.4
Merchandise exports	12.6	14.5	15.0	16.2	17.5	18.1	18.5	19.1	18.9
Merchandise imports	21.1	21.6	21.4	22.2	22.7	23.1	23.2	23.5	23.4
<i>Of which:</i> capitalization and pipeline	4.9	2.9	1.6	1.0	0.7	0.1	0.0	0.0	0.0
Direct investment (net)	12.2	8.6	9.0	8.3	6.8	6.4	5.9	5.9	5.9
Grants and loans 4/	5.5	5.6	5.9	5.7	5.6	5.2	4.7	4.3	4.0

Sources: Central Bank of Bolivia; and Fund staff estimates and projections.

1/ Reflects lower scheduled debt service, starting in 1998, owing to HIPC assistance in the form of stock-of-debt reduction.

2/ In months of imports of goods and services in the following year.

3/ Previously, assistance under the HIPC Initiative was treated as exceptional financing.

4/ Official transfers and loans to public sector, excluding HIPC debt relief.

Table 13. Bolivia: Poverty and Social Indicators

	1990	1994	1996	1997	1998	1999	Prel.	Targets (PRSP)		
							2000	2005	2010	2015
Poverty										
GDP growth per capita	2.2	2.2	2.0	2.5	2.8	-1.8	0.1	2.8	3.5	3.6
Poverty incidence (income based, in percent) 1/	63.2	...	62.7	62.4	55.8	47.9	40.6
National	63.2	...	62.7	62.4	55.8	47.9	40.6
Urban	54.3	...	51.5	50.4	45.5	41.0	37.0
Rural	77.3	...	81.6	79.3	68.9	59.9	52.0
Extreme poverty (national)	37.9	...	36.5	36.2	29.7	22.8	17.3
Health										
Life expectancy at birth (number of years) 2/	58.3	59.3	60.4	61.4	61.9	62.1	62.7	65.1	67.1	68.9
Infant mortality rate (per 1000 live births)	...	75.0	...	...	67.0	...	57.4	50.5	44.4	39.5
Maternal mortality rate (per 100,000 live births)	...	390	...	...	...	...	374	304	246	200
Childbirths handled institutionally (in percent)	32.6	39.3	42.7	45.2	49.0	65.0	...	...
Pregnant women with prenatal checkups (in percent)	19.3	23.9	26.4	30.1	34.0	49.0	...	...
Residential infestation by Chagas disease (in percent)	60.0	51.4	23.6	10.9	5.0
Education										
Percentage of population with 8 or more years of schooling	50.7	51.6	56.3	61.4	67.0
Academic lag 3/	44.0	42.8	37.7	35.7	30.8
Continued school attendance in first 4 years of primary school	64.6	69.9	80.0	84.9	90.2
National	64.6	69.9	80.0	84.9	90.2
Urban	67.4	73.3	83.4	87.5	91.9
Rural	61.8	66.7	76.9	82.5	88.5
Students at risk in language	23.4	13.4	8.4	...
Students at risk in mathematics	27.6	19.6	15.6	...
Basic sanitation										
Households with piped water (in percent)	70.0	71.1	74.7	...	...	...	...	...
Households with basic sanitation (in percent)	57.5	59.2	64.8	...	...	...	...	...
Households with electricity (in percent)	65.7	67.3	71.3	...	...	...	...	...

Source: Bolivian Central Bank, Bolivia's Poverty Reduction Strategy Paper (EBRP), National Statistical Institute & Poverty Diagnostic (World Bank, 2000)

1/ Poverty indicators in 1997 were calculated based on income. This limits their comparability to the figures in 1999, which were calculated with information of the survey on household consumption.

2/ In 1996, the figure corresponds to that observed in 1995.

3/ Percent of students with age above the minimum required for their school year.

Table 14. Bolivia: Indicators of Medium- and Long-Term External Public and Publicly Guaranteed Debt and Debt Service, 1999-2007 1/

	Prel.	Est.	Prog.	Projections					
	1999	2000	2001	2002	2003	2004	2005	2006	2007
(In millions of U.S. dollars)									
Debt outstanding									
Nominal (after HIPC assistance)	4,292	4,447	3,894	4,084	4,300	4,519	4,741	4,939	5,123
<i>Of which: publicly guaranteed</i>	280	261	245	226	211	199	190	184	178
NPV before HIPC assistance	3,272	3,342	3,399	3,419	3,461	3,543	3,669	3,792	3,930
NPV after HIPC assistance	2,635	2,747	1,995	2,102	2,221	2,384	2,583	2,772	2,970
(In percent of exports of goods and services)									
Debt outstanding 2/									
Nominal (after HIPC assistance)	315.6	323.9	270.0	257.9	245.9	233.6	223.2	213.1	204.3
<i>Of which: publicly guaranteed</i>	20.6	19.0	17.0	14.2	12.1	10.3	9.0	7.9	7.1
NPV before HIPC assistance	240.6	243.4	235.7	215.9	197.9	183.2	172.7	163.6	156.7
NPV after HIPC assistance	193.8	200.1	138.3	132.7	127.0	123.2	121.6	119.6	118.4
Debt service due before HIPC assistance 3/	25.5	23.8	23.8	22.3	19.8	17.8	15.9	15.3	14.6
<i>Of which: multilateral creditors</i>	13.2	11.9	17.8	17.2	15.0	13.5	12.0	11.4	10.8
<i>Of which: publicly guaranteed</i>	2.1	1.8	1.6	1.3	1.1	0.9	0.8	0.7	0.7
Debt service due after HIPC assistance 3/	19.0	18.4	16.7	13.0	12.2	11.0	10.2	10.5	10.5
(In percent of GDP)									
Debt outstanding									
Nominal (after HIPC assistance)	51.5	52.6	45.0	45.3	45.2	44.8	44.0	42.7	41.1
<i>Of which: publicly guaranteed</i>	3.4	3.1	2.8	2.5	2.2	2.0	1.8	1.6	1.4
NPV before HIPC assistance	39.3	39.5	39.3	38.0	36.4	35.1	34.0	32.8	31.5
NPV after HIPC assistance	31.6	32.5	23.0	23.3	23.3	23.6	24.0	24.0	23.8
Debt service due before HIPC assistance	4.0	4.1	4.3	4.3	4.0	3.7	3.4	3.3	3.2
<i>Of which: multilateral creditors</i>	2.1	2.0	3.2	3.3	3.1	2.8	2.6	2.5	2.3
<i>Of which: publicly guaranteed</i>	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.1
Debt service due after HIPC assistance	3.0	3.2	3.0	2.5	2.5	2.3	2.2	2.3	2.3
(In millions of U.S. dollars)									
Memorandum items:									
Exports of goods and services									
Current year	1,310	1,453	1,563	1,735	1,947	2,122	2,304	2,527	2,693
Three-year moving average	1,360	1,373	1,442	1,584	1,748	1,935	2,124	2,318	2,508
GDP	8,326	8,457	8,660	9,006	9,519	10,097	10,777	11,560	12,470

Sources: Central Bank of Bolivia; and Fund staff estimates and projections.

1/ Figures for 1999-2000 on debt stocks after HIPC assistance reflect assistance under the original HIPC framework only. Beginning in 2001, figures also incorporate the entire amount of the assistance under the enhanced framework.

2/ In percent of three-year historical average exports of goods and services.

3/ In percent of current year exports of goods and services.

Table 15. Bolivia: Scheduled Debt Service on Medium- and Long-Term External Public and Publicly-Guaranteed Debt, 1999-2007

(In millions of U.S. dollars)

	1999	Prel.	Prog.	Projections					
		2000	2001	2002	2003	2004	2005	2006	2007
Debt service due 1/	334.0	345.9	365.4	383.8	382.2	375.6	364.7	383.7	391.3
Principal	201.8	210.1	227.2	250.9	253.1	246.6	232.4	244.3	245.1
Multilateral	173.5	172.5	184.9	207.5	204.7	200.3	186.7	193.2	191.1
IMF	33.4	29.6	29.9	27.6	27.7	34.7	32.2	37.5	35.8
World Bank	18.9	19.9	12.7	14.5	15.9	17.5	18.9	21.3	23.1
IDB	63.4	64.4	80.2	89.1	88.4	87.9	81.5	83.2	75.7
CAF	44.7	45.8	48.2	63.1	60.8	49.4	45.0	43.8	47.8
Other	13.1	12.8	13.9	13.1	12.0	10.8	9.1	7.5	8.7
Official bilateral	21.8	28.5	35.6	38.2	43.4	41.8	42.6	46.4	47.3
Paris Club	18.8	25.2	31.2	33.8	37.8	38.6	38.9	42.3	41.8
Non-Paris Club	3.0	3.3	4.4	4.4	5.7	3.2	3.4	2.7	2.2
Unspecified 2/	0.0	0.0	0.0	0.0	0.0	0.0	0.3	1.4	3.3
Commercial	6.5	9.1	6.7	5.3	5.0	4.6	3.1	4.7	6.6
Interest	132.2	135.8	138.2	132.9	129.1	129.0	132.3	139.4	146.2
Multilateral	92.4	90.6	93.2	90.6	87.1	86.4	89.0	95.0	100.6
IMF	1.2	1.2	1.3	1.3	1.1	1.0	0.8	0.7	0.5
World Bank	12.5	10.9	9.3	10.9	13.1	16.6	21.3	27.3	33.7
IDB	57.4	54.1	52.1	50.1	48.4	46.3	44.4	44.2	43.0
CAF	16.4	19.7	26.3	24.7	21.0	19.2	19.1	19.3	19.6
Other	4.9	4.7	4.1	3.7	3.5	3.3	3.4	3.6	3.9
Official bilateral	37.5	43.2	43.5	41.2	41.0	41.4	41.9	42.4	43.1
Paris Club	36.9	42.7	39.8	38.9	37.9	37.0	35.8	34.6	33.5
Non-Paris Club	0.6	0.5	3.4	1.4	1.2	1.1	1.1	1.1	1.1
Unspecified 2/	0.0	0.0	0.3	0.9	1.8	3.3	4.9	6.6	8.4
Commercial	2.3	2.0	1.5	1.2	1.1	1.1	1.4	2.0	2.5
Memorandum items:									
Total HIPC assistance	84.7	79.1	104.9	159.1	144.0	142.2	129.9	118.2	108.7
Original framework	84.7	78.4	59.6	51.0	40.0	36.2	30.2	26.3	25.0
On interest	46.9	39.3	34.0	32.6	28.5	26.0	23.3	21.5	20.1
On principal	37.8	39.2	25.6	18.4	11.5	10.1	6.9	4.7	4.9
Enhanced framework	...	0.7	45.3	108.1	104.0	106.0	99.8	92.0	83.7
On interest	...	0.7	6.7	20.2	14.1	12.0	10.4	8.4	7.1
On principal	...	...	38.5	87.9	90.0	94.0	89.4	83.5	76.6

Sources: Central Bank of Bolivia; and Fund staff estimates and projections.

1/ After the full implementation of traditional debt relief and before debt relief provided under the HIPC Initiative.

2/ After 2001, reflects debt service on new borrowing from bilateral lenders.

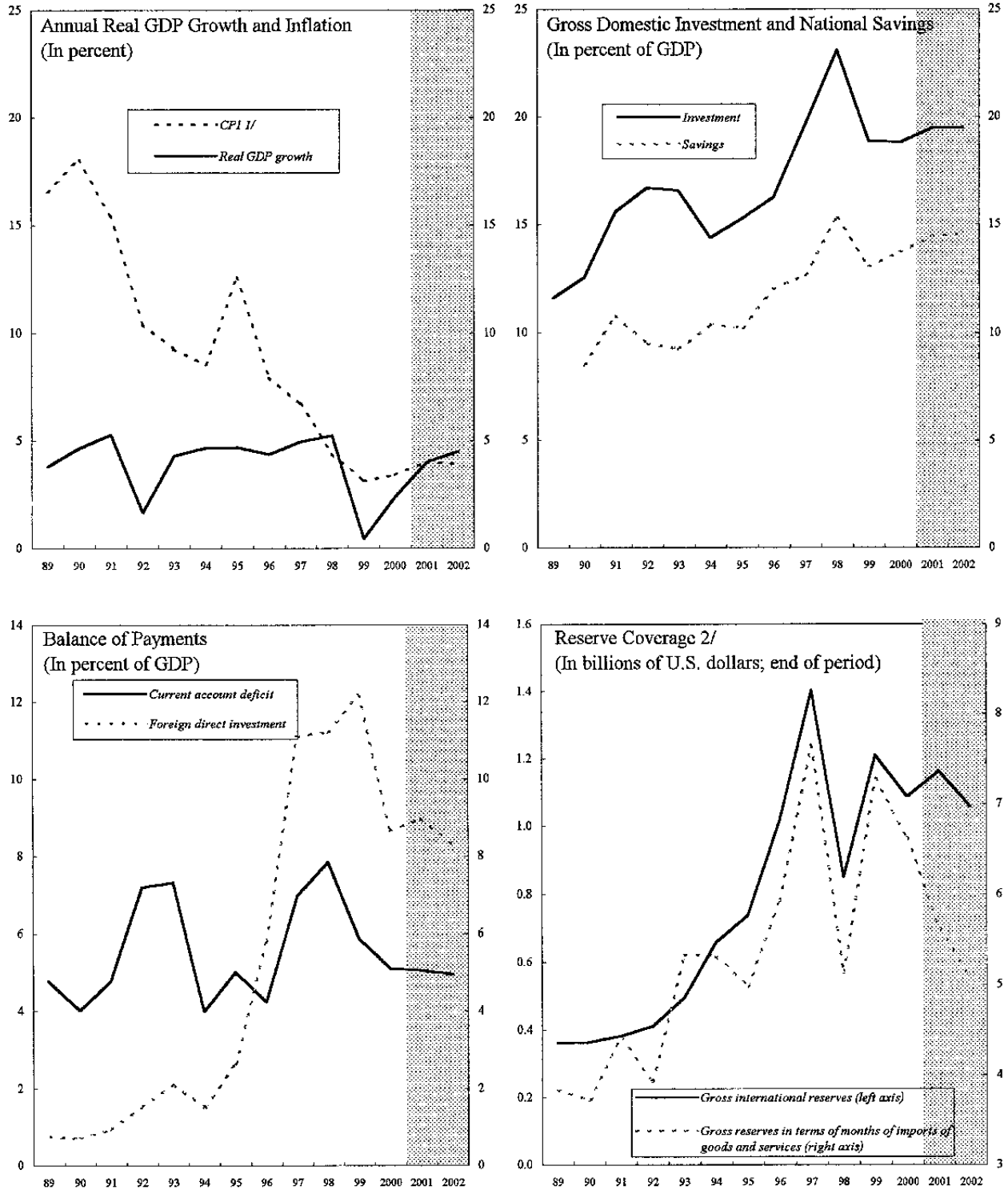
Table 16. Bolivia: Indicators of Fund Credit, 1999-2007

	Prel. 1999	Est. 2000	Projections						
			2001	2002	2003	2004	2005	2006	2007
Outstanding Fund credit									
In millions of SDRs	180.0	168.8	183.9	180.8	159.6	133.0	108.3	85.6	60.5
In percent of quota	104.9	98.4	107.2	105.4	93.0	77.5	63.1	49.9	35.3
In percent of GDP	3.0	2.6	2.8	2.7	2.2	1.8	1.4	1.0	0.7
In percent of exports of goods and services	18.8	15.4	15.6	13.9	11.0	8.4	6.4	4.6	3.0
Debt service due to the Fund									
In millions of U.S. dollars	34.8	30.9	31.5	29.5	29.6	36.7	34.2	31.4	34.5
In percent of quota	14.8	13.6	13.9	12.9	12.9	15.9	14.8	13.5	14.9
In percent of exports of goods and services	2.7	2.1	2.0	1.7	1.5	1.7	1.5	1.2	1.3
In percent of gross service due	11.9	10.1	10.2	9.9	10.0	12.9	12.3	10.8	11.4
In percent of gross official reserves	2.9	2.7	3.0	2.8	2.6	3.0	2.5	2.2	2.2
Gross Fund financing									
In millions of U.S. dollars	23.0	14.9	50.2	24.1	0.0	0.0	0.0	0.0	0.0
In percent of Bolivia's gross financing needs 1/	3.0	1.8	4.3	2.1	0.0	0.0	0.0	0.0	0.0
Memorandum item:									
Quota (in millions of SDRs)	171.5	171.5	171.5	171.5	171.5	171.5	171.5	171.5	171.5

Sources: Central Bank of Bolivia; International Monetary Fund, Treasurer's Department; and Fund staff projections.

