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Bolivia: 2003 Article IV Consultation, First Review Under the Stand-By Arrangement, and Request for Waiver of Performance Criteria—Staff Report; Staff Supplement; Public Information Notice and Press Release on the Executive Board Discussion; and Statement by the Executive Director for 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 2003 Article IV consultation with Bolivia, first review under the Stand-By Arrangement, and request for waiver of performance criteria, the following documents have been released and are included in this package:

- the staff report for the combined 2003 Article IV Consultation, first review under the Stand-By Arrangement, and request for waiver of performance criteria, prepared by a staff team of the IMF, following discussions that ended on **May 21, 2003**, 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 June 24, 2003**. 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 supplement of **July 3, 2003** updating information on recent economic developments.

- a Public Information Notice (PIN) and Press Release, **summarizing the views of the Executive Board as expressed during its July 7, 2003 discussion** of the staff report on issues related to the Article IV consultation and the IMF arrangement, respectively.

- a statement by the Executive Director for Bolivia.

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

Letter of Intent sent to the IMF by the authorities of Bolivia*
Supplementary Memorandum of Economic Policies by the authorities of Bolivia*
Selected Issues Paper and Statistical Appendix

*May also be included in Staff Report

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

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

BOLIVIA

Staff Report for the 2003 Article IV Consultation, First Review Under the Stand-By Arrangement, and Request for Waiver of Performance Criteria

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

Approved by Eliot Kalter and Michael T. Hadjimichael

June 24, 2003

- **On June 8, 2001, Directors concluded the last Article IV consultation with Bolivia.** They stressed the importance of increasing public sector savings while protecting social spending, advancing structural reforms, and closely monitoring the banking system.
- **Article IV consultation discussions took place in La Paz in November 2002, and February and May 2003,** combined with discussions on a program that could be supported under the PRGF. The missions met with the President, the Ministers of Finance and Economic Development, the central bank President, representatives of political parties, donors, civil society organizations, business groups, and financial institutions.
- **Stand-By Arrangement (SBA).** Following the February 2003 social unrest, the authorities requested a one-year SBA in an amount equivalent to SDR 85.75 million (50 percent of quota), which was approved by the Executive Board on April 2, 2003. Following the completion of the first review—for which a Letter of Intent is presented in Attachment I— a purchase of SDR 10.72 million would become available.
- **Missions.** The teams comprised W. Lewis (Head), S. Cueva, A. García Pascual (all WHD), K. Kostial and H. Monroe (PDR), and M. Guin-Siu (FAD). E. Kalter (WHD) joined the latter two missions, and M. Cortés (MFD) and I. Coelho (FAD) the May mission. G. Peraza, the Resident Representative in La Paz, assisted the missions. A. Segura (OED) attended the closing meetings in May.
- **FSSA**. A Financial System Stability Assessment (FSSA) is being issued concurrently.
- **Fund relations**. Outstanding Fund credit is SDR 183 million (107 percent of quota). Bolivia has accepted the obligations of Article VIII, sections 2, 3, and 4, and has no restrictions on the making of payments and transfers for current international transactions.

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Executive Summary

- **Macroeconomic and financial vulnerabilities have intensified in recent years, while the social and political situation remains difficult.** After years of sluggish economic activity, the fiscal position has deteriorated markedly. Financial disintermediation and a loss in international reserves have raised vulnerabilities in a highly dollarized financial system. Rising social tensions and political fragmentation have weakened the government's ability to implement economic reforms. Large hydrocarbon projects could substantially improve the medium-term outlook, but face political obstacles.
- **The authorities are implementing a comprehensive strategy to deal with these vulnerabilities.** The 2003 economic program supported by the SBA is aimed at stabilizing the economy through fiscal consolidation and financial reforms. This program is broadly on track. The authorities are also developing a broader set of policies to boost productivity and employment, which are key for sustained growth and poverty reduction. In support of these reforms, the authorities aim to agree with the Fund on a PRGF-supported program in the coming months.
- **A sustained fiscal effort over the coming years is needed for a return to a sustainable public debt path.** The authorities aim at reducing the fiscal deficit by 6½ percentage points of GDP over 2003–07. Key measures include changes in oil sector taxation, the implementation of a new tax procedures code and other improvements in tax administration, an automatic mechanism to adjust retail fuel prices, a tax reform, steps to control pension costs, and enhanced mechanisms for controlling municipal spending. In the short term, contingency measures have been identified to cover risks to the fiscal program.
- **Monetary policy aims at gradually building up international reserves.** The authorities plan to move toward a more flexible exchange rate regime over the medium term, while developing market-based incentives to reduce dollarization.
- **The authorities recognize the banking system's vulnerabilities, which are presented in the accompanying FSSA, and have made a good start to put in place a comprehensive financial and corporate restructuring strategy.** The regulatory functions on prudential matters have been efficiently allocated; and prompt corrective action and resolution mechanisms are now ready to be put into operation if needed. The next priority is to put in place an efficient framework for bankruptcy procedures and corporate restructuring.

I. Introduction

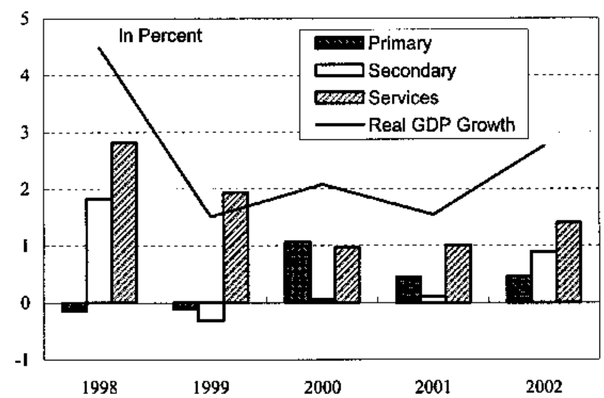
1. **The 2003 economic program supported by the Stand-By Arrangement (SBA) is broadly on track, with the authorities remaining fully committed.**[1] All quantitative performance criteria for end-March were met. Moreover, despite the difficult political and social situation, the authorities have moved forward with important fiscal and financial reforms covered by structural performance criteria, albeit with some delays (Table 1 and Figure 1). In the attached Letter of Intent (LOI, Attachment I) and Supplementary Memorandum of Economic Policies (SMEP, Attachment II), the authorities lay out policies for the remainder of the year to meet program objectives.

2. **The Article IV consultation discussions focused on the challenges of reducing Bolivia's significant vulnerabilities and laying the basis for sustained growth and poverty reduction.** The staff stressed the need for sustained fiscal adjustment over the coming years, combined with vigorous structural reforms, to meet these challenges. The authorities emphasized the high priority they attach to reaching an understanding with the Fund on a PRGF-supported program in the coming months, in support of these objectives.

II. Recent Economic Developments[2]

3. **Economic activity has been sluggish since 1999, but has shown some signs of recovery in 2002 and early 2003.** Real GDP growth averaged only 1.4 percent during 1999–2001, dampened by the regional slowdown, and an appreciation of the real exchange rate, as well as the impact of the coca eradication program (Table 2). The hydrocarbon sector was the main source of growth, while domestic demand declined. However, growth increased to 2.8 percent in 2002, boosted by the building of a new pipeline to Brazil as well as public works and transportation projects, although other domestic demand remained weak. Economic activity so far in 2003 has benefited from a strong performance in the agricultural sector, especially soybeans. Open unemployment has risen in the last four years to 8½ percent by end–2002; and about half of the labor force is underemployed. Inflation remains controlled, with a 12–month rate of 3.1 percent at end-May.

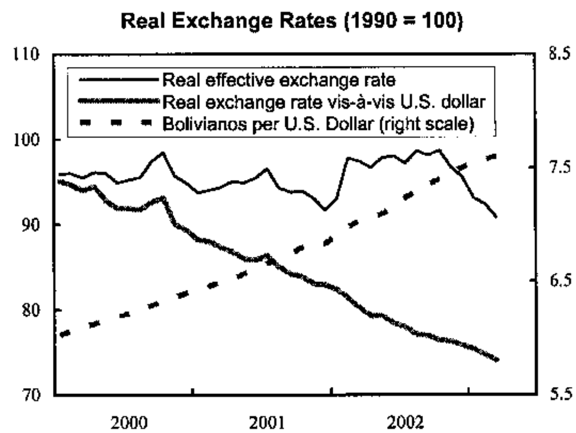
Contributions to Real GDP Growth, 1998 - 2002



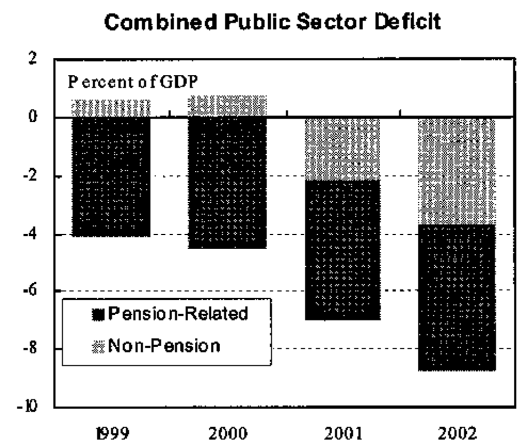
[1] Relations with the Fund, the World Bank, and the Inter-American Development Bank (IDB) are laid out in Annexes I, II and III. Annex IV discusses statistical issues.

[2] This section supplements the discussion on recent developments in the March 2003 Request for a Stand-By Arrangement (EBS/03/37).

4. **The appreciation of the boliviano in real terms during the first ten months of 2002 has been fully reversed.**[3] The boliviano experienced a 7¾ percent real effective appreciation through October 2002 because of the weakness of the currencies of the main regional trade partners—particularly Argentina and Brazil—despite depreciating against the U.S. dollar. From October to May 2003, by contrast, with the neighbors' currencies gaining strength, the boliviano depreciated by 12 percent in real effective terms. The central bank sought to limit the appreciation in 2002 by stepping up the rate of crawl against the U.S. dollar (to 10 percent), but the pace has slowed to an annualized rate of 4 percent since end–2002.



5. **Weak domestic demand has caused the external current account deficit to contract over the last two years to 4¼ percent of GDP in 2002 (Table 3).** During this period, the terms of trade deteriorated, reflecting a drop in export prices for metals and minerals, and exports increased on average by only 3 percent annually in U.S. dollar terms. FDI remained substantial (over 8 percent of GDP), mainly in the hydrocarbon sector, but dropped from the higher levels of the late 1990s, reflecting the phasing out of investment made after the privatization of several public enterprises in 1997.

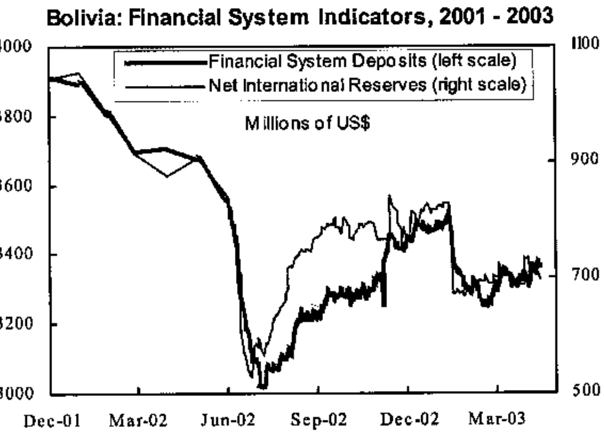


6. **The fiscal position deteriorated sharply in 2001–02.** The combined public sector deficit rose to almost 9 percent of GDP in 2002 from 3½ percent in 1999 (Table 4). Revenues were weak because of the sluggish domestic demand, delays in tax reforms, a shortfall in oil revenues, and a freeze on domestic fuel prices. Spending was boosted by rising pension costs, significant wage increases, and an expansion in public investment.