1/ Gross financing needs are defined as the sum of the external current account deficit, scheduled amortization, repayments to the fund, changes in gross international reserves of the central bank, change in arrears, and net private capital flows.

Figure 1. Bolivia: Selected Economic Indicators, 1989 - 2002

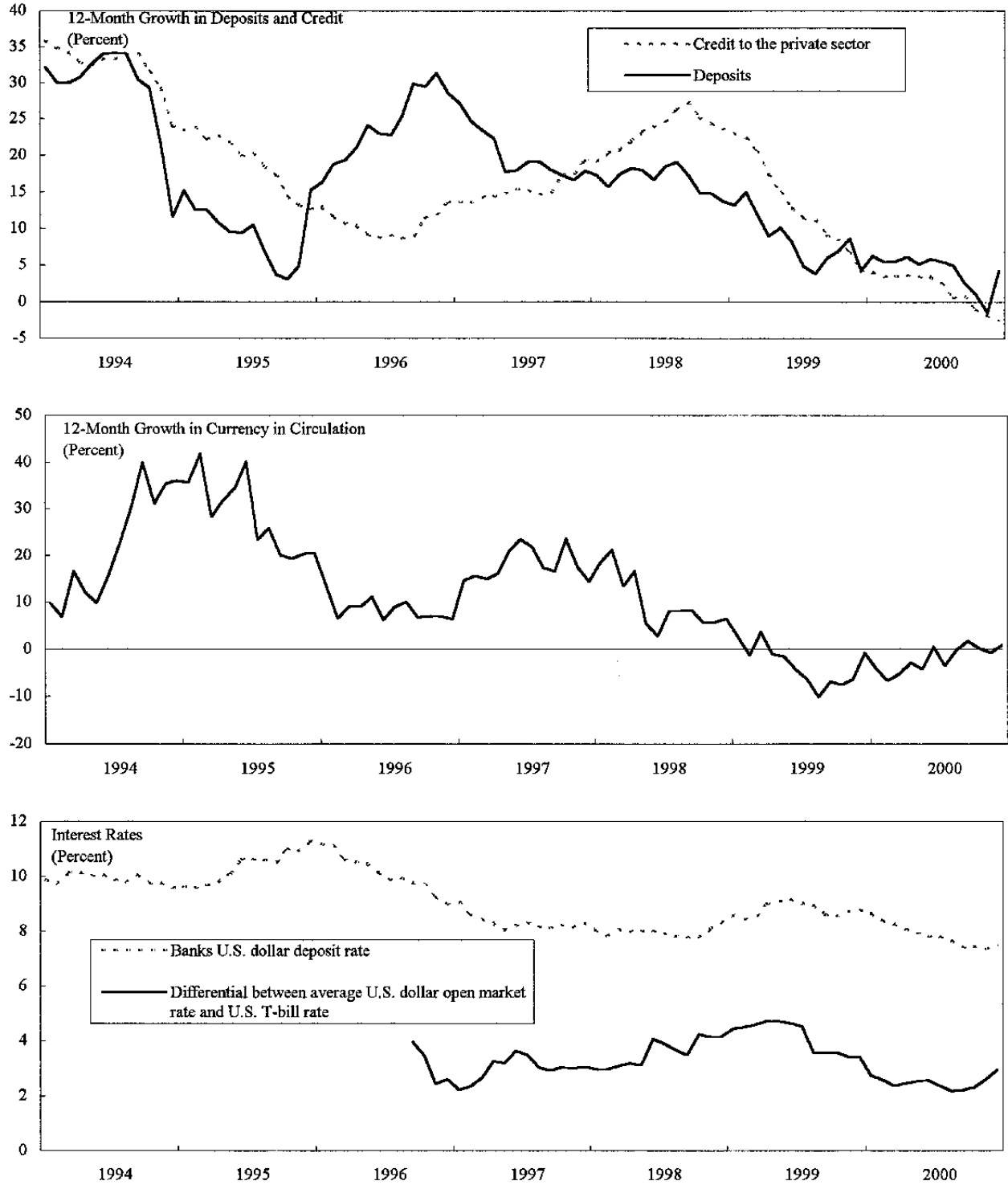


Sources: Central Bank of Bolivia; Ministry of Finance; and Fund staff estimates.

1/ December over December.

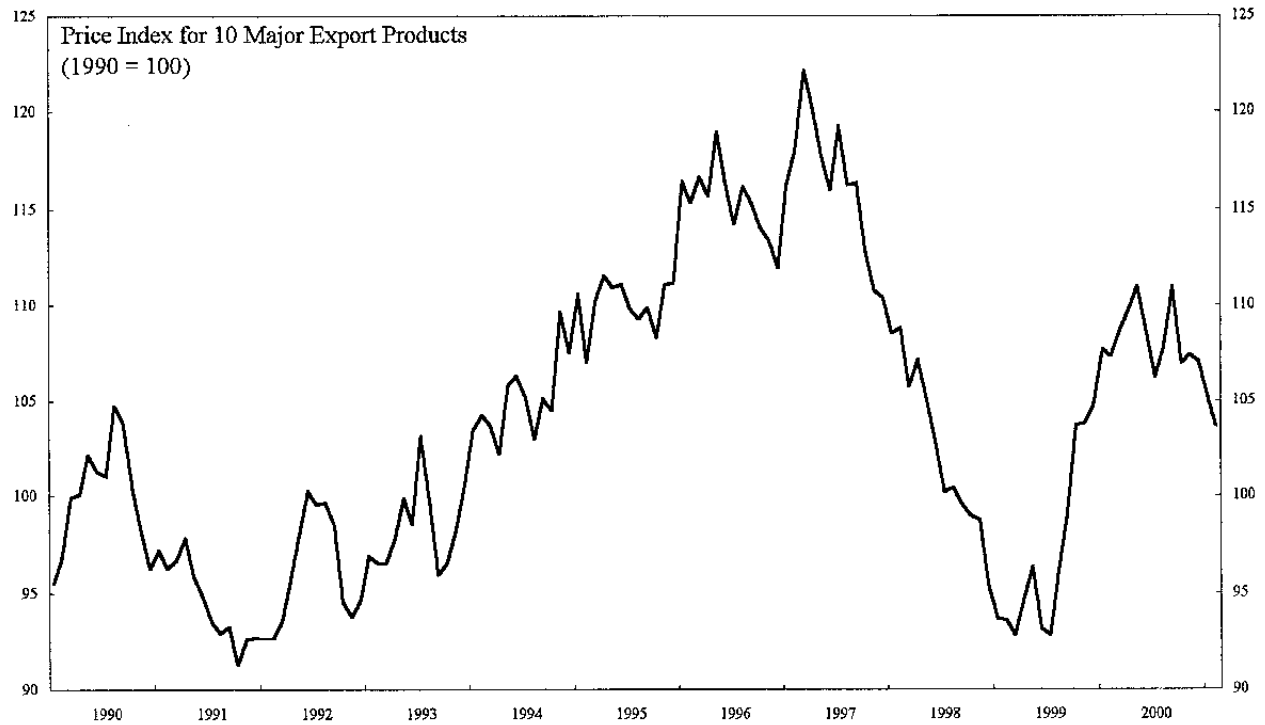
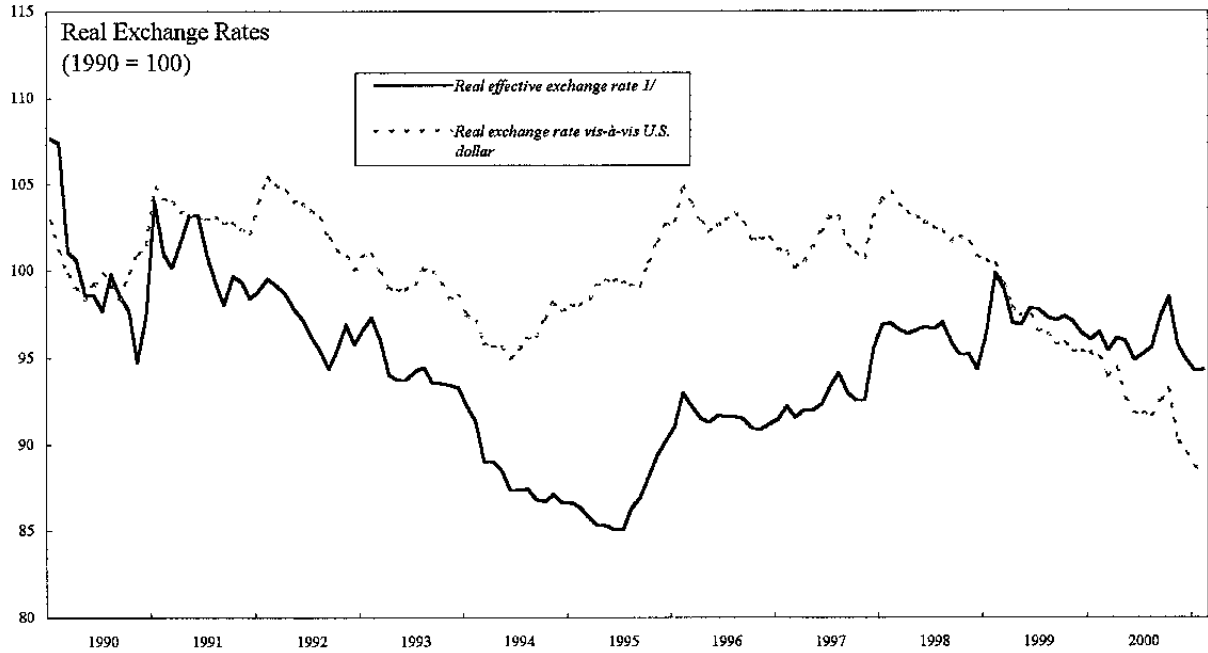
2/ Since 1997, includes reduced reserve requirements on foreign currency deposits and gold re-valuation from US\$250 per troy ounce.

Figure 2. Bolivia: Monetary and Financial Sector Indicators



Sources: Central Bank of Bolivia, Superintendency of Banks; and International Monetary Fund, *International Financial Statistics*.

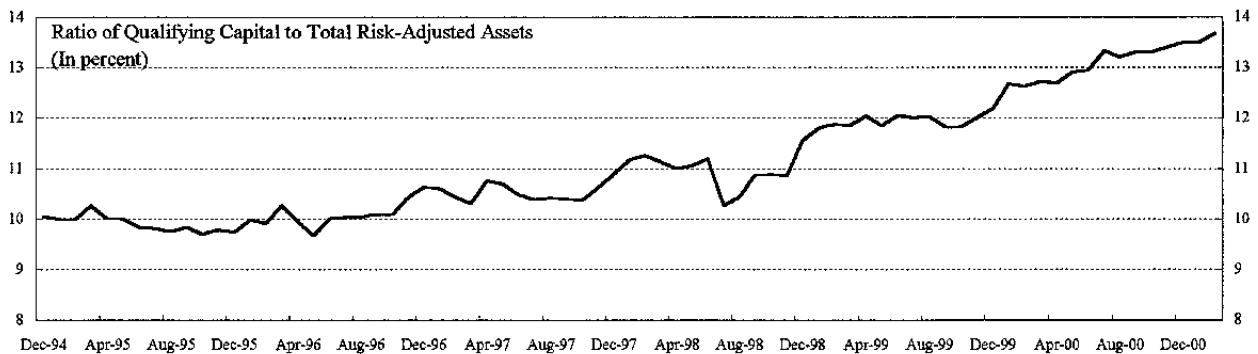
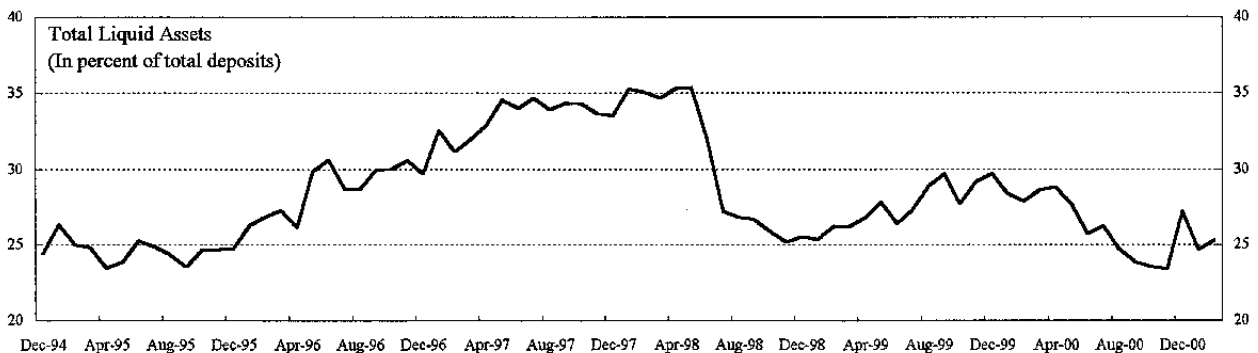
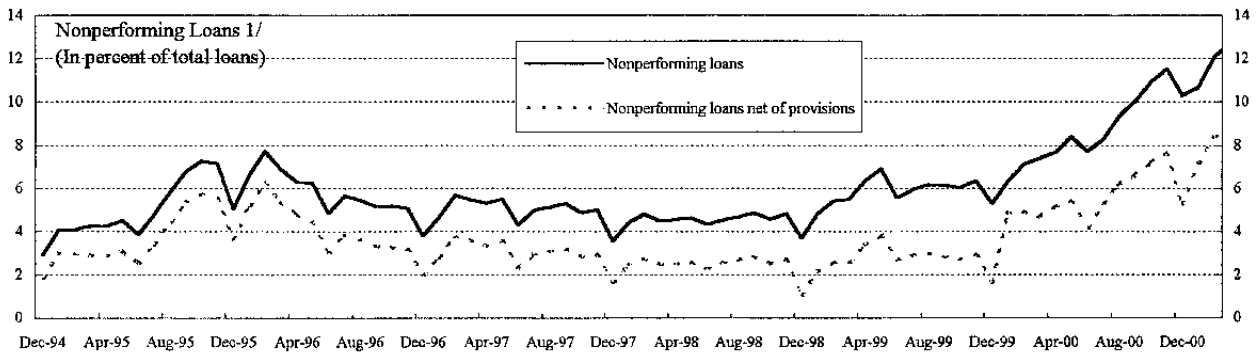
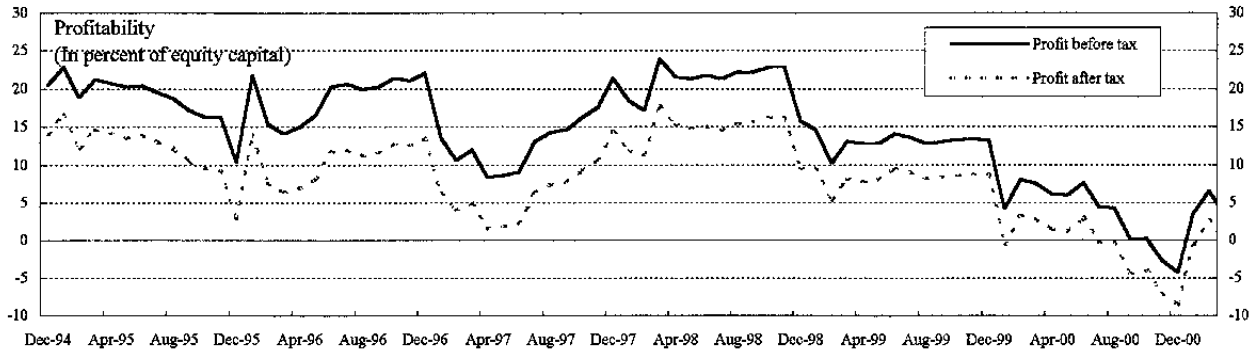
Figure 3. Bolivia: Exchange Rate and Export Price Indicator, 1990 - 2000



Sources: International Monetary Fund, *International Financial Statistics*; and Fund staff estimates.