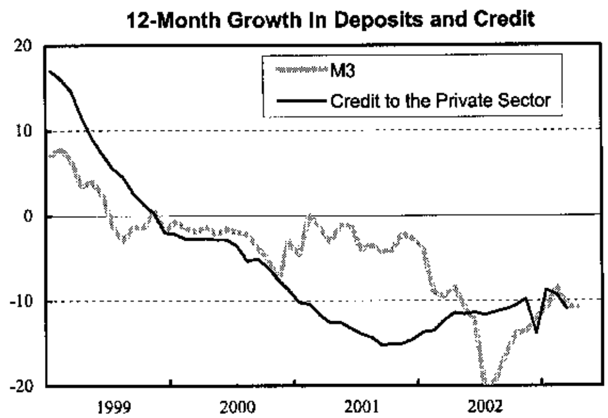
7. **Financial intermediation has contracted over the past two years, contributing to a loss in international reserves.** Both credit and deposits have declined as political uncertainty, sluggish growth, and weaknesses in corporate sector regulations have weakened confidence in the banking system and resulted in more cautious behavior by banks (see the

[3] The rate of depreciation is determined on the basis of projected inflation differentials, but is not announced; the central bank decides on short-term variations in the rate of crawl in response to external shocks or changes in demand at the daily auctions.

FSSA report).[4] As a result, broad money in relation to GDP fell by 12 percentage points of GDP to an estimated 31 percent of GDP at the end of the first quarter of 2003 (Table 5 and Figure 2). Two episodes of heavy deposit withdrawals (in mid–2002 and in February 2003) were halted after the central bank supplied liquidity, but the result has been a sharp decline of gross official reserves. Coverage of dollar-denominated bank deposits by disposable reserves declined to 30 percent at end-May, 2003.



8. **Monetary policy was eased over 2001-02 in the face of increased government financing needs and liquidity requirements of the banking system, before being tightened in recent months.** Central bank credits to the government have increased by over 1 percent of GDP since end–2001. The yield on three-month dollar-denominated treasury bills has more than doubled since late January, to 4 percent. The central bank has increased its benchmark repo rate in U.S. dollars in recent months to 6½ percent, with the aim of encouraging some gradual de-dollarization. Around 92 percent of deposits and 97 percent of loans are denominated in U.S. dollars.



9. **Several years of financial disintermediation and economic stagnation have added to vulnerabilities in a highly dollarized financial system.**[5] Nonperforming loans rose to 20 percent as of end-April and repossessed collateral to 5¼ percent of the banks' total assets, as a result of the corporate sector's weak cash flow.[6] Nevertheless, banks report capital adequacy ratios in excess of the minimum requirement, partly reflecting the partial recapitalization in December 2001 of three banks (representing 30 percent of total bank

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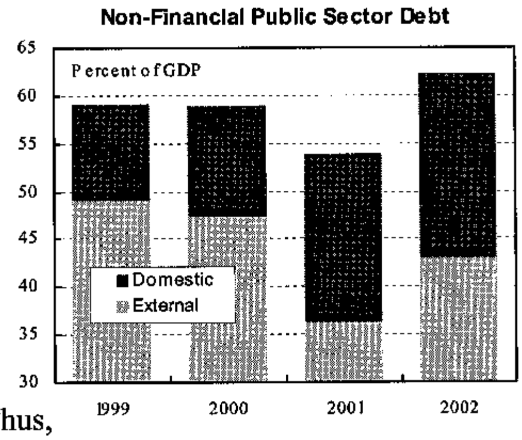
[4] Annex V of EBS/03/37 provides a summary of the FSAP team's main findings.

[5] Within the last six months, Moody's and Standard and Poor's downgraded the sovereign credit ratings to B and B3, respectively; and Moody's and Fitch downgraded the ratings of several financial institutions.

[6] These average figures mask large disparities across banks.

deposits) through subordinated loans guaranteed by the public sector (Tables 6 and 7, and Figure 3).



10. **Nonfinancial public sector debt has increased, despite the enhanced HIPC debt relief received in June 2001** which, by itself, reduced external debt by 15 percentage points of GDP. However, the impact on total debt was more than offset by the large recourse by the public sector to domestic financing on market terms and a substantial increase in nonconcessional foreign borrowing over the past two years (Tables 8 and 9). Thus, the debt-to-GDP ratio rose from 58½ percent in 2000 to 61¼ percent in 2002, while the NPV of public debt as of end–2002 remained at its end–2000 level of 45 percent of GDP.

III. Political and Institutional Context

11. **About two thirds of Bolivia's population live in poverty, with one third subsisting in extreme poverty.** After a steady decrease during most of the 1990s, the share of people living below the poverty line increased again in recent years. Poverty incidence is particularly high in rural areas and among indigenous people.

12. **Poor economic performance has contributed to social and political fragmentation.** A growing disenchantment with the traditional parties and reform fatigue—reflected in several episodes of social unrest—have weakened the ability of successive coalition governments to implement fiscal adjustment policies and economic reforms. The present government—which took office in August 2002 for a five-year term—has only a thin majority and faces a vocal opposition in and out of Congress. Social tension continues to rise among the indigenous population and coca farmers, who have been hard hit by the weak economy and a coca eradication program which did not provide alternative sources of income.

13. **The government's room to maneuver is limited by the strong desire for economic reactivation after years of stagnation and pressures from numerous interest groups.** The rapid response by the bilateral and multilateral community to the events of last February is allowing a more gradual fiscal adjustment. However, pressures are increasing to relax the fiscal stance, resist efforts to control tax evasion, and provide bailouts.

14. **Governance issues have persistently been viewed as a serious obstacle to growth and private investment prospects.** According to Transparency International, Bolivia is perceived to be the second most corrupt country in Latin America.

15. **A decision based on economic grounds on the routing of the gas pipeline for the LNG project faces strong opposition**. The government decision will be made when a sales-purchase agreement between the LNG consortium and the buyer of gas for the North American market is signed. While the interested private companies have made it clear that a route via Chile would be the only economically viable choice, poll surveys show significant

opposition to this option. Further delays could jeopardize the project because of competition for the U.S. market from other countries.

IV. Policy Discussions

A. Lessons from the Previous PRGF Arrangement

16. **The staff and authorities reviewed the experience with the previous PRGF arrangement.** It covered a period (September 1998-June 2002) in which external and domestic shocks and rising social and political tensions combined to adversely affect macroeconomic performance and the pace of structural reforms. One of the purposes of the review was to draw out lessons for the design and implementation of the government's economic program, including plans for a revision of the 2001 PRSP (highlights in Annex VI).

17. **Several lessons for future policy design emerged:**

- **The economy's vulnerability to external and domestic shocks needs to be reduced**, including through sustained strengthening of the fiscal position, dealing with balance sheet problems in the financial and corporate sectors, and moving toward a more flexible exchange rate regime over the medium term. Dollarization would be reduced through establishing a more stable financial environment and increased regulatory disincentives to dollar-based financial intermediation.

- **Fiscal adjustment is needed to reverse the deterioration in debt dynamics and ease financing constraints.** The relaxation of fiscal policy in 2001–02 was counterproductive. Instead of fostering the hoped for economic recovery, it significantly increased the debt-to-GDP ratio, limiting the government's ability to tackle difficult social issues and increasing risks of financial crisis. An effective fiscal strategy will require improvements in tax administration, greater efficiency of government spending, and control over pension costs.

- **The PRSP strategy needs to be embraced within and outside the government.** The staff pointed out that the process of consensus-building should start within the ruling coalition, encompass the congress, and—for the National Dialogue and revision of the PRSP—involve the major political parties.

- **The consensus-building effort should aim at renewed momentum for structural reforms** to boost employment, productivity, and private investment (including labor reform and sectoral strategies for agriculture and industry) and plans for the rational use of gas wealth.

- **Effective anti-poverty efforts would depend on institutional strengthening in municipalities and a greater emphasis on development in rural areas.** The situation of the coca farmers (comprising 1–2 percent of the rural labor force) needs urgent attention to forestall further social and political instability.

- **Banks' financial problems can be addressed adequately only through a comprehensive strategy that also stimulates corporate restructuring.**

18. **The authorities' emerging strategy builds upon these lessons.** The 2003 program addresses the most urgent problems, including the need for fiscal adjustment and for a comprehensive corporate and financial strategy, while providing some initial incentives for a gradual and voluntary financial de-dollarization. The national dialogue process that is getting underway will seek to build a stronger consensus—including with the main political parties—on the main structural reforms needed to lay the foundations for sustained growth and poverty reduction.

B. Medium-Term Outlook and Vulnerabilities

19. **The macroeconomic framework underlying the authorities' medium-term program is broadly unchanged from that presented in the staff report on the request for stand-by arrangement (EBS/03/37, 3/24/03).** Real GDP growth has the potential to rise to 4–5 percent over the medium-term based on strong reform efforts and led by the hydrocarbon and manufacturing sectors (Box 1). Economic growth would be boosted by increasing gas exports to Brazil through 2006 via the existing pipeline, and production from the new gas-to-liquids project (GTL) starting in 2007 and the new LNG project in mid–2008. Inflation would remain low (Table 10).

Table A. Macroeconomic Framework, 2002-08
(In percent of GDP, unless otherwise indicated)

	Prel.	Proj.					
	2002	2003	2004	2005	2006	2007	2008
Real GDP growth (in percent)	2.8	2.9	4.3	4.7	5.1	5.4	5.0
Excluding hydrocarbons	2.6	2.5	2.7	3.6	4.3	4.3	4.3
Inflation (in percent; end of period)	2.4	2.8	3.5	3.5	3.0	3.0	3.0
External current account	-4.3	-2.8	-3.1	-2.9	-2.9	-2.9	-2.9
Gross official reserves (US$ million)	854	992	1,070	1,116	1,158	1,204	1,304
As percent of broad money	27.5	30.8	32.9	33.3	32.9	32.5	33.6
Combined public sector balance	-8.9	-6.4	-4.6	-3.5	-2.9	-2.4	-2.0
Nonfinancial public sector debt	61.4	68.2	72.2	72.6	71.4	69.7	68.1

20. **After improving in 2003, the external current account deficit would remain around 3 percent of GDP in the medium term.** Strong export growth would be driven mostly by new mining and hydrocarbon projects. Public sector loan disbursements and FDI are expected to finance the current account deficit, while capital outflows would taper off. Gross official reserves would strengthen coverage of broad money.

21. **In order to return to a sustainable public debt path, the authorities aim at reducing the fiscal deficit by 6½ percentage points of GDP over the five years to 2007, to 2½ percent of GDP.** Revenue would be bolstered by continued efforts to increase the efficiency of the two tax agencies and, starting in 2004, the introduction of an automatic mechanism to adjust retail fuel prices and the implementation of a tax reform. The quality and composition of expenditure would be improved through a better tracking of pro-poor spending, the development of a medium-term expenditure framework and enhanced mechanisms for controlling municipal spending, all with support from the World Bank, and further steps to control pension costs, with the support of the IDB. Such improvements are

particularly important as Bolivia will need to borrow increasingly on nonconcessional financing terms, as the capacity of the World Bank and the IDB to lend on concessional terms to Bolivia may be phased out over the next three to five years.

22. **With this fiscal adjustment path, public debt indicators would stabilize in 2004 and then decline over the medium term, but this trajectory is subject to considerable downside risks (Annex V).**[7]

- Besides the risks of fiscal slippage and a slower recovery of the neighboring economies, delays in developing large hydrocarbon projects could markedly reduce the improvements in external debt indicators, particularly in the years beyond 2008.
- In the absence of policies to bolster growth (including corporate and financial restructuring, steps to foster rural development, and more flexible labor markets) public debt would be unsustainable.[8]

23. **An alternative "low-growth" medium-term scenario is based on GDP growth lower by 1 percent on average than in the baseline.** The lower growth is assumed to reflect a lower demand by Brazil for natural gas and delays in the completion of new gas projects until after the end of the projection period; a slower pace of corporate sector restructuring and recovery; and more limited success in taking advantage of trade benefits granted by the United States in 2002 (Table 11). As a result, the external current account deficit would rise, relative to the baseline scenario, and progress toward fiscal sustainability would be slower, as a higher deficit path would result from weaker tax revenues. The progress in reducing poverty would be lower as a result of the direct effects on the poor of slower growth of output and incomes, and through the negative impact on fiscal expenditure on anti-poverty programs.

24. **The authorities recognized that Bolivia's medium-term prospects depend crucially on the development of hydrocarbon resources, fiscal consolidation, and structural reforms.** They expressed their strong commitment to such policies, and to working closely with the international community (including through a PRGF from the Fund) to obtain external financing on concessional terms whenever possible.

C. Fiscal Policy

Policies for 2003

25. **Fiscal policy in 2003 aims at reducing the combined public sector deficit from almost 9 percent of GDP in 2002 to 6½ percent of GDP in 2003 through a combination of revenue and expenditure measures.** As described in EBS/03/37, revenue increases rely

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[7] The baseline debt sustainability analysis is close to that reported in EBS/03/37, with slightly lower debt projections reflecting the use of actual debt figures for 2002 and the most recent exchange rates.

[8] Under a stress test with lower growth, public debt could rise sharply to 78 percent of GDP in 2004–05.

on changes in the structure of oil sector taxation, the elimination of some tax exemptions, a broadening of the base of selected taxes, a strengthening of tax and customs administration following the implementation of the new tax code, and a tax regularization scheme. Expenditure measures include steps to reduce current nonwage outlays and to cut non-priority capital investment while controlling pension expenditure.

26. **Policy adjustments have been required to ensure that the fiscal program stays on track.** The 2003 budget was approved without the companion tax bill that was envisaged, and the related structural performance criterion was not observed.[9] The authorities are implementing additional fiscal measures to offset projected lower-than-budgeted revenue, reflecting both the delay in the tax bill (revenue loss of 0.4 percent of GDP)[10] and a downward revision of collections from import-related taxes and fuel excise taxes (by about 0.4 percent of GDP).

27. **Given the difficult political situation, the corrective fiscal measures are centered on spending cuts, particularly the activation of contingency plans for reducing already identified low-priority investment (¶ 4–5).**[11] In particular, investment outlays are being cut by 0.65 percent of GDP and current spending is being cut by 0.15 percent of GDP[12] (mainly consultancy services). Projects that are already under way, aim at reducing poverty, and are tied to concessional financing would continue to receive priority. Poverty-reducing expenditure will be affected somewhat, but still will be slightly higher relative to GDP than in 2002.

28. **The draft tax procedures code now before congress would promote greater tax enforcement, and has the main elements of a modern tax code (Box 2).** While the mission noted that the accompanying tax regularization scheme appeared generous (e.g., it has the character of a tax amnesty since it forgives interest and covers cases already decided by courts), it acknowledged that such a scheme would greatly facilitate the approval of the tax code that has been delayed for several years in Bolivia. The staff stressed the urgency of congressional approval of the code, since the announcement of the tax regularization scheme was already causing a drop in voluntary tax compliance, as well as the importance of resisting pressures to separate the tax regularization scheme from the tax code.

29. **Initial steps have been taken to rein in pension costs (under an IDB-supported program) but much remains to be done (see Box 4).** Regulations have been issued for the

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[9] The draft tax law would have eliminated some exemptions and adjusted selected tax rates; its passage together with the budget would have met the performance criterion.

[10] The scope of the tax bill now before Congress has been scaled back, with a revised yield of 0.15 percent of GDP.

[11] ¶ denotes paragraph numbers in the SMEP.

[12] Once the scaled back tax bill has been passed by Congress, the authorities could have some room to reverse cuts up to the projected yield of the package.

December 2002 law that switched the indexation of pension benefits from the U.S. dollar to inflation and eliminated a previously granted bonus for those pensioners that may still retire under the old system. Moreover, eligibility requirements are starting to be enforced more strictly, and the authorities plan to repeal an early ministerial resolution that granted early retirement to selected workers. An actuarial valuation of the liabilities under the old pension system is under way. In view of the significant outlays arising from pension payments under the old pay-as-you-go system, the staff urged the authorities to continue efforts to lower administrative costs further, limit previously granted benefits, and curtail fraud.

30. **The authorities stressed that the identified contingency measures are sufficiently large to cover continuing risks to the fiscal program** (¶ 9). These risks include the outcome of ongoing renegotiations with Brazil on the "take-or-pay" agreement for gas exports; legal impediments to the repeal of the previous administrations' decisions granting early retirement to selected workers; and the potential impact of delays or modifications of the new tax code.

31. **Net external financing is broadly in line with programmed levels and would still cover virtually all of the nonfinancial public sector's financing needs (Table 12).** Bilateral grants are slightly larger than previously expected, including an agreement on debt relief from Spain that was recently signed.

32. **The staff expressed some concerns about two proposals under consideration that aim at alleviating the Treasury's cash flow position (Box 3):**

- **A swap of about half of the private pension funds' (AFPs) holdings of dollar-indexed treasury bonds for inflation-indexed bonds.** The staff noted the risk of legal challenges, and stressed the importance of carefully analyzing the impact on the AFPs' financial position. The authorities responded that they are discussing these issues with the AFPs. Moreover, the staff recommended gradually reducing the government's reliance on AFPs for its financing, to make room for increased financing to the private sector.

- **Increased transfers of central bank profits or net worth to the Treasury in the context of a bond swap operation.** The mission emphasized the need to avoid impairing the central bank's independence and financial autonomy and to review carefully implications for the monetary program. In response, the authorities decided to request technical assistance from the Fund before moving ahead.

Medium-Term Fiscal Issues

33. **The staff supported the authorities' plans to strengthen the existing payroll tax and the simplified tax regime, starting in 2004**. With technical assistance from the Fund, the authorities aim at reforming the complementary value added tax (RC-IVA)—a withholding tax on wages and interest income with a 13 percent flat rate—to broaden its coverage to other sources of personal income that could be audited. Over the medium term,

as the tax administration is strengthened, the RC-IVA could be replaced by a conventional personal income tax.[13]

34. **The authorities are maintaining efforts to strengthen the two tax agencies, in line with FAD recommendations.** However, the domestic tax administration continues to be weak, and its institutional reform lags behind that in the customs area. While the staff acknowledged that progress has been made, it stressed the need for support from stakeholders, including the judiciary branch and congress.[14]

35. **The authorities intend to advance the fiscal decentralization process in coordination with the World Bank.** Plans focus on making municipal governments more efficient by improving the regulatory and institutional framework, strengthening governance, enhancing community participation, supporting fiscal discipline at the subnational level, and continuing efforts to strengthen fiduciary management. The staff welcomed the authorities' plans to start implementing a medium-term expenditure framework (MTEF) later this year with World Bank assistance.

D. Monetary and Exchange Rate Policy

36. **The monetary program for 2003 targets a gradual buildup in international reserves.** Continuing uncertainty following the February social unrest has been reflected in a slow recovery of bank deposits, and a slow growth of the monetary and credit aggregates is expected this year. The central bank aims to control its NDA consistent with raising net international reserves by US$65 million during the year.[15] So far, currency issue has been in line with programmed levels.

37. **The central bank remains prepared to provide liquidity to the financial system as needed, in case deposit withdrawals resume**, including by drawing on back-up lines from the Latin American Reserve Fund. Commercial banks have maintained a high preference for liquidity, reflected in large holdings of excess reserves with the central bank (which caused the overperformance in the end-March target for international reserves).

38. **The authorities concurred with the staff that a gradual and voluntary de-dollarization process is key for the medium term.** They have been promoting the use of the new inflation-indexed unit of account (UFV) as an alternative to asset holdings in U.S.

[13] Policy changes in income taxation will need to take account of the political economy of tax reform, in view of the reaction to tax proposals in February 2003.

[14] Regarding customs reform in the near term, the staff cautioned that an extension of the pre-shipment inspection contract beyond June 2003 would not allow Customs to fully undertake valuation responsibilities.

[15] The projected resumption of private credit has been lowered. However, alternate channels are expected to provide the private sector with financing, such as purchases of future agricultural production (especially soybeans), capital market issuances, or direct loans from foreign banks to large firms.

dollars, but acceptance has been low so far. In addition to increasing repo rates on U.S. dollar instruments, the authorities plan to implement further market-based disincentives to dollar-based financial intermediation, such as higher reserve requirements for dollar-denominated deposits and increased provisioning requirements for dollar lending to non-dollar income earners.

39. **The authorities affirmed their aim of preserving the recent gains in competitiveness.** They also saw potential opportunities to further reduce the real effective exchange rate if regional currencies continued to strengthen, which would not have the damaging balance sheet impact of boliviano depreciation against the U.S. dollar. The staff welcomed this approach, emphasizing that further improvements in Bolivia's external competitiveness would help to strengthen growth prospects, and that a move toward a more flexible exchange rate regime could reduce Bolivia's exposure to exogenous shocks. The authorities noted that the boliviano had now reached its most depreciated level in real effective terms since 1996, and stressed that they were monitoring developments with a view to discerning any resulting inflationary pressures. They indicated that they would tighten monetary conditions if needed.

40. **The authorities stressed that any move to increased exchange rate flexibility should be gradual,** taking into account the possible adverse impact on corporations' and banks' balance sheets (Figure 4). The staff agreed that this timing should be based on progress toward voluntary de-dollarization and strengthening of the financial system and of the fiscal accounts. A joint study with staff on Bolivia's competitiveness—to be completed by September 2003—will help the authorities to develop their strategy.

E. Financial and Corporate Sector Strategy [16]

41. **The financial system has been under stress for several years and the authorities are closely monitoring the situation of individual institutions.** The authorities stressed that they were fully aware of the financial system vulnerabilities that were highlighted by the FSAP exercise. They were concerned by the sharp deterioration in the banks' loan portfolio, driving a rapid rise in capital at risk, despite efforts to increase provisions in recent years. The main recommendations of the FSSA report are summarized in Box 4.

42. **The staff commended the progress made in the financial and corporate strategy in recent months,** under the coordination of the recently appointed high level team:

- A decree issued in early May clarified and efficiently allocated the powers to regulate on prudential matters.[17]

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[16] The mission worked closely with MFD and World Bank staff to assess progress in the financial and corporate sector areas. Further details are presented in an accompanying selected issues paper.