1/ New weights, based on trade 1996-97

Figure 4. Bolivia: Commercial Bank Performance Indicators



Source: Superintendency of Banks.

1/ Data prior to January 2000 have been adjusted to exclude loans that are less than 30-days past due, based on the average ratio of such loans to total past due loans during January-September 2000.

BOLIVIA: FUND RELATIONS
(As of April 30, 2001)

I. Membership Status: Joined: 12/27/1945; Article VIII.

II. General Resources Account:	SDR Million	% Quota
Quota	171.50	100.0
Fund holdings of currency	162.64	94.8
Reserve position in Fund	8.87	5.2

III. SDR Department:	SDR Million	% Allocation
Net cumulative allocation	26.70	100.0
Holdings	27.30	102.2

IV. Outstanding Purchases and Loans:	SDR Million	% Quota
ESAF arrangements	165.13	96.3

V. Financial Arrangements:

Type of Arrangement	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
ESAF/PRGF	09/18/98	9/17/01	100.96	44.86
ESAF	12/19/94	9/09/98	100.96	100.96
ESAF	7/27/88	5/31/94	163.26	163.26

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

	Overdue 03/31/2001	2001	Forthcoming		2004	2005
			2002	2003		
Total	0.0	20.1	21.9	21.8	27.1	25.0
Principal	0.0	19.3	21.2	21.2	26.6	24.7
Charges/interest	0.0	0.8	0.7	0.6	0.5	0.3

VII. Exchange Rate Arrangement: The Bolivian currency is the boliviano. The central bank holds a daily foreign exchange auction, accepting all bids that are at least equal to the central bank's minimum price. If acceptable bids exceed the amount offered for auction, the lowest acceptable bids are prorated so as to exhaust the amount offered. The minimum price is adjusted from time to time in light of the evaluation of Bolivia's real exchange rate with respect to Bolivia's key trading partners. The administration of the system has resulted in spreads between the maximum and

minimum bids of less than 2 percent. On April 26, 2001, the official buying rate was Bs 6.50= US\$1.

VIII. Article IV Consultation: The previous Article IV consultation was concluded by the Executive Board on February 7, 2000 (EBS/99/235, SM/99/308). Bolivia is on the standard 12-month consultation cycle.

IX. Technical Assistance:

Department	Purpose	Time
FAD	Mission to advise on tax policy	January 1999
FAD	Mission to advise on modernization of the customs administration	June 1999, ongoing
FAD	Mission to advise on tax administration	June 1999 and February 2000
FAD	Mission to advise on fiscal decentralization	December 2000
MAE	Mission to advise on central bank operations and development of domestic capital markets	June 1999, ongoing
MAE	Mission to assess the vulnerability of the banking system	October 1999, April and December 2000
STA	Mission to advise on money and banking statistics	January 1999
STA	Mission to advise on balance of payments statistics	August 1999

X. Resident Representative: Mr. Gerardo Peraza, since February 2001.

Bolivia: Relations with the World Bank Group

(As of April 30, 2001)

The Bank's lending program for Bolivia is designed to support government efforts to implement its PRSP and reorient the role of the public sector toward provision of social services and infrastructure and improving efficiency in the provision of services to alleviate poverty and develop human capital.

Proposed operations for the period FY 2000-FY 2002 will consist of 8 IDA operations for the total of US\$235 million, including projects to expand and improve the quality of health services, rationalize the role of the state, increase and maintain physical infrastructure, and develop public sector institutions, including strengthening the capacities of departmental and municipal administrations and the judiciary.

The status of World Bank loans, IDA credits and IFC investments are shown in the following tables:

Bolivia: IBRD and IDA Lending by Sector (As of April 30, 2001)

(In millions of U.S. dollars, unless otherwise indicated)

	Number of Loans/Credits	Approved 1/	Amount	
			Disbursed	Undisbursed 2/
Disbursed	74	1,230.4	1,246.3	3.7
Current	16	571.5	246.8	301.4
Environment, industry, and mining		11.0	2.5	7.0
Integrated child development		30.7	17.3	11.5
Road maintenance		80.0	79.8	2.0
Education reform		40.0	25.5	14.3
Financed decentralization and accountability		15.0	10.5	3.8
Land administration		20.4	17.8	0.9
Rural water and sanitation		20.0	15.5	2.5
Participatory rural investments		62.8	18.7	41.4
Education quality		75.0	20.6	51.4
Regulatory reform T.A.		20.0	6.1	13.1
Regulatory reform adjustment (including IDA reflow)		41.8	22.3	18.6
Institutional reform		32.0	2.7	27.6
Health sector reform		25.0	7.0	15.9
Abapo-Camiri road		88.0	0.0	82.2
Hydro. Sec. Soc. Env. Mgt Capac. building		4.8	0.5	4.2
Indigenous peoples development		5.0	0.0	5.0
Total (net of cancellations)	90	1,801.9	1,493.1	305.1
<i>Of which : repaid</i>			327.9	

1/ Amount approved less cancellations.

2/ Not always equal to the difference between the amounts approved and disbursed because of changes in

BOLIVIA: RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

Background

As of April 30, 2001, the Inter-American Development Bank (IDB) had approved loans to Bolivia amounted to US\$ 2.6 billion, of which cumulative disbursements amounted to US\$2.3 billion. Bolivia's outstanding debt to the IDB was US\$1.5 billion.

The lending program

The IDB's lending program for Bolivia is aimed at supporting the Government's efforts to reduce poverty, as reflected in the *pillars* of the Operative Action Plan 1997–2002. This strategy, focuses on: (i) promoting sustained growth and increased employment opportunities in the productive infrastructure sectors, microenterprise, and rural development (*opportunity* pillar); (ii) supporting direct actions to improve access to the basic social services (*equity* pillar); and (iii) helping to consolidate the reform process (*institutionality* pillar). In infrastructure, the Bank-financed projects focused on roads, in particular, trade corridors that facilitate economic integration with neighboring countries. In the social area, the Bank is supporting reforms in health, education, and housing, including water supply and sanitation projects in urban areas. In addition, the IDB participates in the HIPC initiative with the IMF and the World Bank.

The proposed IDB lending program for Bolivia in 2001 is subject to the availability of concessional funds. It consists of nine loans for a total of US\$222 million, of which about 44 percent are targeted for the social sectors and 38 percent for infrastructure. The IDB Board of Directors has assigned US\$200 million for Bolivia during the period 2000–2001, US\$39 million of which were approved in the year 2000 and US\$47 in the first quarter of 2001.

Recent economic and sector work

During 2000, several missions visited La Paz to review the Bank's lending program and its lending portfolio. The Board of Directors approved the Country Paper for Bolivia, which outlines the Bank's strategy with the country, in June 9, 1999. The IDB also prepared several documents covering its lending program in support of the private sector, and is undertaking a study on the decentralization process.

IDB nonreimbursable technical cooperation and small projects

The IDB portfolio also includes active projects for US\$41 million in nonreimbursable technical cooperation, and US\$1.7 million in nonreimbursable small projects.

Bolivia: Relations with the Inter-American Development Bank
(In millions of U.S. dollars)

Number	Projects	Number of Loans	Approved	Disbursed	Undisbursed
I. Statement of IDB loans (as of April 30, 2001)					
Totally disbursed (less cancellations)			1,501	1,501	
Sectors		37	1,065	562	503
Roads		6	201	128	73
698/OC	Río Seco-Desaguadero		55	39	16
893/SF	Cotapata-Santa Barbara		40	37	3
840/SF	Patacamaya-Tambo Quemado		51	50	0
1039/SF	Ventilla-Tarapaya		52	0	52
1030/SF	PPF: Ventilla-Tarapaya		2	1	1
1065/SF	PPF: Santa Cruz-Pto Suarez		2		2
Energy		1	68	67	1
598/OC	Electricity		68	67	1
Agriculture		5	91	29	62
901/SF	Small rural projects		13	11	1
929/SF	Protection of environment		19	7	12
964/SF	Irrigation and drainage		26	11	14
1054/SF	FPP: Agricultural Services		0	0	0
1057/SF	Agricultural Services Program		34	-	34
Sanitation		4	174	93	81
777/OC	Sewerage-water supply		57	57	-
914/SF	Environment		7	7	0
987/SF	Basic Sanitation		70	29	41
1050/SF	Sanitation Small Municipalities		40	-	40
Social sectors		8	303	135	168
931/SF	Education Reform		80	36	44
858/SF	Basic health service		34	33	1
950/SF	Social investment fund		60	53	7
982/SF	Social management		3	0	3
995/SF	Programa de Atención al Menor		20	4	16
1006/SF	Housing		60	6	54
1031/SF&	Epidemiological Shield and		45	2	43
1033/SF	Health Reform		1	0	1
Institutional Strengthening		10	107	25	82
976/SF	Governability		12	7	5
954/SF	National register (RUN)		12	7	5
888/SF	Preinvestment		6	5	1
993/SF	Decentralization SNIPPRE		7	1	6
961/SF	Loan TC Tourism		5	3	2
1038/SF	Loan TC Access to Justice		3	-	3
1043/SF	Strengthening tax services SNII		3	-	3
1046/SF	National Census		7	2	5
1056/SF	Customs reform and Modernization		5	-	5
1075/SF-BO	Local Development and Fiscal Adjustment		47	-	47
Multisectoral lending		2	105	79	26
939/SF	Recapitalization of commercial banks		70	69	1
1020/SF	Micro and Small Enterprises		35	9	26
Private sector		1	15	6	9
1151/OC	Aguas de Illimani		15	6	9
Technical assistance		64	41	20	21
Total			2,607	2,083	
Repaid				598	
Outstanding				1,486	

Bolivia: Relations with the Inter-American Development Bank
(In millions of U.S. dollars)

	Amount	In Percent of Total
II. Proposed IDB Lending Program 2001		
Number of loans	9	
Total loan amounts	222	100.0
Social sectors	97	43.7
Local Development and Fiscal Responsibility	47	21.2
Education Pilot	10	4.5
Social Security Pilot	10	4.5
Support Poverty Reduction Strategy	30	13.5
Infrastructure	85	38.3
Socioenvironmental Impact Sta Cruz-Pto Suarez	25	11.3
Sta Cruz-Pto Suarez	60	27.0
Other	40	18.0
Rural Development	20	9.0
Municipal Financial Administration	10	4.5
Eco-tourism	10	4.5

Source: Inter-American Development Bank.

BOLIVIA: STATISTICAL ISSUES

The timeliness and coverage of economic statistics in Bolivia is generally adequate for monitoring purposes, but several data sources remain weak and additional work is needed. For instance, data on national accounts is usually produced with delay, wages and unemployment have very limited and inconsistent coverage, and lack timeliness; price indices, although methodologically correct, are becoming outdated; and the methodology used to construct the monthly indices of economic activity could be improved, and their release made more efficient. The fiscal and monetary authorities provide data to the Fund, mainly through the resident representative office, in a timely manner; information on national accounts often presents delays. Bolivia has several statistical publications, but there is no fully articulated publication policy.

The Fund's Statistics Department (STA) has provided extensive technical assistance on national accounts, consumer prices, external trade indices, and money and banking statistics. The authorities have been participating in GDDS since September 2000.

National accounts and economic activity

The National Statistics Institute (INE) prepares the data on national accounts. Drawing on technical assistance from STA, INE has revised its national income accounts to bring its methodology closer to international standards and developed better estimates of the contribution of informal activities to GDP. Still, some of the data sources remain weak, and the information is usually released with a delay. There is also a possibility that government consumption (in the expenditure breakdown) and the GDP for financial services (in the sectoral breakdown) might be overstated. In 2001 INE released quarterly national accounts statistics for GDP going back to 1990, but has yet to present revised quarterly figures for 1998 and 1999, as well as preliminary series for 2000.

INE also produces a monthly index of economic activity (IMAE), which is not available on a regular basis, but the methodology may need to be revised. In particular, the index may be overstating the degree of economic activity taking place in the financial sector. Further, the aggregation of sectoral indices of economic activity that are produced at different frequencies (i.e., the index of activity for manufactures is produced quarterly, while the other indices are constructed in a monthly basis) may be creating inconsistencies, as well as delays in the release of the IMAE.

Prices

The price statistics mission of February 1998 found that both the consumer price index (CPI) and producer price index (PPI) were due for revision. For the CPI, a new household budget survey is needed so that the basket of items, their weights, and the sample of outlets covered can be updated (the current index is based on 1990 expenditure data). The manufacturing PPI is based on 1990 output data, and is compiled quarterly but published only annually due to lack of resources. The INE intends to revise the PPI once 1997 industrial statistics are available, putting

the index on a base of 1998=100, updating the sample of producers, and improving price collection methods. Ideally, indices will also be established for the mining, gas, energy and water industries.

Public finances

Monthly data on revenues, current and investment expenditures, and the financing for the general government (central government, local governments and decentralized entities), public enterprises and the central bank's operating balance, with appropriate disaggregation, are provided with a relatively short lag. However, only data for 111 out of 314 municipalities are included in these figures.

The ministry of finance provides annual data to STA on the operations of the consolidated central government, and regional and local governments for publication in the *Government Finance Statistics Yearbook*. However, these data do not cover all operations of decentralized agencies and special funds, although the creation of a single fund for the direction of special funds will provide the authorities with more reliable information, especially at the local level. However, problems remain regarding the quality of data from local and regional governments, particularly with respect to debt.

It is currently impossible to track poverty-related spending at all levels of government, and the quality of the available data is poor. The authorities are planning to issue norms that will require municipalities to report on poverty and social spending. The data will be compiled on a quarterly basis by the Finance Ministry's programming unit (UPF) for 111 municipalities.

The future implementation of a comprehensive financial management system (SIGMA) will help ensure proper monitoring of public sector financial operations including local debt and social spending. The Inter-American Development Bank and the World Bank are funding the project.

Balance of payments statistics

Bolivia adopted the standards of the fifth edition of the *Balance of Payments Manual BPM5* in 1998, and balance of payments statistics for the period 1997-1999 have been reported to STA using the *BPM5* methodology. However, the coverage of Bolivia's balance of payments statistics is still quite narrow, particularly as regards services and financial transactions of the private sector. These weaknesses can be traced mainly to (a) the lack of a defined strategy in the Balance of Payments Department of the Central Bank that has hindered the implementation of enterprise surveys, and (b) the fact that data reported by financial institutions do not distinguish transactions between residents and nonresidents. The balance of payments mission that visited Bolivia in August 1999, reported its finding to the authorities and a two-stage action plan was developed with a view to alleviate major constraints and strengthen the balance of payments data base.

Monetary statistics

Monetary data for publication in *IFS* are provided for the central bank and the rest of the banking system on a timely basis. The coverage of banks in the monetary survey is comprehensive, and in 1995 the central bank also started to compile and provide the staff with data on the operations of other banking institutions.

The central bank also provides data on key variables such as net foreign assets, currency, and credit to the nonfinancial public sector to the resident representative office on a weekly basis. Two STA missions in 1998 and 1999 have resulted in an improvement of the coverage and quality of the monetary data of the central bank, and on a strengthening of its integrated monetary database. The coverage of monetary aggregates was expanded by including the operations of savings and loans associations, cooperatives and financial funds. Since July 1999, the Central Bank has shifted to a new accounting structure that has facilitated the derivation of monetary statistics.

With regard to the other depository corporations, there are still large inconsistencies in the interbank accounts, and the plan of accounts and supplementary information for commercial banks and other banking institutions need to be improved regarding residency and sectorization by economic sector.

**SURVEY OF REPORTING OF MAIN STATISTICAL INDICATORS
(AS OF MAY 18, 2001)**

Country: **Bolivia**

	Exchange Rate	International Reserves	Reserve/ Base Money	Central Bank Balance Sheet	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	GDP/ GNP	External Debt Service
Date of latest observation	May 17	May 4	May 4	May 4	Apr. 27	May 4	Apr. '01	Feb '01	Q4 2000	May 4 (prel.); Mar. '01	Q2 2000; 2000	Q4 2000
Date received	May 18	May 18	May 18	May 18	May 18	May 18	May 3	Apr. '01	Mar. '01	May '01	Dec. '00; May 01	Feb. '01
Frequency Of data 1/	D	W	W	W	W	W	M	M	Q	W (prel.); M	Q; A	Q
Frequency Of reporting 1/	W	W	W	W	W	W	M	M	Q	W; M	Q; A	Q
Source Of data 2/	A	A	A	A	A	A	A	A	A	A	A	A
Mode of reporting 3/	C	C	C	C	C	C	C	C	O	C	C	O
Confidentiality 4/	C	C	C	B	C	C	C	C	C	B	C	C

1/ D-daily, W-weekly, M-monthly, Q-quarterly, and A-annually.

2/ A-direct reporting by Central Bank, Ministry of Finance, or other official agency.

3/ C-cable or facsimile, and O-other (diplomatic pouch).

4/ A-for use of staff only, B-for use of staff and the Executive Board, C-for unrestricted use.

La Paz, Bolivia
May 25, 2001

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

Dear Mr. Köhler:

1. The attached Memorandum of Economic and Financial Policies reviews progress so far under the three-year PRGF arrangement approved by the Executive Board of the Fund on September 18, 1998, and describes the objectives and policies that the government intends to pursue during 2001 under the program supported by the third annual PRGF arrangement.

2. We believe that the policies and measures set forth in this memorandum are adequate to achieve the objectives of our program, but will take any other measures necessary for this purpose. During the period of the arrangement, the government will consult with the Managing Director, on its own initiative or at the request of the Managing Director, concerning the adoption of appropriate measures. Bolivia will conduct two reviews of the program supported by the third annual arrangement, to be completed no later than October 31, 2001 and March 31, 2002, respectively. The macroeconomic framework will be reviewed in the context of the reviews of the program, and takes into account the impact of additional debt relief that may be granted under the enhanced HIPC Initiative. Moreover, while Bolivia has outstanding financial obligations to the Fund arising from loans under the arrangement, Bolivia will consult with the Fund from time to time, at the initiative of the government or whenever the Managing Director requests consultations on Bolivia's economic and financial policies.

3. On this basis, we request that the two undisbursed loans under the second annual arrangement under the PRGF for Bolivia, for a total amount equivalent to SDR 22.443 million, be rephased over the period of the third annual arrangement, which will thus be for an amount equivalent to SDR 56.096 million, with two disbursements of SDR 19.0 million each, of which the first one is to be made available after approval of this arrangement and the subsequent one upon completion of the first program review and observance of performance criteria for end-June 2001, and a third disbursement of SDR 18.096 million upon completion of the second program review and observance of performance criteria for end-December 2001. We also request an extension of the three-year commitment period to June 7, 2002, to allow for three disbursements under the third annual arrangement.

4. The government of Bolivia authorizes the publication and distribution of this letter and all reports prepared by Fund staff regarding the 2001 Article IV consultation with Bolivia and the program for the third annual arrangement under the PRGF, reports prepared jointly with Bank staff regarding Bolivia's reaching the completion point under the enhanced HIPC Initiative, and Bolivia's Poverty Reduction Strategy Paper.

Sincerely yours,

 /s/
José Luis Lupo
Minister of Finance

 /s/
Juan Antonio Morales
President

BOLIVIA: MEMORANDUM OF ECONOMIC AND FINANCIAL POLICIES

I. INTRODUCTION

1. **Since 1985, Bolivia has achieved substantial progress in the areas of macroeconomic stability and structural adjustment under a series of democratically elected governments.** Anchored by sound fiscal policy and a comprehensive program of structural reforms, economic growth averaged 4 percent a year during the 1990s, as inflation was reduced to low single-digits. Direct foreign investment exceeded 10 percent of GDP during the latter part of the decade and the import coverage of gross official international reserves rose to more than six months of imports of goods and services. However, despite the overall good performance of the 1990s, external shocks and the negative impact on domestic demand of the successful coca eradication program, resulted in a sharp economic slowdown in 1999, when real GDP grew by only 0.4 percent.

2. **In recent years, the government, with the support of the international community, has stepped up its efforts to reduce poverty, which in 1999 still covered nearly two-thirds of the Bolivian population.** In particular, having established a track record of sound economic policies, Bolivia reached the completion point under the original Heavily Indebted Poor Countries (HIPC) Initiative in September 1998, and was one of the first countries declared eligible for debt relief under the enhanced HIPC Initiative in February 2000. In conjunction with the original HIPC Initiative, the government set an ambitious agenda to improve social welfare, as measured by a set of indicators, under the 1997 National Action Plan (POA), which was based on our first National Dialogue. The POA, which partially achieved its goals, has now been succeeded by the Bolivian Poverty Reduction Strategy (EBRP), developed over the past year and a half months in the context of a second, broadly participatory, National Dialogue that featured extensive discussion at the local, regional, and national levels. Under the EBRP, Bolivia aims to reduce the incidence of poverty by a third by 2015, while cutting the incidence of extreme poverty in half.

II. DEVELOPMENTS UNDER THE 2000 PROGRAM

3. **The economic recovery in 2000 proved to be slower than envisaged in the program.** Real GDP growth is estimated to have recovered to nearly 2½ percent in 2000, compared with the program target of 4 percent. The stagnation of domestic demand continued, owing to falling income in the informal sector from coca eradication and a reduction in contraband-based commerce, as the ongoing customs reform has reduced illegal imports. Moreover, during the year, two episodes of acute social unrest disrupted transportation and output in various sectors. Although prices surged temporarily during the unrest, the increase in consumer prices during 2000 was only 3.4 percent, compared with the program target of 4.0–4.5 percent. Exports staged a strong recovery in 2000, led by increased sales of natural gas via the new pipeline to Brazil, and the external current account deficit narrowed to 5.5 percent of GDP, from 5.9 percent in 1999. Foreign direct investment tapered

off in 2000, but remained strong at 8½ percent of GDP, and net international reserves of the central bank fell by only US\$23 million, compared with a programmed decrease of US\$150 million (after adjustments).

4. **The weaker-than-expected economic recovery and periods of social unrest exerted strong pressure on the public finances in 2000.** In response to the economic slowdown, the government approved a stimulus package (PRE) in April, consisting mainly of selected tax breaks and temporary spending measures, including a temporary emergency employment program for unskilled workers. Also, domestic fuel taxes were lowered to stabilize domestic fuel prices. Tax revenues remained flat at 18½ percent of GDP, as the weak economy and tax relief measures offset the gains in tax efficiency. To maintain fiscal control, both current and capital spending were restrained. Because of the additional cost of the emergency employment program, together with the higher-than-expected cost of the pension reform, in July we agreed with Fund staff on a modest increase of 0.3 percentage point of GDP in the end-December program ceilings for the overall fiscal deficit and net domestic financing of the combined public sector. These modified targets for December were met, as were all other quantitative program benchmarks and performance criteria for 2000.

5. **A weakening of activity in the banking sector, which began in 1999, continued during 2000, but a number of changes in the structure of bank balance sheets have improved banks' ability to withstand such periods of weakness.** In U.S. dollar terms, both broad money and bank credit to the private sector fell slightly during the year, mainly reflecting the weak economy. Credit was constrained also by the ongoing financial restructuring of the country's largest bank, purchased by foreign investors in 1998. The bank's loan portfolio was rationalized, and foreign liabilities were reduced. The phasing-in of stronger prudential norms, including the categorization of new credits based on borrowers' cash flow, instead of collateral, also encouraged more conservative lending practices, while the social unrest further discouraged domestic lending. Commercial bank performance indicators deteriorated in 2000, including nonperforming loans which rose from 6.6 percent of total loans at end-1999 to 10 percent at end-2000. However, banks' balance sheets have been strengthened by a significant improvement in their net foreign asset position, and increases in capitalization and in loan-loss provisions have helped maintain the soundness of the banking system, which is generally well supervised.

6. **Although there were some delays in the structural adjustment program, progress has been achieved in several areas.** The customs reform advanced with the issuance of regulations in August 2000 for implementation of the 1999 Customs Law that establishes an autonomous customs agency with an independent board of directors and professional staff. Some 50 percent of the professional and technical staff have been selected through a competitive selection process thus far. The selection process for the remaining 50 percent is under way and is expected to be completed by mid-2001. In December 2000, congress passed a law for the reform of the internal revenue service (SI), which allows for the restructuring of this institution along the same lines as the customs reform. Advances were also made with the privatization program. The sales of the state smelting company (Vinto) and dairy (Milka) were completed in early 2000. Further, the sale of the refineries,

the storage facilities, and jet fuel stations of the state-owned oil company (YPFB) were sold by December 2000.

III. ECONOMIC PROGRAM FOR 2001

7. **The new poverty reduction strategy (EBRP) provides the basis for reorienting policies and programs toward a more effective fight against poverty over the medium term. It incorporates a macroeconomic framework, aiming at higher rates of sustained economic growth with sound economic management.** This framework, which will form the basis of our annual economic programs starting in 2001, aims to lift economic growth to 5½ percent a year by 2008, maintain annual inflation rates of 3½–4 percent, and assure long-term fiscal sustainability by gradually reducing the deficit of the combined public sector to less than 1½ percent of GDP by 2008 and beyond.

8. **Consistent with output growth of about 4 percent, the program for 2001 aims at limiting inflation to 4–4½ percent during the year.** In addition to supporting poverty reduction projects, the assistance under the enhanced HIPC Initiative (equivalent to about ½ percent of GDP in 2001) will provide a timely economic stimulus. Led by continued export growth, the external current account deficit is projected to decline to 5.1 percent of GDP. Foreign direct investment would remain strong in 2001, especially in light of the large ongoing investment in the San Cristóbal mining project, but other capital shortfalls are expected to yield an overall balance of payments deficit and a loss of official net international reserves of US\$100 million. Gross reserves will be maintained at the equivalent of more than 5½ months of imports of goods and services. A targeted increase in public sector savings, based on a recovery of the tax base, and further gains in the efficiency of the customs and domestic tax administrations, is expected to help finance a growing public investment program, while still achieving a slight decrease in the fiscal deficit. The central bank will continue to control the expansion of its net domestic assets and maintain an exchange rate policy stance that preserves external competitiveness.

A. Fiscal Policy and Reforms

9. **The combined public sector deficit will hold steady at 3.7 percent of GDP in 2001, as the objective of continuing the process of fiscal consolidation needs to be balanced against the need to support the economic recovery with public sector investment.** Tax revenue is projected to improve by 0.8 percentage point of GDP, reflecting in part continued improvements in tax administration. Also, tax revenue from the hydrocarbons sector has been targeted to rise by 0.5 percentage point of GDP. Current spending will be held in check, with the wage bill increasing in line with expected nominal GDP, to allow for a small increase in public sector investment, to 7.1 percent of GDP in 2001, without placing undue pressure on the fiscal deficit. Net external financing is projected to cover two-thirds of the combined public sector financing requirement in 2001, mostly in the form of concessional loans from multilateral and bilateral creditors. External borrowing on nonconcessional terms will be limited so as to permit some reduction of the stock of

commercial debt. Net domestic financing will not exceed Bs 701 million (1.2 percent of GDP) in 2001, mostly reflecting borrowing from the private pension funds. Net domestic financing will continue to decline steadily over time (to zero by 2006) to permit a greater allocation of the economy's financial resources to private investment. The fiscal targets of the program will be monitored on the basis of quarterly ceilings on the overall deficit and the net domestic financing of the combined public sector, as presented in the attached Table 1.

10. After the fiscal program for 2001 was established, a revenue shortfall arose in the first quarter of the year that reflected a weaker-than-expected performance of domestic tax revenue. However, the deficit of the combined public sector was kept below the limit we established for the quarter, as expenditure also was restrained. We have revised the fiscal projections—assuming that an acceleration of tax revenue will accompany a recovery of output and demand in the second half of the year, and also taking account of higher outlays for pensions than initially projected—and we have decided on a set of measures, consisting mainly of expenditure cuts, to close the fiscal gap. The spending cuts are being carried out with a view to protecting poverty-related expenditure to the extent possible.

11. **Given the advanced stage of the customs reform, we expect significant revenue increases from taxes on imports in 2001** (10 percent increase in ordinary customs revenue, including tariffs, VAT, excise taxes, and hydrocarbon taxes on imports). Building on the progress made last year, the Customs administration will implement modern control mechanisms such as: an automated transit control system by June 2001, using magnetic cards; a computerized customs control system being installed (ASYCUDA) is expected to become fully operational by end-2001 for exports, imports and transit regimes; and a system of customs control a posteriori for imports will be established by end-2001. The government is committed to strengthening the Customs administration by assuring the full funding of the agency's budget in the short- and long-term (which could be achieved through assigning a fixed percentage of collections of taxes on imports) and providing resources to increase the customs unit of the national police to 100 full-time officers; these two measures will be subject to a structural benchmark under the program.

12. **Domestic tax administration is being strengthened, which will improve transparency and, in the future, generate increased revenue from existing taxes.** A new tax procedures code, which aims at strengthening the enforcement power of both the tax and customs administration, is well advanced in the congressional approval process. Under the new code, (i) disputes over tax liabilities will proceed through an administrative process with the payment of most or all of the disputed amount before judicial review of the case is pursued; (ii) tax fraud and similar violations will be subject to criminal penalties; (iii) sworn tax declarations will be a sufficient legal basis for pursuing tax collection; and (iv) clear and adequate rules for applying the statute of limitations (*interrupción del periodo de prescripción*) will be specified. The tax code, following approval by the Senate, is now being considered by the Chamber of Deputies, where it has been approved on the first of two readings. The draft code has been given priority over all other laws being considered by the chamber of deputies, which will wait until the tax code has been approved before considering other legislation. If it has not been approved when the current congressional period ends, an

extraordinary congress will then be called for the exclusive purpose of passing the tax code before the next ordinary congress begins in August. Full congressional approval will be subject to a structural performance criterion. The implementing regulations of the new tax procedures code will be issued no later than end-December 2001; this measure will be a structural benchmark under the program. Implementing regulations of the SI reform will also be issued by end-August 2001, subsequent to the appointment of the new Board of the SI; this measure will be a structural benchmark under the program. As in the case of the customs reform, the SI reform aims at removing political influence in the selection of staff and establishing a career system for professional staff recruited on the basis of merit. By September all employees will have to pass a competency examination as a precondition to becoming permanent staff.

13. **To control the costs of the pension reform, which has put much pressure on the overall fiscal balance since its inception in 1997**, we will close admission to the old system for new retirees by the end of 2001.

B. Monetary, Credit, and Exchange Rate Policies

14. **We remain committed to a strong and independent central bank, which will continue to promote the objective of keeping inflation low and adhering to its other core responsibilities as defined in the central bank law.** Inflation pressure at the beginning of the year was very low. The central bank will monitor developments in the money market with a view to keeping an adequate supply of liquidity while monitoring the development of its domestic assets. The monetary program is based on currency growth during the year about in line with that of nominal GDP. Some decrease in net international reserves is programmed, which will permit a moderate increase in the net domestic assets of the central bank. In particular, the transfer of a portion of the central bank's development loan portfolio will facilitate NAFIBO's support of long-term bank lending to small- and medium-sized producers. The demand for money and credit is expected to begin a recovery in the course of the year, with broad money and bank credit to the private sector both projected to grow (in U.S. dollar terms) by about 3 percent during 2001. To monitor the monetary program, quarterly targets on the net international reserves and ceilings on the net domestic assets of the central bank have been established (see Table 1).