[17] Two performance criteria for end-April (the allocation of regulatory powers on prudential matters, and the issuance of regulations on prompt corrective action and resolution mechanisms) were fully implemented, albeit with a few days delay, for which the authorities are requesting waivers.

- The prompt corrective action and resolution mechanisms introduced by the December 2001 law have already been put in practice. In May, a small savings and loans institution was successfully intervened and its deposits transferred to another institution under the new mechanisms.
- The central bank issued regulations in April, which clarify the basis for liquidity support to banks, including those undergoing a regularization process.
- Draft laws for bankruptcy procedures and informal corporate workouts have been sent to congress. They would provide (i) a modern legal framework for corporate insolvency, including swift liquidation procedures for nonviable firms; and (ii) the possibility for a debtor enterprise to reach an out-of-court agreement with its creditors on a restructuring plan.
- The solvency situation of individual financial institutions has been assessed, and will continue to be monitored, based on the rules for provisioning requirements in effect since end-March.

43. **Further steps are needed in the near term to consolidate this initial progress:**

- **The authorities reached understandings with the mission on the steps to address shortcomings in the draft legislation** for bankruptcy procedures and informal corporate workouts as quickly as possible and to ensure approval by Congress at the latest by end-September (structural benchmark) (¶ 14).[18] Once the laws are approved, further actions include the issuance of the relevant regulations; the practical implementation of the corporate restructuring strategy including the setup of the Superintendency of Enterprises; and the creation of incentives to enhance the ability of financial institutions and the corporate sector to analyze and resolve corporate restructuring issues.
- **The recently appointed high level team will develop the framework for the use of public funds for bank restructuring and corporate workouts.** With World Bank assistance, a technical group is developing a database for the corporate sector that would provide a diagnostic of the potential impact of corporate workouts on banks. Preliminary results are expected over the next several weeks, and the fiscal implications will be assessed by the time of the second review.
- **With a tightened regulatory framework and in view of the potential impact of corporate workouts on banks, the authorities need to be ready to react in case of potential bank failures.** The staff urged the authorities to closely monitor weak

[18] Both draft laws need to address potential constitutionality challenges from dissenting creditors. Shortcomings include the remaining presumption of fraud, rights of secured creditors, and the timing of payment obligations for the bankruptcy law, as well as the lack of option to extend the period for reaching an informal agreement, the treatment of tax and pension fund liabilities, and the specific powers of the newly created Superintendency of Enterprises for the informal workouts law.

financial institutions and to take early decisions for strengthening them if needed. Such decisions should be based on the objectives of minimizing fiscal costs while ensuring the stability of the financial system.

44. **Over the medium term, the independence and effectiveness of the regulatory and judiciary bodies should be further enhanced, while maintaining and strengthening accountability and transparency standards.** The authorities noted the limitations of the current judicial procedures and institutions for the expeditious liquidation or rehabilitation of overindebted enterprises. To handle the intricacies of bankruptcy proceedings, the judicial branch will need substantive additional training.

F. PRSP-Related Issues

45. **The authorities plan to have a final version of the PRSP progress report (which will include possible strategies for increasing growth and reducing poverty and a revised medium-term macroeconomic framework) in August 2003.** This report—to be assessed jointly by Fund and Bank staffs—would provide the basis for a possible PRGF arrangement. The government is also conducting a new National Dialogue (expected to be concluded in August) which, together with the PRSP progress report, will feed into a new PRSP later this year.

46. **The government is seeking to address the shortcomings of the 2001 PRSP in the new PRSP process.** The 2001 National Dialogue, though broadly participatory and allowing the distribution of debt relief resources under equity criteria, failed to yield the expected benefits in terms of country ownership and raised unwarranted expectations. In the context of the current National Dialogue, the government will seek consensus on policies to boost productivity and employment as key elements for growth and poverty reduction, and on the need to strengthen administrative procedures and institutions. To that end, the authorities are preparing an outline and timetable for a labor market study, which could provide the basis for future labor reform. The authorities have made progress in tracking poverty-related expenditure by local governments, but there is a need to improve the timeliness and quality of the data, which are compiled from different sources with dissimilar coverage (Tables 14 and 15).

47. **The government plans a number of initiatives to ease social tensions, including by developing economic alternatives for coca growers.** Coca plantations in the Chapare region have been reduced by three quarters in recent years, while alternative tropical crops are about 16 times less profitable than coca leaf. The authorities are actively giving consideration to a free trade zone in the affected regions, with fiscal incentives to attract private investment and new technologies, specially for textiles and wood products.

48. **As already identified in the 2001 PRSP, improvements in governance are central to the policy agenda**. The staff shared the authorities' concern that widespread corruption reduces the credibility of the political system, undermines public institutions, and lowers the quality of public services. The authorities are resolved to take firm action and combat corruption at all levels, including through the newly created Anti-Corruption Technical Unit (UTCC) assigned to the Vice President, and the recently introduced new procurement regime, as well as through progress in the institutional reform of public sector entities and the public sector financial information management.

V. Program Risks

49. **The fragile political context remains the main challenge for maintaining solid macroeconomic policies.** While the security situation has been calmer in recent months, the government's ability to build a broader support for economic reforms will be tested in the months ahead on several fronts: the approval of essential laws under an intense congressional agenda; the adherence to the fiscal program targets; the need for prompt decisions to develop critical hydrocarbon projects; and plans to enhance the powers of the revenue collection agencies and restructure the financial and corporate sectors.

50. **Attaining a stronger consensus will depend on demonstrating that the government's program is clearly aimed at sustaining strong growth and addressing social problems.** The delay in approving the tax bill may be indicative of a more general difficulty that the Executive Branch faces in gaining legislative support for its economic policy agenda. Improved communication between executive and legislative branches is essential for ensuring an effective and consistent policy implementation. Readiness to implement fiscal contingency measures is critical to ensure the needed fiscal adjustment despite potential risks to the revised fiscal program.

VI. Program Monitoring

51. **The SBA-supported program for 2003 is broadly on track (see Attachments I and II).** All quantitative performance criteria for end-March and the continuous performance criterion were met. Two structural performance criteria, covering the submission to congress of a draft tax code and draft laws on bankruptcy and informal corporate workouts, also were met. The authorities are requesting waivers for the other three performance criteria for the first review: two of them (clarifying institutional roles for financial sector oversight, and issuing financial sector regulations) were fully implemented a few days after the April 30 expected completion date; regarding the third one, corrective fiscal measures have been taken to compensate for the nonapproval by April 15 of the tax bill that accompanied the 2003 budget (see Section IV.C).

52. **Program targets have been set for the remainder of 2003.** The indicative targets for end-September and end-December would be converted into quantitative performance criteria. Also, the structural conditionality for the second half of 2003 is unchanged (see Table 1).

VII. Other Issues

53. **Trade system.** The staff commended the authorities for maintaining an open exchange and trade system, making Bolivia one of the most open economies in Latin America.[19] As a member of the Andean Community, Bolivia remains committed to regional

[19] The trade regime has a rating of 1 (most open) on the 10-point scale of the Fund's trade restrictiveness index.

integration, and it is working toward a free trade agreement with Chile. The authorities have recently introduced incentives[20] to support exporters' efforts to take advantage of opportunities provided by the increased access to the U.S. market under the trade preferences provided by the Andean Trade Preferences and Drug Eradication Act (ATPDEA) in 2002.

54. **Money laundering.** Bolivia has a system to prevent and suppress money laundering that fulfills most of the 40 Financial Action Task Force on Money Laundering (FATF) recommendations. The system includes mandatory requirements on the supervised financial, stock exchange, and insurance sectors, but does not encompass foreign exchange houses. Operational results on prevention, detection, and suppression have been modest and the Financial Intelligence Unit (UIF) has not been able to conduct onsite inspections. The UIF is working to extend the type of offenses that are legally punishable—including the financing of terrorism and illicit gains from smuggling activities—and the Banking Superintendency is drafting regulations to expand the duties of external auditors in this area.

55. **Capacity to repay.** It is expected that Bolivia will be in a position to discharge its obligations to the Fund in a timely manner, on the basis of authorities' commitment to prudent macroeconomic and financial policies. However, the authorities' ability to create broader support for economic reforms, especially through the new national dialogue, will be key for diminishing social and political risks. On the other hand, Bolivia's debt service to the Fund would be only a small portion of its exports of goods and service and Bolivia has a good record of payments to the Fund.

56. **Statistical issues.** Timeliness and coverage of the economic statistics are broadly adequate. However, the publication of national accounts is delayed and has some inconsistencies, especially with regard to investment data. Despite significant progress in labor market statistics, wages and unemployment data have very limited coverage and lack quarterly information (see Annex IV).

57. **Technical assistance.** Priority areas for Fund technical assistance to Bolivia include tax policy, tax and customs administrations, the banking system, and monetary and national accounts statistics.

58. **Safeguards assessment.** A full safeguards assessment is in the final stages of preparation, as required under the Fund's safeguards assessment policy. The safeguards assessment is expected to be completed by the time of the Board meeting for the first program review, and its main findings will be communicated to the Board for its consideration.

VIII. STAFF APPRAISAL

59. **Economic performance has been weak since the 2001 Article IV consultation, heightening the economy's vulnerabilities.** Growth has been slow; a sharply higher fiscal

[20] Including a reduction in the VAT rate and customs tariffs for certain capital imports and tax deferrals.

deficit in 2001–02 has worsened indicators of fiscal sustainability; and problems in the highly dollarized financial system became acute in 2002 and early 2003. The economic slowdown exposed inefficiencies in the corporate sector and exacerbated a difficult social and political situation, culminating in the violent protests of February 2003.

60. **The authorities have adopted a program for 2003 to stabilize the situation, and the SBA-supported program is broadly on track.** The quantitative performance criteria for end-March were met, and most of the structural policy actions planned for April have been implemented, although with delays. Growth is expected to rise slightly this year, although a sustainable economic recovery will depend on restoring financial soundness to the banking and corporate sectors and broader reforms.

61. **Timely policy adjustments have been made to keep the fiscal program on track.** The authorities responded to a delay in approving the tax bill and a downward revision of other public sector revenue by activating contingency plans for cutting low-priority investment, reducing current spending, and implementing a reduced set of tax measures. The staff encourages the authorities to continue monitoring fiscal developments closely, and to be ready to activate additional spending cuts, if needed.

62. **The tax procedures code recently submitted to congress is central to the strategy for improving tax collections**, which also encompasses ongoing reforms of the two tax agencies. The draft legislation has been combined with a tax regularization scheme that could adversely affect taxpayer compliance. To minimize this risk, it will be important to approve the tax code soon and to prepare for its implementation.

63. **Other fiscal reforms also are needed to put the public finances on a sustainable basis.** The authorities are anticipating these needs with their plans to pursue tax reform, control the high costs of the pension reform, enhance the effectiveness of fiscal decentralization, and develop a medium-term expenditure framework.

64. **The authorities' proposals aimed at alleviating the treasury's cash flow position—through a swap of private pension funds' holdings of bonds for inflation-indexed bonds and increased transfers of central bank profits—raise serious concerns.** It will be important to preserve the central bank's financial strength and avoid unwanted sources of monetary expansion, and to avoid compromising the long-term financial health of the privately administered pension funds.

65. **Monetary policy is appropriately geared to supporting a gradual buildup of international reserves while ensuring needed liquidity for the financial system.** A shift toward monetary tightening would be needed if clear evidence developed of rising inflation pressures.