15. **Sound financial sector policies will continue to be pursued during 2001.** A draft law for strengthening the financial system, which is currently before congress, would reinforce the role of the Superintendency of Banks in the early detection of bank problems and their prompt correction, and provide for more effective bank resolution procedures. We have decided to postpone the introduction of a funded deposit insurance scheme, pending further study of the appropriate size of the guarantee, in line with international norms, and of the timing of its introduction. Approval of the other financial sector reforms in the draft law by October 2001 will be subject to a structural performance criterion under the program. Implementing regulations of the new law will be issued by the Committee on Prudential Norms (CONFIP) and Superintendent of Banks by end-2001; this measure will be a structural benchmark. Further, as part of the continued phasing in of stronger prudential

norms that became effective in September 1999, the twice-yearly adjustments to provisioning requirements will continue this year with increases in June and September 2001.

16. The share of nonperforming loans has continued to rise in the first months of 2001, as the economic recovery in a number of sectors has not yet gained momentum. To encourage banks to reschedule their loans to clients with the capacity to repay, in May 2001 a Special Fund for Economic Reactivation (FERE) was established. It will be financed by government-guaranteed bonds issued by the second-tier bank, NAFIBO, up to a total of US\$250 million, and long-term (12-year's maturity) credit will be granted to banks that reprogram loans, allowing them to meet the productive sector's need for a lengthening of the maturities of bank loans, while helping banks avoid a maturity mismatch. The credit risk for the restructured loans is retained by the banks, ensuring that only if a bank fails will the government's guarantee be invoked. It is important to note that every bank negotiates with its borrowers on an individual basis, and the reprogrammed loans will be subject to the supervision of the Superintendency of Banks. The May package also provides one-time subordinated credits from NAFIBO to capitalize banks, up to a total of US\$80 million, that will be financed through the transfer to NAFIBO of the development portfolio and corresponding liabilities of the central bank. This capitalization program will be designed to ensure that fiscal and quasi-fiscal costs are minimized, and will be managed within the agreed fiscal program.

17. **The government will continue implementing an exchange rate policy aimed at preserving Bolivia's external competitiveness.** The Government of Bolivia believes that the current exchange rate system, by which the central bank manages the *boliviano* in the daily foreign exchange auctions, has served the country well. The central bank will continue to monitor developments in the foreign exchange market closely.

C. Poverty Reduction and Structural Reforms

18. The poverty-reduction strategy, which incorporates the conclusions of the National Dialogue 2000, identifies a comprehensive agenda for infrastructure projects, social expenditures, and institutional reforms aimed at reducing the incidence of poverty and extreme poverty in Bolivia to 41 percent and 17 percent of the population, respectively, by 2015. The four main components of the strategy are to enhance opportunities of the poor for employment and income; develop the productive capacities of the poor; provide greater security and protection; and increase social participation and integration. Together with these four components, the strategy incorporates two cross-cutting issues—gender equity and sustainable use of natural resources—and develops an institutional framework for its implementation. Upon reaching the completion point under the enhanced HIPC Initiative, the government will begin to direct the new flows of debt relief to all municipalities for poverty reduction projects. As decided in the National Dialogue, 70 percent of this assistance will be distributed to municipalities based on the concentration of poverty, and the remaining 30 percent will be distributed evenly to the nine regional departments (and, within each department, to municipalities also on the basis of poverty incidence). In conjunction with the

Catholic Church and other civil groups, a system of social oversight will be established to monitor the use of HIPC resources and to provide feedback for setting future priorities.

19. **The program of social policies will be carried out in accordance with the strategy described in the EBRP.** Intermediate targets have been set for various social and economic indicators, in order to help evaluate the progress of the strategy in a timely manner, and provide a reference for the social monitoring mechanisms. In line with the EBRP, the public investment program will focus on roads, education (especially at the primary level), primary health care, basic sanitation (especially in rural areas), rural electrification, establishment of clear property rights for agricultural lands, and small scale irrigation.

20. **In order to ensure the proper tracking of poverty-related expenditures, we are committed to developing a comprehensive financial management system (SIGMA),** which will permit a more effective control of government expenditure generally. This system, already operational at the central government level, will be adapted for use by municipalities. The modifications will be completed for ten large municipalities by August, and for five small- and medium-sized municipalities by October 2001. The systems will be fully operational in these municipalities by mid-2002. The phased implementation will include an additional five municipalities to the system each month, so that by end-2003 about 100 local governments will be operating under the SIGMA. We will also develop, in association with a joint Bank-Fund mission, an action plan to improve public expenditure management for tracking poverty-related expenditures.

21. **The government will issue norms that require municipalities to report on poverty-related and social-sector spending, showing separately the use of HIPC resources, as well as a breakdown between current and capital outlays.** These data, which will be compiled on a quarterly basis by the Finance Ministry's programming unit (UPF) for the 111 municipalities that report to it, will help provide for effective mechanisms of social oversight. We will work with the World Bank to plan for a tracking survey of the HIPC resources spent by at least one large city and continue periodic tracking surveys of HIPC resources in other large municipalities in the future.

22. **The EBRP provides a significant step toward a medium-term budget framework that will be further developed in the period ahead.** The EBRP outlines poverty-related spending needs, which account for a major proportion of all public investment, and it takes account of associated recurrent outlays and provides an accounting framework for ensuring that spending levels and financing needs are in line with the fiscal program. This will be expanded into a more comprehensive medium-term framework in order to improve fiscal planning associated with the implementation of the antipoverty strategy, while maintaining consistency with fiscal sustainability. In 2001, UDAPE will carry out the monitoring and evaluation of the strategy in coordination with the macro group. By the end of the first quarter of 2002, the Ministry of Finance will prepare the methodology and budget guidelines for the preparation of medium-term budget plans. For the 2003 Budget, the line ministries will submit three-year expenditure plans (subject to ceilings prescribed by the Ministry of

Finance) with their annual budget request. These plans would form the basis for future budget requests.

23. **The government intends to prepare a proposal for a comprehensive tax reform, which would be ready for consideration by the next government.** The proposal will be aimed at enhancing the efficiency of the tax system, but it also would provide for a more progressive taxation and a greater revenue-generating capacity, thus supporting the objectives of the EBRP. We expect to have an outline of the tax policy proposal, adapting where appropriate the recommendations of the Fund's Fiscal Affairs Department, by end-September 2001 and to have a proposal by March 2002. If adopted by the new government, the tax reform could be ready for full implementation by January 1, 2003. It will aim at replacing distortionary taxes with alternative revenue sources, either by increasing existing tax rates or by introducing new, more equitable taxes, such as a personal income tax. It also will address the need to modify the special tax regimes in the commercial and transportation sectors, so that the relatively few large taxpayers in these sectors can be incorporated in the general tax regime.

24. **The Government of Bolivia intends to complete its privatization program by the end of 2001.** Following the privatization in 2000 of most of YPFB's assets, the remaining gas networks and the LPG bottling plants will be sold during the fourth quarter of 2001. The government also intends to offer for sale in 2001 the electricity distribution company of Tarija (SETAR), the electricity generation and distribution company of Potosi (SEPSA), and the electricity generation company of Trinidad (COSERELEC).

25. **During 2001, the government intends to continue improving the process of fiscal decentralization.** The draft law on the National Dialogue provides for a phased transfer of responsibilities for current spending on health and education from regional to municipal governments, so that a better coordination of needs and spending programs can be achieved. Also, the government has established a program of fiscal reform and debt restructuring for municipalities with serious problems of overindebtedness, with the aim of helping them regain control over their finances and improve their fiscal monitoring capability. The government has agreed with five municipalities on financial adjustment programs (PRF), and an additional six PRF programs, including those agreed with the development fund FNDR, are expected to be signed by the end of 2001. Although the performance targets under these programs are annual, progress will be monitored on a quarterly basis, and an evaluation carried out on a semiannual basis. A plan for further reform on fiscal decentralization will be formulated, for which the assistance of the Fund's Fiscal Affairs Department will be requested.

26. **With a view to achieving consensus on a modernization of labor legislation, pilot programs to demonstrate the benefits that a modern labor law would permit are being implemented** (for example, hourly work that is agreed upon by private firms and university students).

D. External Sector

27. **The external current account deficit is projected to decline from 5.5 percent of GDP in 2000 to 5.1 percent of GDP in 2001.** Export growth is expected to reflect continued strong growth of Bolivia's two major exports, natural gas and soy products. Over the medium term, the current account deficit will remain in the region of 5 percent of GDP, fully covered by foreign direct investment inflows. The central bank will be able to maintain gross international reserves at more than 5½ months of imports of goods and services. During the period of the program, Bolivia will keep the current account of the balance of payments free of restrictions and will refrain from increasing external tariffs or introducing nontariff barriers for balance of payments purposes.

28. **The government of Bolivia views the favorable medium-term outlook for foreign direct investment as a signal that Bolivia's reforms are yielding significant gains.** The investment projects in export sectors, such as oil and gas exploration, electric energy, and mining, are expected to contribute to a vigorous growth in exports and economic activity over the medium term. Nonetheless, this outlook depends in part on the environment in the region, and the Bolivian authorities stand ready to adjust their policies, if necessary, to ensure attainment of these medium-term objectives. The government will also seek to open export markets through free trade agreements, with the aim of expanding investment in labor intensive sectors, such as manufacturing and agriculture.

29. **The program for 2001 is fully financed, and the government of Bolivia would like to express its gratitude to Bolivia's official creditors for the relief already granted under the original HIPC Initiative.** The assistance received since September 1998 has helped to reduce the external debt burden to a more manageable level and assists in covering the fiscal costs of structural reforms without compromising social expenditure. However, poverty remains widespread in Bolivia, and the government hopes that official creditors will consider favorably Bolivia's request for reaching the completion point under the enhanced HIPC Initiative, which grants a further reduction in the net present value of its external debt at end 1998 from close to 214 percent of exports at present to 150 percent of exports. The Government of Bolivia will continue to improve the structure of its external debt in order to maximize the benefits that would accrue to it under the enhanced HIPC Initiative. Bolivia does not have any external payments arrears, and will not incur any new external payments arrears at any time during the arrangement.

Attachments

Table 1. Bolivia: Financial Benchmarks and Performance Criteria
Third Annual Arrangement Under the PRGF

	2001				
	Mar. Benchmark	Outturn	Jun. 2/	Sep. 1/	Dec. 2/
(Cumulative amounts from December 31, 2000 in millions of bolivianos)					
Deficit of the combined public sector 3/	509	406	969	1,378	2,102
Net domestic financing of the combined public sector 4/ 5/	279	412	227	330	701
(Cumulative changes from December 31, 2000 in millions of bolivianos)					
Net domestic assets of the central bank 4/	527	322	528	509	887
(Cumulative changes from December 31, 2000 in millions of U.S. dollars)					
External debt with maturities up to one year 6/	10	...	10	10	0
Nonconcessional external debt 7/	0	-24	0	0	-10
Net international reserves of the central bank 8/ 9/	-135	-123	-128	-120	-100
Projections for calculation of adjusters to the program					
(Cumulative change from December 31, 2000 in millions of bolivianos)					
Adjuster for currency issue					
Currency issue (program)	-361	-486	-314	-281	229
Maximum adjustment to net international reserves target	25	...	49	74	99
(Cumulative amounts from December 31, 2000 in millions of U.S. dollars, unless otherwise indicated)					
Adjuster for net external financing of the nonfinancial public sector					
Net external financing of the nonfinancial public sector (program) 10/	36	0	109	145	191
Maximum adjustment to domestic financing of the combined public sector (Bs millions)	43	43	85	128	170
Financing through HIPC debt relief (program) 11/	-1	-1	4	14	22
External arrears, stock at end of period (program)	0	0	0	0	0

1/ Program benchmarks.

2/ Performance criteria.

3/ The deficit limit will be reduced (increased) by the amount of the shortfall (excess) between actual and projected financing through HIPC debt relief. The financing from HIPC relief comprises refinancing and the amortization component of stock of debt reduction operations.

4/ The limits will be adjusted downward by the amount of any overdue obligations to foreign creditors.

5/ This limit will be adjusted upward by the shortfall, if any, of the actual cumulative net external financing to the nonfinancial public sector from the projected cumulative external financing, subject to the maximum adjustment shown in this table.

6/ Excludes normal import credits and reserve liabilities of the central bank. The term "debt" has the meaning set forth in point No. 9 of the Fund's Guidelines on Performance Criteria with Respect to Foreign Debt, adopted on August 24, 2000, and reflected in paragraph 7 of the Technical Memorandum of Understanding.

7/ Excludes: (i) concessional loans with a grant element of 35 percent or more using the OECD commercial interest reference rates (CIRRs) as of April 15, 2001; (ii) changes in central bank liabilities defined as part of the net international reserves; and (iii) debt of the private sector with official guarantee.

8/ This limit will be adjusted upward by the amount of any overdue obligations to foreign official creditors.

9/ The limits will be adjusted downward by the shortfall, if any, of currency issue from the projected change shown in this table.

10/ Does not include the HIPC debt relief through rescheduling or the amortization component of stock of debt reduction operations.

11/ Comprises refinancing and the amortization component of stock of debt reduction operations under HIPC initiative, less debt service on earlier HIPC debt rescheduling operations.

Table 2. Bolivia: Structural Benchmarks and Performance Criteria, 2001
Third Annual Arrangement under the Current PRGF

Performance Criteria/Benchmark	Policy Measure	Timetable for Implementation
<i>Public Sector Institutional Reform</i>		
Benchmark	Issue implementing regulations of the Internal Revenue Service.	August 2001
Performance criterion	Passage by Congress of a tax procedures code that will, inter alia: (i) shift the adjudication of disputes from judicial to administrative procedures, with the payment of most or all of the disputed amount made prior to judicial review of the case; (ii) establish tax fraud and similar violations as a crime, and (iii) adequate rules about the use of sworn tax declarations and application of the statute of limitations.	September 2001
Benchmark	Issue implementing regulations of the new tax procedures code.	End-December 2001
Benchmark	Strengthening the customs administration by: (i) assuring the full funding of the customs agency's budget in the short and long term, and (ii) providing resources to increase the customs unit of the national police to 100 full-time officers.	December 2001
Benchmark	Adapt the public financial management system (SIGMA) for use by ten large municipalities.	August 2001
<i>Financial sector and capital markets</i>		
Performance Criterion	Approve financial sector legislation for strengthening bank resolution procedures and facilitating prompt corrective action for banks with problems.	October 2001
Benchmark	Approve implementing regulations for the law to strengthen the financial system.	December 2001

**Technical Memorandum of Understanding
for the Third Annual Arrangement Under the PRGF**

1. This memorandum sets forth the definitions of the financial and structural performance criteria and benchmarks referred to in the memorandum of economic and financial policies for the third annual arrangement under the PRGF (the "policy memorandum"). The quantitative targets and limits described below for 2001 will be measured as cumulative amounts from **December 31, 2000**.

Financial performance criteria and benchmarks

2. The **deficit of the combined public sector** referred to in Table 1 of the policy memorandum is defined as the sum of the net external financing and domestic financing of the nonfinancial public sector as specified below. The nonfinancial public sector comprises the general government (including the central administration, public sector social security institutions, prefectures, municipalities, and other decentralized government agencies) and the nonfinancial public enterprises.

3. **Net domestic financing of the combined public sector** is the sum of (i) the increase in the net claims of the domestic financial system on the nonfinancial public sector (excluding deposits in the central bank resulting from net disbursements of foreign loans administered by the central bank as trust funds, and including holdings of treasury bills C and time deposits resulting from the assumption of private pension funds as of November 1996); (ii) the cash operating results before distribution to the treasury's account (or losses, as positive financing) of the Central Bank of Bolivia; (iii) all domestic borrowing from the nonfinancial private sector, including the change in domestic holdings of treasury bills C and bonds, and municipal bonds; (iv) the change in the nonfinancial public sector's liabilities to the private sector in the form of fiscal certificates (including, but not limited to, the CEDEIM, papeles D. S. 21060 and NOCREMINFIN); (v) the increase in the domestic floating debt of the nonfinancial public sector, defined as the liabilities incurred for goods and services received but not yet paid for, including public enterprise liabilities to foreign oil contractors, but excluding claims on and liabilities to other entities within the nonfinancial public sector; and (vi) the net increase in any new debt instruments issued by the government. The floating debt with respect to public sector wages as of the end of each month will include unpaid wage increases and wages for work performed during that month that have not been paid in the first 15 days of the following month. Floating debt will include the floating debt of the ten principal municipalities (nine departmental capitals and El Alto).