66. **The staff welcomes the authorities' intention to preserve the recent gains in competitiveness.** A more competitive exchange rate would help to promote stronger growth prospects, but the staff recognizes that a shift to more flexible exchange rate management needs to be handled carefully in view of the high degree of dollarization and the related financial and corporate vulnerabilities. An assessment will be made by this September in the context of a joint report by the authorities and the staff on Bolivia's competitiveness. Over

the medium term, a move toward a more flexible exchange rate regime would reduce Bolivia's vulnerability to exogenous shocks.

67. **Good progress has been made in developing a comprehensive strategy for the financial and corporate sectors.** Important follow-up includes the passage and effective implementation of draft laws now before congress for corporate bankruptcy and voluntary corporate restructuring. It will be important to maintain the momentum in implementing this strategy; delays in corporate reform would heighten the risk of further deterioration of the situation of the banking sector.

68. **The staff welcomes the government's progress toward a medium-term economic program that would move beyond the current stabilization phase to policies for fostering a higher rate of sustained growth and the reduction of poverty.** There is a need for policies to remove obstacles to growth that include insufficient infrastructure, excessively bureaucratic requirements for businesses, labor market rigidities, inadequate investment in human capital, and governance problems in the executive and judicial branches. The staff urges the authorities to move quickly on large natural gas projects, including steps to ensure the public's acceptance of a decision on the LNG export project on economic grounds.

69. **The review of experience with recent Fund-supported programs has highlighted the need for greater country ownership of the policy strategy.** The Congress should play a more central role in the participatory process of the PRSP. Also, a future program that could be supported by a PRGF arrangement should seek to reduce the vulnerability to external shocks.

70. **The staff recommends the completion of the first review.** The macroeconomic program is basically on track and the progress in advancing the financial and corporate sector strategy is broadly in line with expectations. As two of the performance criteria have been implemented with a few days delay, and appropriate compensating measures have been taken with regard to the PC on the approval of the budget deficit by congress, the staff recommends approval of the authorities' request for waivers.

71. It is recommended that the next Article IV consultation with Bolivia be held on the 24–month cycle, subject to the provisions of the decision on consultation cycles adopted on July 15, 2002.

Box 1. Sources of Growth

The economic crisis that led to the 1984–85 hyperinflation and a more than 10 percent cumulative decline in real GDP was reversed through a broad agenda of structural reforms during the late 1980s and 1990s. These included the elimination of nontariff barriers and the reduction and simplification of tariffs; the opening to private partners of the five major public enterprises (*capitalización*); a pension reform; a significant strengthening of banking supervision together with the opening to foreign competition in banking services; and providing autonomy to the central bank.

After several years of a negative contribution of total factor productivity to real GDP growth, the structural reforms led to an improvement in productivity, whose contribution to growth was 1.3 percent during the period 1991–97 (see table below). However, during 1998–2002, several exogenous shocks contributed to a slowdown of economic activity that resulted in a 1 percent drop in per capita income.

Bolivia: Contribution to Growth
(Average, in percent)

		Factor contribution			Sectoral contribution		
	GDP	**Capital**	**Labor**	**Productivity**	**Primary**	**Secondary**	**Tertiary**
1981-1985	-2.0	0.8	1.1	-3.9	-0.6	-1.2	-0.6
1986-1990	2.2	1.0	1.2	0.1	0.3	0.6	0.7
1991-1997	4.3	3.5	-0.6	1.3	1.0	0.9	2.1
1998-2002	2.4	5.8	-2.2	-1.2	0.3	0.5	1.6
2003-2008	4.6	2.1	0.7	1.7	1.8	0.9	1.8

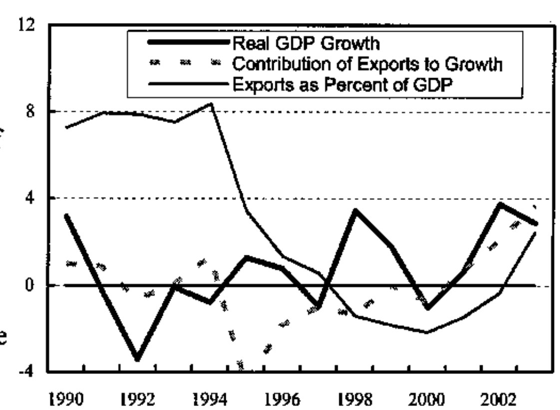
Note: Estimates are based on a Cobb-Douglas production function (with one third capital share), 6 percent depreciation rate for the construction of the capital series, and 3.2 percent labor growth for the 2003-08 projections.

Over the medium term, sound macroeconomic policies, structural and institutional reforms (especially at the municipal level), a more efficient labor market, and the restructuring of the corporate and financial sectors would constitute a solid basis for enhanced productivity and sustained growth. Under these assumptions, total factor productivity could contribute 1½ percent to medium-term growth of about 4½ percent, which is expected to be led by natural gas and manufacturing exports.

- Bolivia's oil and gas sector could contribute about 1 percentage point on average to the annual growth of GDP during 2003–08. Over the next four years, increasing gas exports through the existing pipeline to Brazil will continue to boost growth. Given the high import content of construction, the main impact of new projects on GDP would be felt after they reach the production phase. Natural gas exports to North America could begin in 2008 if a sales-purchase agreement between the LNG consortium and the North American buyers is signed by the end of 2003. In addition, a new gas-to-liquids project (GTL) is being planned for the export of diesel and other liquids to Brazil, which could start by 2007. However, changes in world oil prices and a fall in Brazil's demand for energy could affect the scale of this project.

- Despite a better-than-average growth performance since 1990, and a higher degree of openness relative to its Latin American trade partners, the contribution of Bolivian exports to growth has been lackluster so far (see Figure). The authorities' export promotion strategy to take advantage of the Andean Trade Preferences and Drug Eradication Act will target four sectors (textiles, leather, wood products, and jewelry), that could potentially increase overall real growth by about ½ percent a year.

Bolivia and Largest Latin American Economies 1/



1/ All variables are 3-year moving averages and are computed as differences with respect to a simple average of Argentina, Brazil, Chile, Colombia, Mexico, Peru, and Venezuela. Forecast for 2003.

Box 2. Tax Code and Tax Regularization Scheme

The existing tax code is inadequate for enforcing tax compliance. The current set of rules and regulations, which date back to 1992, does not empower the tax authority to properly exercise its powers and perform its duties.

The draft tax code has the elements of a modern tax code and corrects many deficiencies of the current legislation. The draft—submitted to congress on April 30 and expected to be in place by the end of the third quarter—is of good quality, incorporates measures needed to strengthen the powers of both the domestic tax and custom administrations.

The main changes introduced by the proposed tax code include:

(i) Disputes over tax liabilities will proceed through an administrative procedure prior to judicial recourse. For that purpose, the tax superintendency is being created.

(ii) Tax fraud and similar violations will be subject to criminal penalties.

(iii) A legal presumption of validity of the tax administration's acts and their immediate effectiveness. For instance, sworn tax declarations will be sufficient legal basis for pursuing tax collection.

(iv) The introduction of customs issues for the first time.

(v) The concepts of joint liable liability and secondary liability; that is, the tax liability can be extended beyond the main taxpayer.

(vi) The obligation for taxpayers to provide information to the tax administration, while providing the tax administration with the authority to obtain such information, subject to very few exceptions. Bank secrecy is abolished for tax purposes.

(vii) The possibility of undertaking precautionary measures to ensure the collection of tax liabilities, even prior to concluding the administrative process for determining such liabilities.

(viii) The rules for applying the statute of limitations will be specified.

The implementation of the tax code will require the issuance of regulations, training of tax administration officials, taxpayers' education, and the setting up of a tax superintendency for the administrative appeals process. Before the tax code enters into force and during the six months following its publication, the required regulations (either by supreme decree or by administrative decision).

Included in the tax code legislation is a tax regularization scheme. It eliminates penalties and interest and allows the balance to be paid over five years with two years' grace. Unlike previous schemes, debts finally determined after appeal to the Supreme Court would also qualify. There are pressures to extend this scheme to vehicles smuggled into the country. This should be avoided as it would undermine the customs administration's efforts to require the payment of vehicle import taxes.

BOX 3. PROPOSALS TO EASE THE TREASURY'S CASH FLOW POSITION

Two proposals for changing the terms of existing domestic debt are being considered, as part of the efforts to ease the Treasury's cash flow position:

1. Since 1997 private pension funds (AFPs) have been required to buy treasury bonds up to a ceiling of US$180 million a year (equivalent to about 2½ percent of GDP) on terms to be agreed annually. The authorities plan to swap about half of the existing stock of dollar-indexed bonds with a yield of 8 percent to inflation-indexed bonds with a real yield of 5 percent,[1] as:

- there has been no annual revision of the financial conditions of the bonds since 1997, despite a decline in market rates (the yield for one year dollar-denominated treasury bonds has declined from 7–9 percent in 1998–99 to below 5 percent in 2003);
- a gradually increasing proportion of the AFPs' liabilities will be indexed to the CPI (new pensions, starting in 2003, will be indexed to inflation); and
- the real depreciation of the boliviano against the U.S. dollar has sharply increased the fiscal costs associated with the dollarization of the bonds held by the AFPs.

2. Central bank profits or net worth could be transferred to the Treasury, in the context of a bond swap operation. The central bank holds about US$680 million of nonnegotiable dollar-denominated treasury bonds that were issued for the recapitalization of the central bank. The operation could involve a swap of such securities for inflation-indexed treasury bonds and changes in accounting rules for reserve accounts built up to cover exchange rate risk.

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[1] This would match the terms and conditions of the new bonds issued since January 2003, consistent with the December 2002 law that switched the indexation of pension benefits from the U.S. dollar to inflation.

Box 4. Main Recommendations of the FSSA

Design a comprehensive strategy to deal with the interlinked banking and corporate sector problems, guided by a set of general principles that aim to minimize the risk of a contagious run, do not over commit the State by first adjudicating losses to shareholders of banks and corporations, avoid delays in tackling insolvency problems, decentralize the process, and maintain the highest standards of accountability and transparency.

Appoint a high level systemic restructuring team to help design and implement such strategy, and to provide vision and leadership to a process very likely to be risky, difficult, and protracted. Also develop contingency plans to deal with unexpected systemic liquidity problems.

Reform the dysfunctional corporate reorganization and bankruptcy framework by enacting reform legislation, and a new law that would support informal, decentralized, out-of-court workouts.

Strengthen financial supervisory and regulatory arrangements by clarifying the allocation of powers to issue regulation, fostering a process that ensures technical integrity of the norms and minimum political interference. Further, clarify the inter-institutional relationship between the Ministry of Finance, SIREFI, and the four Superintendencies so that the operational, budgetary, and supervisory independence of the sectoral superintendencies is buttressed.

Issue regulation to effectively implement prompt corrective action and bank intervention to strengthen supervisory tools and to allow the timely adoption of solution to troubled institutions. Issue prudential regulation to improve banks risk management practices. By regulation, limit the scope to use Article 38 of the BCB Law to cases of intervention of financial intermediaries.

Gradually introduce prudential regulation to help internalize the risk posed by financial dollarization.