4. The **net domestic assets of the Central Bank of Bolivia** referred to in Table 1 of the policy memorandum are defined as the (i) currency issue less (ii) the net international reserves of the central bank, as defined in paragraphs 8 and 9 below. Medium- and long-term external

liabilities of the central bank and net credit to the nonfinancial public sector from the central bank exclude net disbursements of foreign loans administered by the central bank as trust funds for the nonfinancial public sector. Net international reserves and medium- and long-term external liabilities will be valued at the accounting exchange rate of Bs 6.58=US\$1 in 2001. Medium- and long-term external liabilities denominated in foreign currencies other than U.S. dollars will be converted to U.S. dollars as established in paragraph 8 below. For purposes of the monetary program, the operations of the *Fondo de Desarrollo del Sistema Financiero* (FONDESIF) are consolidated with the central bank, while net credit to the nonfinancial public sector includes holdings of treasury bills C and net credit to the rest of the financial system and to the nonfinancial private sector includes treasury bills B and D held by these sectors.

5. **External debt with maturities up to one year** referred to in Table 1 excludes normal import credits.

6. **Nonconcessional external debt** referred to in Table 1 consists of all the outstanding external debt of: (i) the nonfinancial public sector as defined in paragraph 2,¹ (ii) the central bank, and (iii) the private sector with official guarantee, excluding: (i) concessional loans with a grant element of 35 percent or more using the most recent OECD commercial interest reference rates (CIRRs) as of April 15, 2001; (ii) changes in central bank liabilities defined in paragraph 7 as part of the net international reserves; and (iii) debt reprogrammed with official creditors.

7. The **external debt** referred to in paragraphs 5 and 6 above will be understood to mean a current (i.e., not contingent) liability created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans (i.e., advances of money to obligor by the lender) made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits) and temporary exchange of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) supplier's credits, i.e., contracts where the supplier permits the obligor to defer payments until some time after the date on which goods are delivered or services are provided; and (iii) leases (i.e., arrangements

¹ The grant element of each loan will be assessed only with regard to: (i) the interest rate and repayment schedule of the loan and (ii) any grants or other concessional loans provided by a foreign official entity in connection to the loan in question.

under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title of the property). For the purpose of this technical memorandum, the debt of a lease arrangement is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement, excluding those payments that cover the operation, repair or maintenance of the property. Under this definition of debt, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under the above definition (e.g., payment on delivery) will not give rise to debt.

8. The **net international reserves of the central bank** are defined as the value of (i) its liquid foreign assets, less (ii) all its liabilities to nonresidents (including swaps and the net position under the LAIA clearing mechanism) with an original maturity of up to and including one year, plus (iii) the outstanding purchases and disbursements from the Fund (excluding disbursements from the trust fund); and (iv) its net liabilities to the Latin American Reserve Fund, including bridging loans (even those obtained by the nonfinancial public sector) and those obtained by pledging the gold of the central bank. Assets and liabilities denominated in foreign currencies other than U.S. dollars will be converted to U.S. dollars at the market exchange rates for the respective currencies in effect at the date of measurement except for: (i) gold, which will be valued at the accounting rate of US\$250.00 per troy ounce; and (ii) SDR holdings and the net Fund position which for the program period will be converted into US\$1.303=SDR 1 for 2001. The following will be excluded from the net international reserves of the central bank: (i) reserve gains resulting from the conversion of monetary gold of the central bank into foreign exchange and (ii) reserve gains resulting from the acquisition of domestically produced gold.

9. The **change in net international reserves of the central bank** referred to in Table 1 of the policy memorandum will be measured by differences in stocks of the net international reserves, as defined in paragraph 8.

10. The **cash operating result of the Central Bank of Bolivia** referred to in paragraph 3 above is defined as revenue less expenditure of the bank on a cash basis (cash losses, if negative). The cash expenditure includes current payments to (i) the International Monetary Fund (excluding repurchases and SAF, ESAF and PRGF loan repayments); (ii) other international organizations (excluding amortization and interest on loans administered by the central bank as trust funds for the nonfinancial public sector); (iii) the domestic commercial banks on account of reserve requirements; (iv) interest on certificates of deposit and treasury bills B and D; (v) operating and financial cash expenses of FONDESIF; and (vi) administrative and other current expenditures. For the purpose of consolidation with the nonfinancial public sector accounts, transfers to the treasury in lieu of operating profits will be excluded from expenditures. The cash revenue includes current receipts from: (i) interest on deposits abroad; (ii) the earnings on the central bank's portfolio with the nonfinancial public

sector and the financial system; (iii) interest payments by the treasury on government paper held by the central bank; (iv) interest on LAIA accounts; (v) commissions and realized foreign exchange gains; (vi) operating and financial cash receipts of FONDESIF; and (vii) other current receipts. Any sale of fixed assets, including the gold of the central bank, will be excluded from revenue.

11. U.S. dollar-denominated debt, or *boliviano*-denominated debt with a maintenance-of-value clause, will be converted into *bolivianos* at an accounting exchange rate of Bs 6.58=US\$1. Debt denominated in other foreign currencies will be converted into U.S. dollars as established in paragraph 8.

Adjusters to the program

12. The program for 2001 assumes that the **currency issued** will amount to the cumulative flows included under "Projected currency issue" in Table 1. The target for net international reserves of the central bank will be adjusted downwards for shortfalls in currency issued up to the designated ceiling on the adjustment.

13. The change in **net external financing of the nonfinancial public sector** is the sum of (i) external disbursements to the sector; (ii) total HIPC debt relief from refinancing operations; (iii) net disbursements of funds for the nonfinancial public sector administered by the central bank as trust funds; (iv) unpaid current interest obligations; less (v) amortization due by the nonfinancial public sector after HIPC debt relief for the amortization component of the stock of debt reduction operations, and (vi) net payments in settlement of the external arrears of the nonfinancial public sector.

14. **HIPC debt relief** referred to in Table 1 of the policy memorandum includes only debt relief from (i) the reduction in amortization that results from the stock of debt reduction operations and (ii) rescheduling. In both cases, HIPC debt relief (under the original and enhanced initiatives) is included.

15. The **limit on the deficit of the combined public sector** described in Table 1 of the policy memorandum shall be reduced (increased) in 2001 by the full amount of the shortfall (excess) between actual and projected HIPC debt relief, as defined in paragraph 14 above.

16. The **limits on the net domestic financing of the nonfinancial public sector** described in Table 1 of the policy memorandum will be adjusted downward in 2001 by the amount of any overdue obligations to foreign official creditors.

17. The **limits on the net domestic financing of the nonfinancial public sector** will be adjusted upward in 2001 by the full amount of the difference between projected cumulative net external financing to the nonfinancial public sector and actual cumulative net external

financing excluding HIPC debt relief, with a maximum cumulative upward adjustment as specified in Table 1, using the accounting exchange rate of Bs 6.58=US\$1. For this purpose, the projected cumulative net external financing to the nonfinancial public sector can be found under "Projected net external financing to the nonfinancial public sector" in Table 1.

18. The **limits on net domestic assets of the central bank** shall be adjusted downward in accordance with the provision of paragraph 16 above.

19. The **limits on the change to the net international reserves of the central bank** shall be increased under the provision of paragraph 16 above and in the event that Bolivia falls behind in its payments by the full amount of overdue obligations to: (i) multilateral organizations; (ii) bilateral official creditors excluding debts covered under Paris Club or other bilateral reschedulings or debts under negotiation including service on rescheduling but excluding old debts to countries in the region; (iii) supplier's creditors without official guarantee excluding already rescheduled debt service to such creditors; and (iv) holders of private bonds excluding zero-coupon bonds used in the debt conversion schemes.

Structural performance criteria and benchmarks

20. To meet the commitment related to customs police, as part of the structural benchmark on strengthening the Customs administration, plans will have been established for increasing the customs unit of the national police to 100 full-time officers through provision in the budget for 2002 for the requisite payroll for the 100 officers, starting in January 2002. It is understood that corresponding actions for the recruitment and hiring of these officers will be taken, consistent with this timetable.

21. The structural benchmark on implementation of the public financial management system (SIGMA) will be met through modifications to the financial management system to be finished, so that the system is ready for implementation in the nine departmental capitals and the municipality of *El Alto* by August 2001.

22. The performance criterion on approval of financial sector legislation will be met through congressional passage of the reforms included in the draft law on the financial system that was before congress as of end-April 2001, with the exception that the introduction of explicit deposit insurance need not be included among the approved reforms.

Statement by the IMF Staff Representative
June 8, 2001

1. This statement contains information which has become available since the staff report was issued (EBS/01/80, 5/25/01). This information does not change the thrust of the staff appraisal.
2. The consumer price index declined by 0.2 percent in May. The 12-month inflation rate rose to 2.1 percent, from 1.0 percent in April, reflecting the sharp decrease in prices in May 2000, when calm was restored following severe social unrest the month before.
3. Net international reserves at end-May were US\$973 million, compared with the program target for end-June of US\$947 million.
4. Commercial banks' portfolios weakened in April, as the share of nonperforming loans rose to 13.4 percent (12.7 percent in March), and nonperforming loans net of provisions increased to 8.8 percent of total loans (8.7 percent in March).
5. The Belgian authorities confirmed that they will provide to Bolivia debt relief beyond the HIPC Initiative as follows: 100 percent of Belgium's pre-cut-off-date claims on Bolivia, and 6 percent of its post-cut-off-date claims. This relief is in addition to the amount indicated in the completion point document (EBS/01/78, 5/23/01, para. 22).
6. On June 7, the Inter-American Development Bank approved financing of debt relief for Bolivia in the framework of the enhanced HIPC Initiative. This approval had been anticipated in the completion point document (para. 18).



INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL
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Public Information Notice (PIN) No. 01/59
FOR IMMEDIATE RELEASE
June 25, 2001

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Bolivia

On June 8, 2001, the Executive Board concluded the Article IV consultation with Bolivia.¹

Background

Bolivia has a long track record of sound macroeconomic policies and substantial structural reforms, which have made it possible to reduce inflation to low single digits, strengthen the balance of payments, and attain real GDP growth of 4 percent a year during the 1990s. The public sector deficit averaged 3–4 percent of GDP during this period, rising in the latter part of the decade as a result of the 1997 pension reform; the cost of replacing the pay-as-you-go pension system with capitalized private pension funds—a reform with long-term benefits in terms of a sustainable fiscal position—averaged 3½ percent of GDP in 1997–99, and exceeded 4 percent of GDP in 2000. Foreign direct investment rose sharply during the latter part of the 1990s, and gross international reserves increased to 7½ months of imports. Bolivia's structural adjustment program has included extensive privatization of public enterprises, financial sector liberalization, independence and recapitalization of the central bank, fiscal decentralization, and trade liberalization. However, poverty is still widespread, with nearly two-thirds of the population living below the poverty line as of 1999.

External shocks and weak domestic demand resulted in the stagnation of the economy in 1999, when real GDP growth fell to 0.4 percent. A sharp depreciation of the Brazilian real and falling commodity prices led to a decrease in exports, while the successful coca eradication program resulted in a permanent decline in incomes in the informal sector of 3 percent of annual GDP or more, adversely affecting domestic demand. Inflation declined to 3.1 percent during 1999, the lowest annual rate achieved in over 30 years.

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. This PIN summarizes the views of the Executive Board as expressed during the June 8, 2001 Executive Board discussion based on the staff report.

The economic recovery in 2000 was weaker than expected (2.4 percent growth of real GDP), owing to the sluggish domestic demand. Coca eradication continued to reduce incomes in the informal sector, while periods of social unrest temporarily disrupted transportation throughout the country, causing production losses and temporary increases in consumer prices. Inflation was held to 3.4 percent for the year as a whole. The fiscal deficit widened modestly in 2000 (to 3.7 percent of GDP), owing in part to a tax revenue shortfall and an economic stimulus package of selected tax breaks and emergency spending measures. The external current account deficit narrowed in 2000 to 5½ percent of GDP as exports staged a strong recovery, led by natural gas and soybeans. A substantial improvement in the net foreign asset position of the banks contributed to a lower financial account surplus.

Some important advances were achieved in the areas of tax administration and budget management in 2000, aimed at improving transparency and governance. The reforms of the customs and domestic tax administrations, and the expected passage of the tax procedures code presently being considered by congress, are expected to improve efficiency significantly and strengthen tax collections. Of other structural reforms that are under way, financial sector reforms included in a draft law currently before congress are among the most important.

The banking system has contracted since late 1999. Broad money and credit to the private sector both fell in U.S. dollar terms during 2000 (Bolivia's financial system is highly dollarized), and the share of nonperforming loans net of provisions has risen to some 8½ percent at end-March 2001. To encourage bank lending, the government introduced measures in 2000 that offered regulatory forbearance on rescheduled loans and low-cost funds and loan guarantees from a state-owned second-tier bank (NAFIBO). In May 2001, the government approved a measure allowing NAFIBO to provide credit to banks—to further encourage them to reschedule loans—up to a total of US\$250 million, or 3 percent of GDP, and to issue subordinated credits to encourage bank recapitalization.

In February 2000, the Boards of the IMF and IDA agreed that Bolivia was eligible for debt relief of US\$854 million in net present value (NPV) terms under the enhanced HIPC framework, which is additional to the assistance of US\$448 million in NPV terms that Bolivia received under the original framework in September 1998. In 2000, conditions for the floating completion point under the enhanced framework were established, according to which Bolivia would maintain sound economic policies and develop a comprehensive poverty reduction strategy in the context of a broad participatory process. The National Dialogue 2000 on poverty reduction entailed extensive participation by civil society and local governments, and much of the Dialogue's main conclusions are contained in the Bolivian poverty reduction strategy paper (PRSP), which was published in March 2001. The overall goal of the PRSP is to reduce the incidence of poverty by a third and extreme poverty by a half, by 2015.

The authorities' economic program assumes real GDP growth of 4 percent, led by a further expansion of natural gas exports and a pickup in domestic demand, and inflation of 4-4½ percent during the year. The fiscal deficit is programmed to remain at 3.7 percent of GDP, two-thirds of which is to be financed with concessional external credits. The program projects a recovery in broad money and in bank lending activity, and the external current account deficit is projected to be about unchanged in relation to GDP. Net international

reserves would be allowed to decline by US\$100 million during the year, with a comfortable level of gross reserves at the year's end, equivalent to 5½ months of imports of goods and services.

The structural reforms programmed for 2001 are focused primarily on tax and customs administration, budget management, and fiscal decentralization, with the aim of enhancing transparency, improving the monitoring of expenditure, particularly for local governments, and increasing tax revenue. The authorities also will seek congressional approval of financial sector reforms.

Executive Board Assessment

Executive Directors commended Bolivia for its prudent macroeconomic policies, which have made it possible to achieve low inflation, advance toward a sustainable external position, and realize moderate economic growth and per capita income gains in the 1990s. However, Directors expressed concern about the recent slowdown in economic activity, and noted that progress in lowering poverty has been limited. Nevertheless, they welcomed the authorities' commitment to give greater priority to poverty reduction, as set out in the PRSP.

Directors considered that the protracted sluggishness of economic activity over the past two years is having adverse effects on employment and poverty and on social spending. They noted the weakness in the economy, which appears to have been caused in part by the large decrease in informal sector incomes arising from the successful coca eradication program and the slowing of contraband trade in the wake of the customs reform. Directors encouraged the authorities to maintain sound macroeconomic policies in order to foster greater confidence, while also protecting social spending for the highest priorities set out in the PRSP.

Directors noted the importance of increasing public sector savings, mainly through substantially higher tax revenues over the medium term, for achieving planned public investment levels while narrowing the fiscal deficit. However, the lack of concrete policy measures in this area was a weakness that needs to be addressed. They emphasized that this will require significant tax reform, in addition to planned improvements in tax administration, to enhance the revenue-generating capabilities of the tax system as well as to increase its efficiency and progressivity. In this regard, Directors welcomed the proposed improvements to the tax code that are currently before the congress. Some Directors encouraged the rapid development of greater revenue generating capacity for the local governments, to strengthen fiscal decentralization.

Directors considered the weakening of bank performance indicators, including the rise in nonperforming loans since 1999, to be a symptom of the economic slowdown. They noted that there were some mitigating factors that would help banks to withstand stress, such as increases in capital and in loan-loss provisions, a substantial improvement in banks' net foreign asset position, and stricter prudential rules on loan classification. Nevertheless, Directors stressed the need for close monitoring by the banking superintendency, and in this regard, underscored the importance of early passage of financial sector legislation that would facilitate prompt corrective action for banks with problems and a strengthening of bank

resolution procedures. A number of Directors expressed concern about the implications of measures to foster the rescheduling of bank loans, both for their potential fiscal costs and because of potential moral hazard.

Directors observed that there had been delays with the structural agenda over the last couple of years, and stressed the importance of advancing expeditiously with fiscal reforms. They recognized the need to strengthen public administration and improve governance, and to improve the efficiency of customs and domestic tax administrations, including through the prompt passage of the tax procedures code now in congress. Directors expressed concern that the tax and labor market reforms have been delayed for a year, and hoped that they would be brought back into the reform agenda as soon as possible. They also stressed the need to implement planned improvements in fiscal monitoring by local and regional governments, and to build up capacity for effective budget management and expenditure control.

Directors agreed that the current exchange rate regime was appropriate in Bolivia's circumstances, as it allowed for adaptation to terms-of-trade and other external shocks. Several Directors suggested, however, that an in-depth study of the exchange rate regime be undertaken to shed more light on its future appropriateness. Directors encouraged the authorities to monitor exchange rate developments, and to be prepared to respond to changes in the external environment with changes in the rate of crawl, if needed. Monetary policy was seen to be prudent and consistent with the price and balance of payments objectives of the authorities. They welcomed the open trade and payments system, and commended the authorities on the improvements in customs procedures that place Bolivia among countries with more open trade regimes.

Directors observed that, owing to improvements in data on municipal debt, the fiscal data for 1998 were revised, leading the authorities to conclude that the performance criteria for the fiscal deficit and domestic financing for that year were not observed, as previously believed. Directors welcomed the improvements in data collection and indicated that these revisions did not affect their assessment of Bolivia's policy performance. They encouraged the authorities to improve the timeliness of statistics on the national accounts, and to strengthen the reporting of labor market statistics, particularly on unemployment.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board. The staff report for the 2001 Article IV Consultation with Bolivia is also available.

Bolivia: Selected Economic Indicators

	1997	1998	1999	2000
(Annual percentage change)				
Income and prices				
Real GDP	5.0	5.2	0.4	2.4
Real domestic demand	7.7	6.6	-1.8	1.6
CPI inflation (end-of-period)	6.7	4.4	3.1	3.4
(In percent of GDP)				
Investment and savings				
Gross domestic investment	19.6	23.1	18.9	18.8
Gross national savings	12.6	15.3	13.0	13.3
Combined public sector				
Overall balance	-3.3	-4.6	-3.4	-3.7
Foreign financing	2.7	2.7	1.9	1.9
Domestic financing	0.5	1.9	1.5	1.7
(Annual percentage change, unless otherwise indicated)				
Money and credit				
M3	17.3	13.7	4.2	3.4
Credit to private sector	19.2	23.8	4.1	-2.6
External sector				
Current account balance (US\$ million)	-553	-667	-488	-464
(percent of GDP)	-7.0	-7.8	-5.9	-5.5
<i>Of which:</i> trade balance	-684	-879	-704	-600
Capital and financial account balance	656	792	515	425
<i>Of which:</i> foreign direct investment	876	955	1,014	731
Overall balance	103	125	26	-39
Exceptional financing	0	3	16	16
Gross official reserves 1/	7.6	7.2	7.0	6.6
Public sector external debt (US\$ billion) 2/ 3/	4.5	4.7	4.6	4.4
(percent of GDP) 2/ 3/	56.6	54.7	54.9	51.8
Debt-service ratio 2/ 3/ 4/	25.2	28.6	19.0	18.4

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

1/ In months of imports of goods and services in the following year. Does not include Bolivia's capital contribution to the Latin American Reserve Fund.

2/ Debt and debt service reflect original HIPC assistance, which became available in 1998.

3/ Includes obligations to the Fund and debt with public guarantee.

4/ Debt service on public sector medium- and long-term external debt, in percent of exports of goods and services.



Press Release No. 01/30
FOR IMMEDIATE RELEASE
June 8, 2001

International Monetary Fund
Washington, D.C. 20431 USA

IMF Approves Third Annual PRGF Loan for Bolivia

The International Monetary Fund (IMF) today approved the third annual program for Bolivia under the Poverty Reduction and Growth Facility (PRGF)¹ in an amount equivalent to SDR 56.1 million (about US\$70 million) to support the government's economic program.

Bolivia's three-year program, originally under ESAF, was first approved on September 18, 1998 (see Press Release 98/41), in an amount equivalent to SDR 100.96 million (about US\$126 million), of which SDR 44.86 million (about US\$56 million) has been disbursed. Today's decision provides Bolivia with another SDR 56.1 million to be disbursed in two drawings of SDR 19.0 million (about US\$23.7 million), the first of which is available immediately, and a third drawing of SDR 18.1 million (about US\$22.6 million).

In a separate decision, the IMF Executive Board has agreed that Bolivia has met the conditions for reaching the completion point under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative. The Executive Board has also broadly endorsed Bolivia's Poverty Reduction Strategy Paper, which should provide the policy framework for future reviews under this PRGF loan (see Press Release 01/29).

In commenting on the Executive Board discussion on Bolivia, Shigemitsu Sugisaki, Deputy Managing Director, said:

"Bolivia is to be commended for its track record of sound macroeconomic policies and substantial structural reforms, which has made it possible to lower inflation, strengthen the

¹ On November 22, 1999, the IMF's concessional facility for low-income countries, the Enhanced Structural Adjustment Facility (ESAF), was renamed the Poverty Reduction and Growth Facility (PRGF), and its purposes were redefined. It is intended that PRGF-supported programs will in time be based on country-owned poverty reduction strategies adopted in a participatory process involving civil society and development partners, and articulated in a poverty reduction strategy paper (PRSP). This is intended to ensure that each PRGF-supported program is consistent with a comprehensive framework for macroeconomic, structural, and social policies to foster growth and reduce poverty. PRGF loans carry an interest rate of 0.5 percent a year, and are repayable over 10 years with a 5½-year grace period on principal payments.

balance of payments, and attain real GDP growth of 4 percent a year during the 1990s. However, there was a sharp economic slowdown in 1999, and poverty is still widespread. Despite a strong export performance, the economic recovery in 2000 was weaker than expected owing to sluggish domestic demand.

“The authorities are to be commended for their efforts in conducting a widely participatory process for the development of a comprehensive poverty reduction strategy, which Directors have endorsed as providing an overall context for the Fund’s assistance to Bolivia. The goal of reducing the incidence of poverty and extreme poverty by one-third and one-half, respectively, by 2015 is ambitious, but achievable. In addition to stepped-up poverty-related spending, strong economic growth over the medium and long term, anchored by sound macroeconomic policies and sustained structural adjustment, will be required to meet these targets.

“The authorities’ economic program for 2001 will be supported by the third annual arrangement under the current three-year PRGF commitment. The program calls for the continuation of macroeconomic policies designed to encourage a stronger economic recovery while keeping inflation under control; well-focused structural reforms, including a reform of the domestic tax agency, a new tax procedures code, and early passage of key elements of financial sector legislation; and increased resources devoted to stepping-up the fight against poverty. Additional debt relief provided under the enhanced HIPC framework will contribute to this strengthened effort to reduce poverty.

“The authorities will need to take appropriate revenue and spending measures to close any fiscal gap that may arise from revenue shortfalls or unbudgeted expenditure, in order to meet the program’s fiscal targets. At the same time, it will be important to maintain the levels of poverty-related expenditure that are needed for the successful implementation of the poverty-reduction strategy.

“The authorities also should avoid further recourse to measures in support of the banking system that increase regulatory forbearance, since such measures may postpone both the detection of bank problems and the timely corrective action needed to address them. In this regard, the proposed financial sector reforms take on added importance”, Sugisaki said.

Program Summary

Bolivia's economic recovery in 2000 was weaker than expected, due to the sluggish economic growth of domestic demand. Real GDP grew by 2.4% despite strong export volume growth, as real domestic demand is estimated to have grown by only 1.6%. The virtual elimination of illicit coca cultivation over the last two to three years, as well as the customs reform, which reduced commercial activity based on contraband imports, may have contributed to lower the incomes in the informal sector. Despite pressure on domestic fuel prices in the first half of the year, inflation remained subdued in 2000, rising slightly to 3.4%.

Fiscal discipline was maintained, although an expected increase in tax revenues failed to materialize, reflecting the weak economy, delays in the implementation of tax and tax administration measures, and lost revenue from tax breaks. Contrary to projections, the external account deficit narrowed to 5.5% of GDP in 2000, owing to an export growth of 11%.

The program for 2001 is based on the government's Poverty Reduction Strategy Paper (PRSP), which incorporated the main conclusions of the National Dialogue on poverty reduction, held between June and August of 2000. The program is based on real GDP growth of 4%, led by a further expansion of natural gas exports and a pickup in domestic demand. The inflation target for 2001 was set at 4%.

The fiscal program for 2001 seeks to achieve a balance between the need for further fiscal consolidation over time, as expressed in the PRSP, and the objective of avoiding a fiscal tightening during the present period of weak domestic demand. The fiscal deficit is expected to remain unchanged at 3.7% of GDP. Revenue gains will result from the impact of tax administration reforms on the efficiency of domestic tax collections, increased fuel taxes and improved collections by customs. The government also intends to prepare a proposal for a comprehensive tax reform, which would be ready for consideration by the next government.

The monetary policy will be guided by the inflation objective for 2001. To address a weakening in the banking system, due to a rise in non-performing loan ratios, measures were introduced on May 2001, providing credits to encourage banks to reschedule loans and subordinated loans for recapitalization.

The external account deficit in 2001 is projected to remain stable and the authorities intend to continue with the crawling peg exchange rate policy, with the aim of maintaining internal price stability and improving external competitiveness.

The structural reforms programmed for 2001 are focused primarily on tax and customs administration, budget management, and fiscal decentralization, with the aim of enhancing transparency, improving the monitoring of expenditure, particularly for local governments, and increasing tax revenue. The authorities also plan to complete the privatization program, by

offering for sale three electricity generation and distribution companies in 2001, and will seek congressional approval of new regulations to strengthen banking supervision.

PRSP Process

The authorities will begin to implement their new poverty reduction strategy over the second half of the 2001. This comprehensive strategy, which aims to reduce the incidence of poverty and extreme poverty by one-third and one-half, respectively, by 2015, will be partly supported by assistance provided by HIPC debt relief.

Bolivia joined the IMF on December 27, 1945; its quota² is SDR 171.5 million (about US\$214 million). Bolivia's outstanding use of IMF credits totals SDR 165.1 million (about US\$206 million).

² A member's quota in the IMF determines, in particular, the amount of its subscription, its voting weight, its access to IMF financing, and its allocation of SDRs.

Bolivia: Selected Economic Indicators

	1997	1998	1999	2000	Prog. 2001
(Annual percentage change)					
Income and prices					
Real GDP	5.0	5.2	0.4	2.4	4.0
Real GDP per capita	2.5	2.8	-1.9	0.0	1.8
Real domestic demand	7.7	6.6	-1.8	1.6	2.5
GDP deflator	5.7	7.3	3.0	5.5	4.3
CPI inflation (period average)	4.7	7.7	2.2	4.6	3.7
CPI inflation (end-of-period)	6.7	4.4	3.1	3.4	4.0-4.5
(In percent of GDP)					
Investment and savings					
Gross domestic investment	19.6	23.1	18.9	18.8	19.5
Public	7.2	7.0	7.1	7.0	7.1
Private, including stockbuilding	12.4	16.1	11.8	11.8	12.4
Gross national savings 1/	12.6	15.3	13.0	13.3	14.0
Public	3.0	1.7	2.8	2.7	3.1
Private	9.7	13.6	10.2	10.6	10.9
Combined public sector 1/					
Nonpension balance	-0.8	-0.7	0.6	0.7	0.6
Pension-related balance	-2.5	-4.0	-4.1	-4.4	-4.3
Overall balance	-3.3	-4.6	-3.4	-3.7	-3.7
Foreign financing	2.7	2.7	1.9	1.9	2.5
Domestic financing	0.5	1.9	1.5	1.7	1.2
(Annual percentage change, unless otherwise stated)					
Money and credit					
Broad money (at current exchange rates)	17.3	13.7	4.2	3.4	7.7
Credit to private sector (at current exchange rates)	19.2	23.8	4.1	-2.6	7.9
Interest rates (percent, end-of-period)					
Lending rate in U.S. dollars	15.6	15.6	16.3	15.3	...
Yield on treasury bills in local currency	11.2	12.2	12.2	13.2	...
Yield on treasury bills in U.S. dollars	8.2	8.6	8.6	8.8	...
External sector (US\$ million) 1/ 2/					
Current account	-553	-667	-488	-464	-471
(Percent of GDP)	-7.0	-7.8	-5.9	-5.5	-5.4
Capital and financial account	656	792	515	425	316
Of which: foreign direct investment	876	955	1,014	731	778
Overall balance	103	125	26	-39	-155
Exceptional financing 3/	0	3	16	16	10
Merchandise export volume, percent change	4.3	4.1	-1.8	11.4	4.2
Merchandise import volume, percent change	25.5	16.0	-8.8	-0.1	0.0
Terms of trade, percent change (deterioration -)	2.9	-1.6	-0.2	0.6	0.1
Gross official reserves 4/					
(Months of imports of goods and services)	7.6	7.2	7.0	6.6	5.6
(In percent of broad money)	39.8	31.3	32.5	32.2	28.5
Public sector external debt (US\$ billion) 5/ 6/	4.5	4.7	4.6	4.4	4.5

(Percent of GDP) 5/ 6/	56.6	54.7	54.9	51.8	52.2
Debt-service ratio 5/ 6/ 7/	25.2	28.6	19.0	18.4	16.7
End-of-period exchange rates					
Bolivianos/U.S. dollar	5.37	5.65	6.00	6.38	...
Nominal effective rate (percentage change) 8/	0.8	-0.5	1.5	-1.9	...
Real effective rate (percentage change) 8/	1.3	3.8	1.4	-1.5	-3.0

Sources: Central Bank of Bolivia; ministry of finance; and Bank/Fund staff estimates and projections.

1/ Includes actual and anticipated assistance under the HIPC Initiative, using the new HIPC accounting conventions.

2/ For the 2001 external sector figures, enhanced HIPC assistance is presented as closing the financing gap.

3/ Includes grants for debt-reduction operations in effect prior to July 2000 and rescheduling operations under the original HIPC framework.

4/ Does not include Bolivia's capital contribution to the Latin American Reserve Fund. Import coverage for the following year.

5/ Debt and debt service reflect assistance under the HIPC Initiative, of which the original became available after September 1998.

6/ Includes obligations to the Fund and debt with public guarantee.

7/ On public sector medium- and long-term external debt (including payments to the Fund) in percent of exports of goods and services.

8/ Weights based on average trade, excluding trade related to natural gas, in 1996-97.