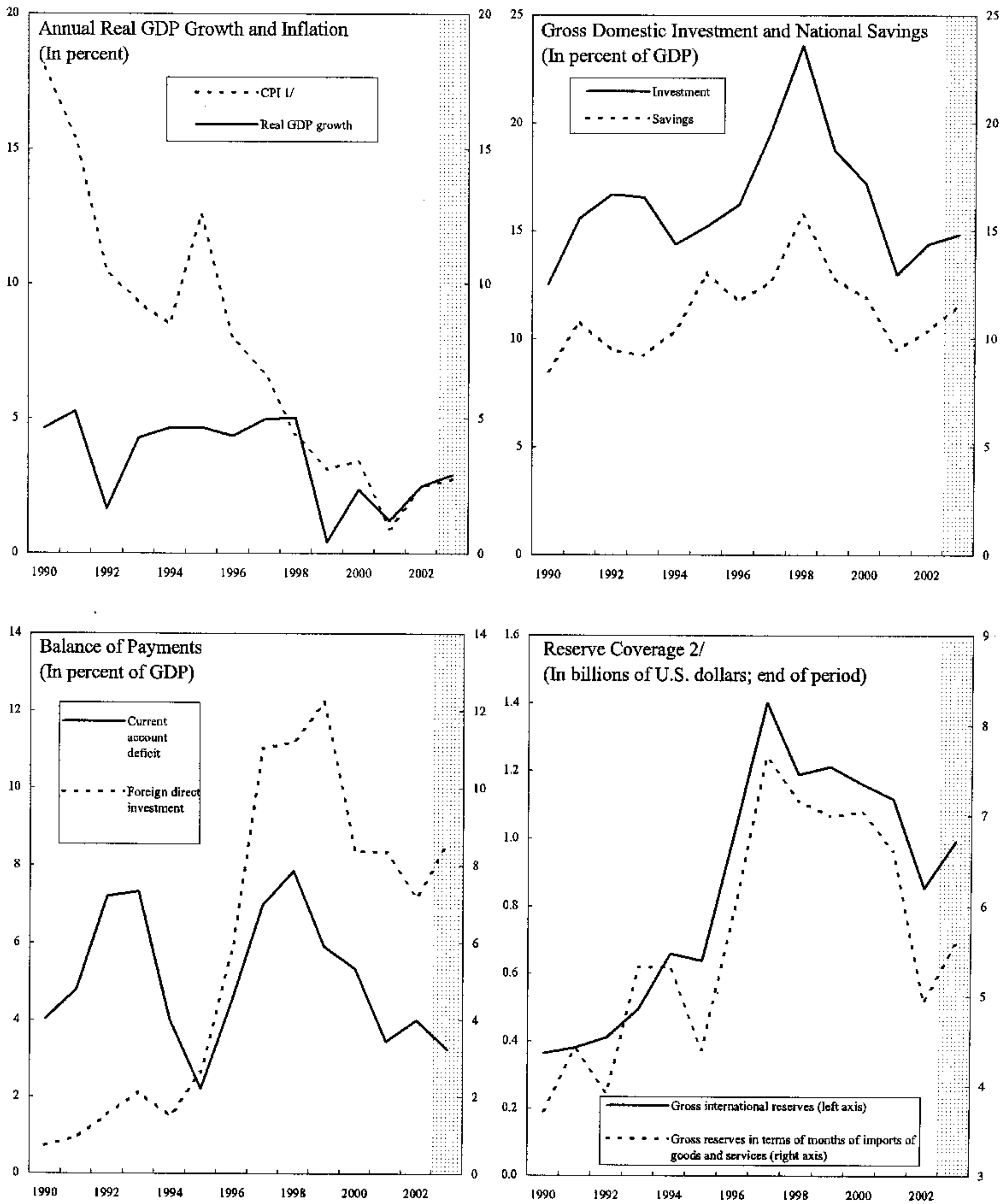
Buttress and maintain an adequate buffer of international reserves to assuage the concerns of jittery investors and build up the credibility of LOLR facilities. Clarify the rules of access to liquidity windows so that (solvent but may be undercapitalized) banks undergoing a regularization process are not denied access.

Correct the legal shortcomings for payment systems, and proceed promptly to complete the development and implementation of a large-value RTGS payment system of the BCB to drastically reduce systemic risk, currently borne by the central bank.

Criminalize the financing of terrorism, and subject foreign exchange bureaus to mandatory requirements for AML.

Strengthen the capacity of the SPVS for on-site inspections of insurance companies, address shortages in staffing, and improve the regulation of the mutual fund industry regarding risk management and disclosure standards.

Figure 1. Bolivia: Selected Economic Indicators, 1990–2003

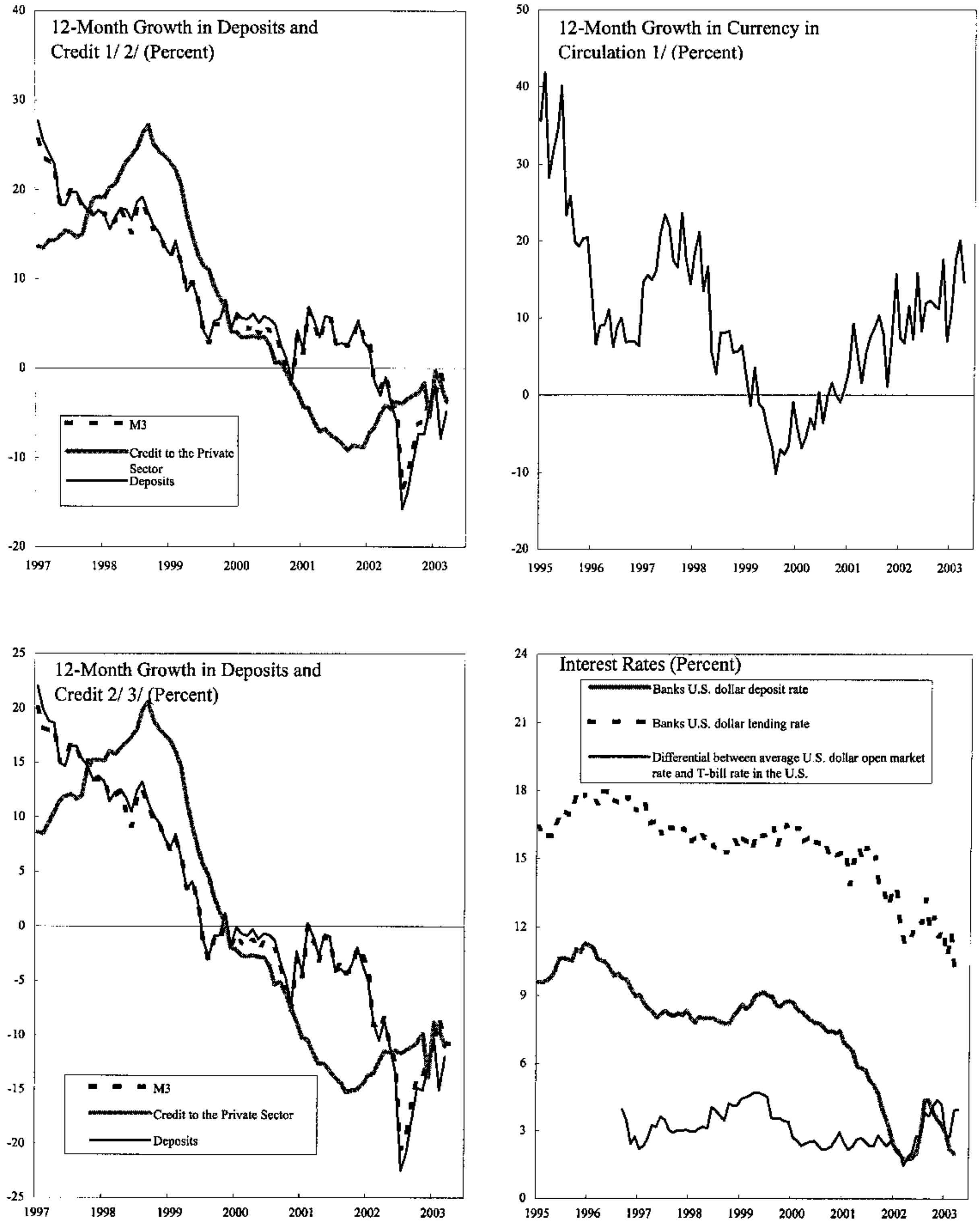


Sources: Central Bank of Bolivia; Ministry of Finance; and Fund staff estimates.

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; for 2003, gold is valued at US$300 per troy ounce.

Figure 2. Bolivia: Monetary and Financial Sector Indicators



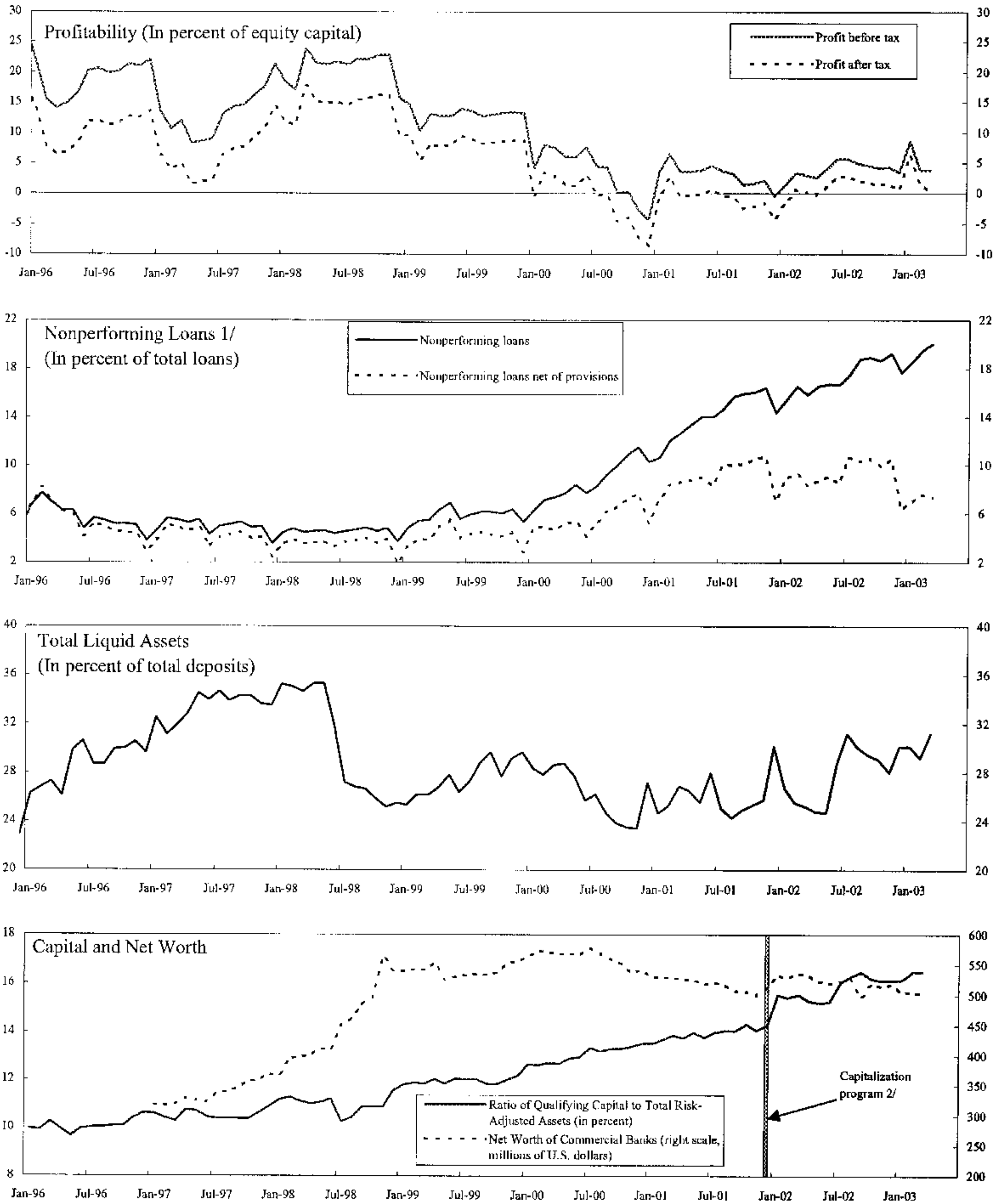
Sources: Central Bank of Bolivia, Superintendency of Banks; and International Monetary Fund, *International Financial Statistics*

1/ In bolivianos, at current exchange rates.

2/ Deposits include restricted and accrued liabilities to the private sector. Credit includes loan portfolio purchased by the central bank and FONDESIF, loans from banks in liquidation, and commercial banks' investments.

3/ In U.S. dollars, at current exchange rates.

Figure 3. Bolivia: Commercial Bank Performance Indicators, 1996–2003

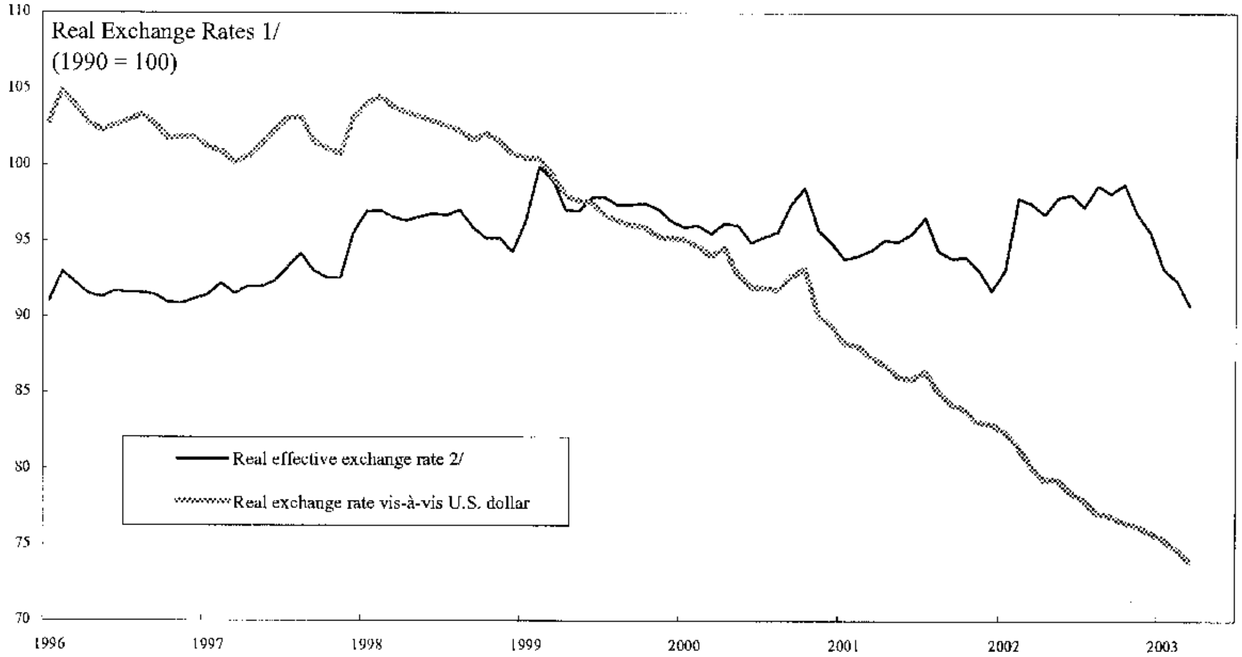


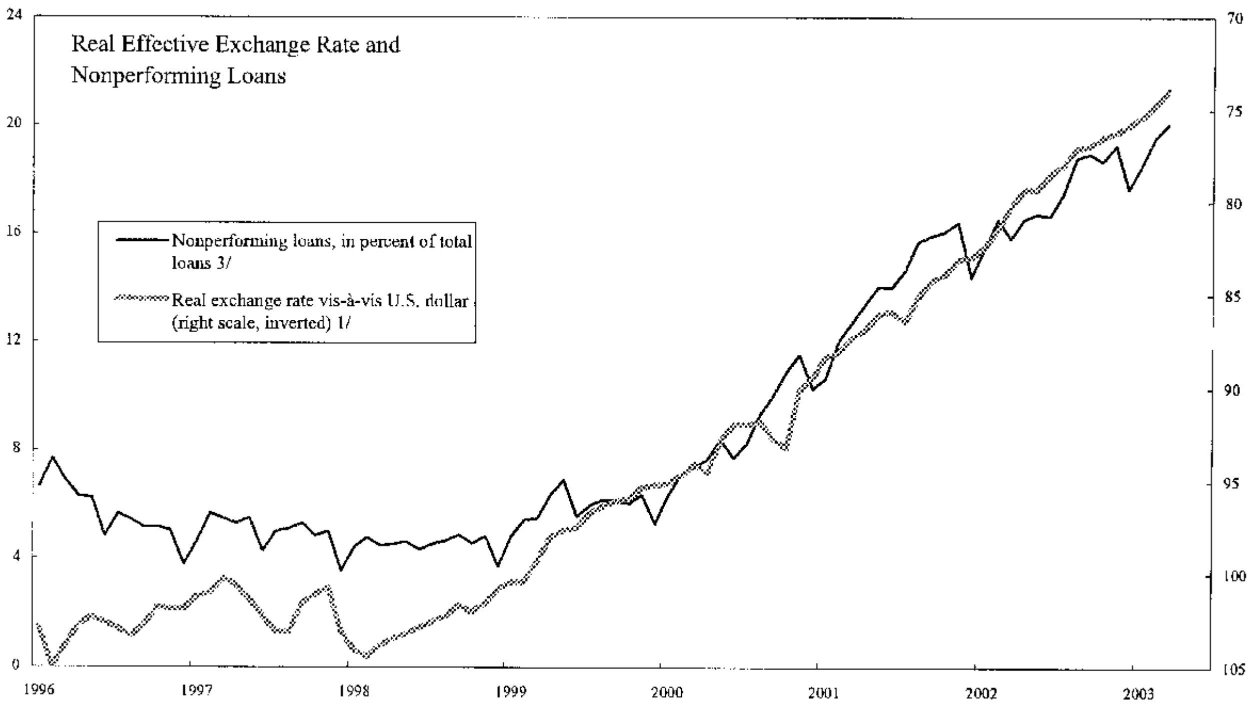
Source: Superintendency of Banks.

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.

2/ In December 2001, three banks were recapitalized through public sector guaranteed subordinated loans under the PROFOP program.

Figure 4. Bolivia: Real Exchange Rate and Quality of Bank Portfolio, 1996–2003





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

1/ Increase is an appreciation. Based on exchange rate data available as of end-February 2003, and staff projections for CPI.

2/ Weights based on trade with ten countries, excluding trade related to natural gas, in 1996–97.

3/ 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.

Table 1. Bolivia: Structural Conditionality Under the Stand-By Arrangement, 2003 1/

Condition	Policy Measure	Timetable	Status
	Public Sector Reform and Financing		
Performance Criterion	Approval of 2003 budget, which together with the proposed revenue measures described in para. 11 of the TMU is consistent with a combined public sector deficit equal to or less than 6.5 percent of GDP	April 15, 2003	Budget approved on April 3, 2003 but tax delayed. Alternative measures to meet the fiscal target have been taken. Waiver requested.
Performance Criterion	Submission to congress of a tax procedures code consistent with para. 12 of the TMU	April 30, 2003	Met.
Benchmark	Approval by congress of a tax procedures code consistent with para. 12 of the TMU	September 30, 2003	Pending.
	Financial Sector and Corporate Sector		
Performance Criterion	Issuance of the final regulations for the bank resolution and prompt corrective action mechanisms introduced by the financial sector law of 2001 consistent with para. 14 of the TMU	April 30, 2003	Implemented on May 9, 2003. Waiver requested.
Performance Criterion	Issuance of supreme decree(s) (i) clarifying the roles of the different institutions with oversight over the financial sector (includes ensuring a technical basis for issuing prudential norms); and (ii) defining certain areas of banking regulation that should be determined by the superintendency consistent with para. 13 of the TMU	April 30, 2003	Implemented on May 6, 2003. Waiver requested.
Performance Criterion	Submission to congress of draft bankruptcy law and draft law for corporate debt workout mechanism, prepared in consultation with Fund staff and consistent with paras. 15 and 16 of the TMU	April 30, 2003	Met.
Benchmark	Approval by congress of law on corporate workout mechanism consistent with para. 16 of the TMU	September 30, 2003	Pending.
Benchmark	Approval by congress of bankruptcy law consistent with para. 15 of the TMU	September 30, 2003	Pending.

1/ References in the table are to the relevant paragraphs of the Technical Memorandum of Understanding (TMU) signed on March 21, 2003.