**Statement by A. Guillermo Zoccali, Executive Director
and Rodolfo Maino, Assistant
for Bolivia
June 8, 2001**

Overview

1. The Bolivian economy exhibited remarkable macroeconomic stability during more than fifteen years, with economic growth averaging 4.2 percent in the 1990s, with a sharp reduction in the rate and volatility of inflation, and with a significant surge in foreign direct investment—now exceeding 10 percent of GDP. The severe slowdown in 1999, when real GDP grew by only 0.4 percent was affected in no small measure by a number of external shocks which, among others, included a significant deterioration in Bolivia's terms of trade,—the sluggish economic activity in Argentina—that resulted also in lower remittances by Bolivian nationals—and the continuous depreciation of the Brazilian real during this period. Additionally, Bolivia was hit by floods in the eastern part of the country significantly affecting its agriculture production.

2. Strong program ownership, anchored on a track record of sound fiscal policy, the stepped-up in efforts to reduce poverty and a comprehensive program of structural reforms have resulted in regained fiscal responsibility and a domestic environment more favorable to investment and sustainable real GDP growth. These undertakings have led to a revamping of the role of the state, an ambitious privatization drive and reform of the pension system, the elimination of subsidized credits, the closing down of state banks, and a more open economy with zero tariffs for capital goods imports. Concurrently, the government prioritized an ambitious social agenda known as the 1997 National Action Plan. This was based on the first National Dialogue aimed at improving the participatory process and creating opportunities for economic growth, reducing poverty, strengthening institutions, addressing corruption and consolidating dignity by getting Bolivia out of the drug circuit in 2002. The Bolivian Poverty Reduction Strategy heavily relies on the reduction of the combined public sector deficit to less than 0.5 percent of GDP by 2008 and on improving the prospects for sustainable growth. The participatory process over the last two years was broadened in a second National Dialogue that included far-reaching discussions of civil society's main concerns for effective poverty alleviation at the local, regional and national levels. The 2000 National Dialogue targets indigenous groups and is built on two strategic pillars, namely, supporting productive activities and improving the quality of basic services.

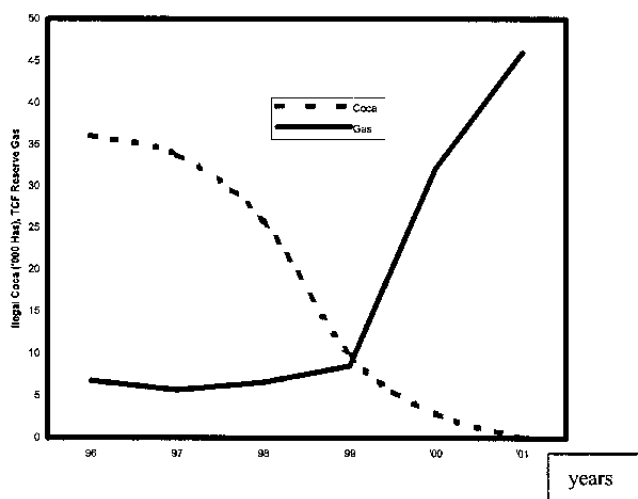
3. Our Bolivian authorities are committed to reducing the incidence of poverty by a third and to halving extreme poverty by 2015. In this regard, they are in general agreement with the thrust of the diagnosis and policy recommendations in the staff report. The government is making utmost efforts not only to maintain macroeconomic stability but to obtain broad support to implement the last stages of several key reforms, aimed at modernizing the tax code and labor market relations. The structural reform process is amply described by staff in the PRGF and the Enhanced HIPC Initiative reports and the continued support of the international community is

critical to its success. Therefore, our comments are aimed at providing selective insight and emphasis.

Developments under the 2000 program

4. Although the recovery in 2000 was slower than expected, with real GDP growing 2.4 percent due to the persistence impact of negative shocks on domestic demand, the government maintained macroeconomic stability, safeguarded the social safety net and made progress in the structural area. In addition to adverse external circumstances, the stagnation of domestic demand and the manifestations of social instability may be ascribed to the fall in income in the informal sector from the successful campaign of coca eradication, the reduction in contraband-based commerce following the customs reform, and the organized opposition to the health care privatization. The eradication of coca production alone produced a loss of income in the informal sector of more than 3 percent of GDP per year in 1999 and 2000, and its recovery will be gradual, as other crops replace illicit coca cultivation. What is important is that this was accompanied by reforms aimed at strengthening the incentives for production in the formal economy and at reducing distortions and curtailing rent-seeking activities.

5. The investment plans and prospects of foreign companies in mining, telecommunications, hydrocarbons, water and energy provide grounds for optimism regarding the prospects of a rapid recovery. By way of examples, estimates of proven gas reserves in Bolivia increased six fold, when compared to the 1999 levels, and exports in 2000, led by increased sales of natural gas to Brazil, rose by 11.4 percent. The pro-market and anticorruption measures adopted by our Bolivian authorities described by Vice President Quiroga in his recent presentation to the Executive Board, may best be summarized by the following graph depicting the economy's changing production composition.



6. In spite of the sharp decline in mineral, agricultural and other international commodity prices, Bolivia's external current account deficit in 2000 narrowed to 5.1 percent of GDP, mostly financed by FDI (hydrocarbons). This downward trend and its financing modality, principally

FDI, are expected to continue with exports of natural gas and soybean volumes reaching new highs and with the significant investment planned in the San Cristobal mining project—one of the world's largest zinc-silver deposits. In addition, Bolivia's public external debt, which is largely long term and concessional, is declining from an average of 71 percent of GDP in 1990-97 to some 52 percent at end-2000. Moreover, important structural reforms are underway. The modernization and restructuring of the public sector administration, the deepening of the decentralization process, the strengthening of the financial sector, including banking system supervision, and the increasing access to pension fund resources, should crowd in needed private investment to sustain strong growth and the poverty reduction strategy.

The profound structural changes, already implemented, that include financial and trade liberalization, divestiture of public enterprises, the establishment of an independent central bank, the popular participation and decentralization reform, and the implementation of an independent regulatory framework, all serve to underpin a convergent debt dynamics consistent with the objective of securing external sustainability and reducing net domestic financing requirements.

7. During the first quarter of 2001, inflation remained subdued and the overall fiscal deficit declined. Net international reserves stood at US\$950 million—equivalent to almost 6 months of imports of goods and services—while non-performing loans, net of provisions, rose to some 8 percent of total loans due to the weak domestic demand conditions prevailing last year. The strength of the recovery, however, will be affected by economic activity in neighboring countries, especially Brazil, the level of mineral production from newly discovered mines (zinc, plumb and silver), the growth of non-traditional exports, the evolution of the terms of trade, and by the degree of access of Bolivian exports to developed country markets.

The Financial System

8. The economic slowdown of the past two years was accompanied by a fall in private sector credit. This outcome was affected significantly by the ongoing balance sheet restructuring of the country's largest bank after its acquisition by a foreign financial institution, as well as by the combination of stricter prudential regulations and more conservative lending practices. While non-performing loans increased in 2000, loan-loss provisions were substantially reinforced and the ratio of qualifying capital to total risk-adjusted assets increased markedly.

9. Deepening financial sector reforms constitutes a heightened priority of our authorities. In this regard, they remain committed to a strong and independent central bank, the prudent conduct of monetary policy, aimed at low inflation through base money expansion consistent with nominal GDP growth, and to an effective banking superintendency. Demand for domestic currency deposits and credit to the private sector, both in domestic and foreign currency, are expected to recover by 7 percent in 2001 as the balance sheet restructuring concludes and growth picks up. The end-2000 financial benchmarks of the program are in the process of being completed, while the Congressional approval of the bill establishing a comprehensive bank resolution framework, which is a structural performance criteria for 2001, is expected to be approved by October and regulations on securitization and development of a secondary housing mortgage market have already been issued.

The aforementioned bill aims at strengthening the internal control mechanisms for the financial sector, at reinforcing the role of the Superintendency, at allowing banks to be intervened in a timely manner, and at detecting banks' problems by relying on early warning signals and other macro prudential indicators. The intention is to advance a consolidated banking supervision framework and to enforce fully the strengthened prudential regulations. At the same time, our Bolivian authorities are giving further consideration to the deposit insurance, in particular the appropriate size of the guarantee and the funding modality of the scheme, to avoid unsettling depositor confidence by moving towards international best practices.

10. Regarding exchange rate policy, the central bank will continue to control the expansion of net domestic assets and intervene daily in the foreign exchange auctions. Bolivia aims at safeguarding its external competitiveness by maintaining a crawling peg mechanism that helps to adjust to terms of trade shocks while avoiding excessive volatility in a highly dollarized financial environment.

The Fiscal front

11. In its efforts to jump-start growth, a new set of economic initiatives and extraordinary fiscal measures were enacted since end-1999 with the support of the Congress. On the revenue side, the government introduced specific tax breaks. These growth-enhancing measures also included a zero tariff on imported capital goods from outside the Andean Community. The strategy for growth, that includes a clear supply-side component, should lend further stimulus to the economy in 2001 and help address concerns voiced by various sectors during a recent period of social unrest.

12. Additionally, the government launched labor-intensive public work programs in the municipalities—an employment initiative directed at unskilled workers—and other temporary spending measures, including the acceleration of public capital spending. Commercial bank reschedulings, on an individual basis, of outstanding loans to clients with the capacity to repay, were also encouraged. The latter involved the creation of a Special Fund for Economic Reactivation (FERE) to grant credits to those banks that are voluntarily reprogramming loans. The Bolivian authorities have clearly affirmed, however, that the banks are responsible for the credit risk, and the program is being monitored closely by the Superintendency of Banks. These proactive financial policies, implemented within the constraints of the PRSP framework, helped to maintain the level of gross domestic investment at almost 19 percent of GDP. Investment is expected to increase further in 2001, based on the growth in hydrocarbon and agro-industrial exports and the strengthening of real domestic demand, without affecting poverty-related expenditure.

13. Fiscal discipline in 2000 was maintained, despite the measures taken to stimulate the economy. Tax revenue rose to 18.5 percent of GDP, while current spending was kept under control by limiting the public wage bill increase. To mitigate the effect of the surge in world oil prices during the downturn in economic activity, the government temporarily lowered taxes on fuel and derivatives, producing a small revenue loss. The behavior of excise taxes partly compensated for this effect. The fiscal deficit is projected to decline steadily from 3.7 percent of

GDP in 2001 to 3.0 percent in 2003, as a result of the implementation of the tax initiatives being considered in the Congress and the reforms to strengthen the tax and customs administrations. In this context, it is worth keeping in mind that the overall public sector balance would show a surplus of 0.7 percent of GDP in 2001 were it not for the costs of the 1997 pension reform.

14. The transformation of the transitional social security system continues to exert considerable pressure on the overall fiscal balance. Pension liabilities of the national government are reflected in the consolidated public sector budget, and should continue to place a heavy burden on the medium-term fiscal performance keeping in mind that social security contributions are being channeled to privately-administered pension funds and, hence, are no longer available to finance the pay-as-you-go system. It is also worth noting that the pension related balance is estimated to absorb 4.3 percent of nominal GDP in 2001, and will remain around that level until 2008. Nevertheless, this reform should contribute to fostering savings, deepening the domestic capital market and lowering the country's vulnerability to volatile capital flows.

15. To advance fiscal consolidation, our authorities are prioritizing the new tax procedures code, which is a structural benchmark under the program. It is aimed not only at improving transparency and eliminating distortions, but also at strengthening the enforcement powers of the tax and custom administrations in several important respects:

- Disputes settlement over tax liabilities;
- Tax fraud penalties;
- Enhanced status of tax declarations and restrictions to the statute of limitations.

The tax code was approved by the Senate and is now being considered by the Chamber of Deputies. The political agreement entails resolution of this issue before any other legislation can be considered, and if needed an extraordinary session of Congress would be convened. Approval is expected by end-August.

16. Tax enforcement will also be reinforced by the ongoing revamping of the Internal Revenue Service, that includes appointment of an independent board of directors, the removal of political influence in the selection of staff, and the establishment of a career system with competency examination for the recruitment of professionals on the basis of merit.

17. The customs reform should, similarly, contribute to revenue gains, especially in the VAT, excise and hydrocarbon taxes on imports. Modern control mechanisms, such as an automated transit control system, magnetic cards, and a computerized customs control system are expected to become fully operational by end-2001 for export, import and transit regimes. To ensure progress, on this structural benchmark, the government is assigning the Customs Administration Authority a fixed percentage of the collection of taxes on imports and providing additional budgetary resources to increase the customs unit of the national police.

18. The quantitative and financial performance criteria for the Second Annual Arrangement under the current PRGF were met. The small modification of the program ceilings for the overall fiscal deficit and net domestic financing of the combined public sector last July responded to the

higher than expected cost of the pension reform program and the emergency employment program enacted by the government.

Structural Area

19. Despite delays in fulfilling several structural objectives, the progress made is encouraging keeping in mind the ambitiousness of the 25 structural performance criteria or benchmarks in the program. The Customs Law was implemented successfully, and the Internal Revenue Service reform law was passed by congress last December. Privatizations and the sale of several companies (Vinto, Milka, refineries, storage facilities and fuel stations of the state-owned oil company, YPFB) were completed as announced in 2000. Most benchmarks for the present review have been satisfactorily met, and the consultation process leading the reform of labor market legislation was initiated. In this regard, draft labor legislation is expected to be taken up by the next government following national elections in June 2002. The Bolivian government also offered in concession the operation of the postal service (ECOBOL), the electricity generation and distribution company of Potosi (SEPSA) and the electricity generation company of Trinidad. The government expects to sell the electricity distribution company of Tarija (SETAR) in 2001.

Enhanced HIPC Initiative and PRSP for Bolivia

20. Our Bolivian authorities are grateful to the international community for the debt relief provided in September 1998, bringing the NPV of debt-to-export ratio, on an ex-post basis, including Official Development Assistance relief from Japan, to about 200 percent as of end-2000.

21. Bolivia's eligibility last February for additional debt relief under the Enhanced HIPC Initiative would lower its NPV debt-to-export ratio further, to 150 percent. Reaching completion point under the Enhanced HIPC Initiative is thus deemed critical to sustain the poverty reduction effort. The willingness of several Paris Club creditors to consider possible additional debt relief to Bolivia constitutes a welcomed recognition of the seriousness of the adjustment and reform effort to date, as well as an incentive to adhere to the path of policy implementation and social investments notwithstanding the prevailing regional uncertainties.

22. The poverty reduction measures implemented, as well as future enhancements in the fight against poverty, are supported by the PRSP and the National Dialogue Law, which are the basis for Bolivia's sustainable development. In turn, these rest on five main pillars:

- Participation (ownership)
- Decentralization of social and productive services
- Progressive resource allocation criteria
- Social control by beneficiaries and civil society to ensure effectiveness and impact
- Institutional strengthening at all levels of government

23. Our final remarks refer to two critical issues, namely, transparency and publication.
- Two reviews of the program will be conducted no later than October 31, 2001 and March 31, 2002 to gauge the macroeconomic framework and to take into account the impact of additional debt relief that may be granted under the Enhanced HIPC Initiative. Our Bolivian authorities are grateful for the close and effective policy dialogue maintained with Fund staff and management and will consult with the Fund whenever necessary in light of changing economic and financial developments. Our authorities have systematically taken the lead in the dissemination of all relevant documentation related to the economic policy framework and undertakings with the international community and civil society pertaining to the poverty reduction effort. As a further demonstration of ownership and commitment to full transparency, they have authorized the publication of all the reports prepared by Fund staff relating to the 2001 Article IV consultation, the program for the third annual arrangement under the PRGF, as well as the reports prepared jointly with World Bank staff concerning the completion point under the Enhanced HIPC Initiative and the Poverty Reduction Strategy Paper (PRSP).
 - Bolivia is in compliance with the safeguards framework. The *Banco Central de Bolivia* has provided Fund staff with independently audited financial statements and related audit reports of the external auditors as well as management letters issued by them in accordance with current auditing standards.