Table 2. Bolivia: Selected Economic and Financial Indicators

	1999	2000	2001	2002	2003 Prog.	2003 Rev. Proj. 1/
(Annual percentage change)						
Income and prices						
Real GDP	0.4	2.3	1.5	2.8	2.9	2.9
Real domestic demand	-2.0	1.2	-2.5	1.6	1.9	1.0
GDP deflator	2.4	5.3	0.7	2.7	3.0	3.0
CPI inflation (period average)	2.2	4.6	1.6	0.9	2.6	2.6
CPI inflation (end-of-period)	3.1	3.4	0.9	2.4	2.8	2.8
(In percent of GDP)						
Investment and savings						
Gross domestic investment	18.8	18.3	14.2	14.7	14.8	14.4
Public	5.0	5.2	5.8	5.4	6.0	5.0
Private, including stockbuilding	13.8	13.1	8.5	9.4	8.8	9.4
Gross national savings 2/	12.9	13.0	10.8	10.4	11.6	11.5
Public	2.9	2.8	1.4	-0.4	1.9	1.2
Private	10.0	10.2	9.4	10.8	9.7	10.3
Combined public sector 2/						
Overall balance	-3.5	-3.7	-6.9	-8.9	-6.5	-6.5
External financing 2/	1.9	2.0	3.1	6.1	6.4	6.4
Domestic financing	1.6	1.8	3.9	2.8	0.1	0.1
Nonpension balance	0.6	0.7	-2.1	-3.9	-1.6	-1.6
Pension-related balance	-4.1	-4.5	-4.8	-5.0	-4.9	-4.9
Nonfinancial public sector debt	59.5	58.6	53.6	61.4	70.2	69.3
External 3/	49.5	47.1	36.0	42.2	50.4	49.1
Domestic 3/	10.0	11.5	17.6	19.2	19.8	20.2
(Annual percentage change, unless otherwise stated)						
Money and credit						
Broad money (in U.S. dollars at current exchange rates)	-1.8	-3.3	-3.1	-11.7	6.3	3.8
Credit to private sector (in U.S dollars at current exchange rates	-2.0	-9.0	-13.6	-9.5	3.4	1.5
Interest rates (percent, end-of-period)						
Commercial banks lending rate in U.S. dollars 4/	16.3	15.3	13.5	11.9	...	9.4
Yield on treasury bills in local currency 4/	13.6	14.7	12.9	17.2	...	12.6
Yield on treasury bills in U.S. dollars 4/	8.9	9.1	5.6	4.9	...	2.4
External sector (US$ million) 2/						
Current account	-488	-446	-276	-338	-245	-218
(Percent of GDP)	-5.9	-5.3	-3.4	-4.3	-3.2	-2.8
Capital and financial account	515	408	255	45	294	265
Of which: foreign direct investment	1,014	701	666	654	647	600
Overall balance	26	-39	-21	-293	49	48
Exceptional financing 5/	16	15	9	17	16	17
Merchandise export volume, percent change	-1.2	13.2	6.0	9.1	4.5	2.0
Merchandise import volume, percent change	-6.8	3.1	-3.5	9.1	-0.8	-6.4
Terms of trade, percent change (deterioration -)	1.4	3.6	0.5	-1.6	1.3	2.8
Gross international reserves 6/						
(Months of imports of goods and services)	8.7	8.7	8.1	6.3	6.9	6.9
(In percent of broad money)	40.2	39.7	39.2	34.6	37.3	38.2
Disposable reserves in percent of dollar deposits 7/	37.7	39.5	39.4	31.6	35.1	36.1
Public sector external debt (US$ billion) 3/	4.6	4.5	3.3	3.7	4.3	4.2
Exchange rates						
Bolivianos/U.S. dollar (end-of-period) 8/	6.00	6.40	6.83	7.50	7.61	7.63
REER (percentage change during year) 9/	2.2	-1.5	-3.4	4.4	...	-11.1
REER, period average (percentage change) 9/	1.4	-1.6	-1.8	3.0	...	-6.3
Memorandum items:						
Overall fiscal balance (in percent of GDP) 10/	-3.9	-4.4	-7.7	-9.6	-7.3	-7.2
External current account balance (in percent of GDP) 10/	-6.7	-6.0	-4.4	-5.6	-4.5	-4.1

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

1/ As percent of the program GDP (nominal GDP has been revised upward since the April SBA, due to a statistical revision of real growth for 2000-02).

2/ Includes actual and anticipated assistance under the HIPC Initiative, using the HIPC accounting conventions. External financing for 2002 includes a US$100 million (1.3 percent of GDP) transfer of foreign liabilities from the central bank to the central government in 2002.

3/ External debt indicators reflect assistance under the original and enhanced HIPC Initiatives, and beyond HIPC relief; includes obligations to the Fund and debt with public guarantee. Domestic debt is the nonfinancial public sector debt, excluding bonds issued for the recapitalization of the central bank.

4/ Weighted average yields of different maturities, as of the latest auction held; May 21 (May 18 for the commercial bank lending rate in U.S. dollars) for 2003.

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

6/ Gross official reserves (including restricted deposits, excluding reserves from the Latin American Reserve Fund, FLAR) plus commercial banks' liquid asset requirement (RAL) held overseas. End-2002 figures reflect an increase of US$45 million in the valuation of holdings of gold; import coverage for the following year.

7/ Ratio of central bank gross disposable reserves (excluding gold holdings but including restricted deposits) plus commercial banks' liquid asset requirement (RAL) held overseas to dollar deposits in the banking system.

8/ Official (sell) exchange rate.; June 5 for 2003.

9/ Weights based on average trade, excluding trade related to natural gas, in 1996-97. Preliminary estimates for December 2002. Data for 2003 refers to May (or average January-May) based on exchange rate data available as of June 5, and Fund staff CPI projections. Positive variation is an appreciation.

10/ According to previous accounting conventions (before HIPC).

Table 3. Bolivia: Summary Balance of Payments

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

	1999	2000	2001	2002	2003 Prog.	2003 Rev. Proj. 1/	Proj. 2004	2005	2006	2007	2008
Current account	**-488**	**-446**	**-276**	**-338**	**-245**	**-218**	**-236**	**-231**	**-246**	**-255**	**-268**
Trade balance	-704	-584	-423	-460	-344	-305	-255	-185	-209	-132	-53
Exports, f.o.b.	1,051	1,246	1,285	1,310	1,435	1,436	1,573	1,708	1,749	1,869	2,010
Of which: gas	36	122	237	264	374	346	483	587	570	564	564
Imports, c.i.f.	-1,755	-1,830	-1,708	-1,770	-1,779	-1,741	-1,829	-1,893	-1,957	-2,002	-2,064
Of which: capitalization and pipeline	...	-161	-136	-235	-84	-84	-24	-12	0	0	0
Services (net)	26	-24	-36	-43	-54	-54	-56	-61	-60	-63	-66
Income (net)	-196	-226	-210	-202	-224	-252	-260	-316	-355	-426	-469
Of which: interest due on external public sector debt 1/	-126	-130	-115	-98	-105	-107	-117	-127	-136	-136	-140
Of which: investment income (net)	-52	-146	-165	-177	-197	-197	-220	-256	-297	-375	-422
Transfers (net)	386	387	393	367	377	393	336	330	378	366	320
Of which: HIPC assistance from grants	62	57	65	80	68	69	69	64	62	55	54
Capital and financial account	**515**	**408**	**255**	**45**	**294**	**265**	**322**	**318**	**367**	**357**	**385**
Capital transfers	0	0	3	2	2	0	0	0	0	0	0
Direct investment (net)	1,014	701	666	654	647	600	809	1,053	1,117	937	774
Of which: from capitalization	506	194	171	47	46	46	30	15	0	0	0
Portfolio investment (net)	-61	55	-23	-83	-86	-185	-150	-250	-250	-200	-200
Public sector loans	113	112	189	321	452	430	326	139	141	131	135
Disbursements	280	292	364	577	733	733	545	394	412	375	375
Amortization 2/	-167	-180	-175	-256	-281	-303	-219	-255	-272	-245	-240
Banks' net foreign assets, excl. liquid asset requirement	-159	-369	-401	16	-142	-137	0	0	9	9	7
Nonbank private sector loans	-12	-16	-50	59	180	167	175	0	-50	-50	50
Other, including errors and omissions	-380	-75	-128	-926	-759	-610	-838	-624	-599	-469	-381
Overall balance	**26**	**-39**	**-21**	**-293**	**49**	**48**	**86**	**87**	**121**	**102**	**117**
Exceptional financing	**16**	**15**	**9**	**17**	**16**	**17**	**14**	**13**	**9**	**8**	**8**
Of which: HIPC assistance from rescheduling	16	15	9	17	16	17	14	13	9	8	8
Net international reserves (increase -)	**-42**	**23**	**29**	**275**	**-65**	**-65**	**-100**	**-100**	**-130**	**-110**	**-125**
Memorandum items:											
Gross official reserves (end-of-period) 3/	1,211	1,162	1,116	854	992	993	1,070	1,116	1,158	1,204	1,304
(In months of imports of goods and services) 3/ 4/	7.0	7.0	6.5	5.0	5.6	5.6	5.8	5.9	5.9	6.0	6.0
Gross international reserves (end-of-period) 3/ 5/	1,498	1,436	1,375	1,073	1,227	1,227	1,304	1,350	1,393	1,439	1,538
(In months of imports of goods and services) 3/ 4/	8.7	8.7	8.1	6.3	6.9	6.9	7.1	7.1	7.1	7.1	7.1
Total HIPC assistance and beyond HIPC relief	85	80	99	159	157	171	161	154	138	130	124
Original HIPC framework	85	79	59	43	39	39	35	33	27	25	25
Of which: assistance from debt reduction	7	7	8	7	9	10	10	10	10	9	9
Enhanced HIPC framework	...	1	28	84	82	87	78	73	66	60	56
Of which: assistance from debt reduction	...	1	5	22	28	30	21	18	12	11	10
Beyond HIPC and other debt relief	...	0	12	32	35	44					
(In percent)											
Export volume growth	-1.2	13.2	6.0	9.1	4.5	2.0	10.2	8.7	1.0	5.4	6.0
Import volume growth	-6.8	3.1	-3.5	9.1	-0.8	-6.4	2.9	2.1	2.0	0.9	1.7
Nonexceptional import volume growth	...	...	-3.5	7.6	2.6	9.7	-4.2	-3.4	-1.7	2.8	10.3
Terms of trade change	1.4	3.6	0.5	-1.6	1.3	2.8	0.0	0.0	0.0	0.0	0.0
(In percent of GDP)											
Current account	-5.9	-5.3	-3.4	-4.3	-3.2	-2.9	-3.1	-2.9	-2.9	-2.9	-2.9
Current account before HIPC assistance 6/	-6.7	-6.0	-4.4	-5.6	-4.5	-4.1	-4.2	-4.0	-3.9	-3.7	-3.7
Merchandise exports	12.7	14.8	16.0	16.8	19.0	19.0	20.4	21.4	20.9	21.2	21.8
Merchandise imports	21.2	21.8	21.3	22.7	23.6	23.1	23.7	23.7	23.3	22.7	22.3
Of which: capitalization and pipeline	4.9	1.9	1.7	3.0	1.1	1.1	0.3	0.2	0.0	0.0	0.0
Direct investment (net)	12.2	8.3	8.3	8.4	8.6	7.9	10.5	13.2	13.3	10.6	8.4
Grants and loans 7/	5.5	5.7	6.8	9.6	12.5	12.7	9.2	7.0	7.6	6.6	5.9
NPV of debt to GNFS exports (3-year backward moving avg.)	221.0	199.3	100.2	119.4	136.5	137.0	141.5	137.1	136.8	138.0	139.7
External debt service to GNFS exports	...	20.4	18.1	12.5	17.6	17.9	17.0	17.4	19.6	16.1	13.8

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

1/ As percent of the program GDP (nominal has been revised upward since the April SBA, due to a statistical revision of real growth for 2000-02).
2/ Reflects lower scheduled debt service, starting in 1998, owing to original HIPC assistance in the form of stock-of-debt reduction.
3/ Including restricted deposits; excluding reserves from the Latin American Reserve Fund (FLAR).
4/ In months of imports of goods and services in the following year.
5/ Commercial banks' liquid asset requirement (RAL) held overseas added to central bank gross official reserves.
6/ Before any assistance under the HIPC Initiative.
7/ Official transfers and loans to the public sector, excluding HIPC debt relief.

Table 4. Bolivia: Operations of the Combined Public Sector

(In percent of GDP)

	1999	2000	2001	2002	2003 Prog.	2003 Rev. Proj. 1/
Balance excluding pensions (deficit -)	**0.6**	**0.7**	**-2.1**	**-3.9**	**-1.6**	**-1.6**
Current revenue	23.2	22.8	22.9	22.5	24.1	23.2
General government	23.1	22.3	22.1	21.9	23.9	23.0
Taxes	18.6	18.7	18.1	18.0	20.6	19.6
Hydrocarbons	5.3	5.1	5.1	4.7	5.5	5.0
Other	13.4	13.6	13.0	13.4	15.1	14.6
Nontax revenue	4.5	3.6	3.9	3.8	3.3	3.4
Public enterprise operating balance	-0.3	0.0	0.3	0.1	-0.1	-0.1
Central bank operating balance	0.4	0.5	0.5	0.5	0.3	0.3
Current expenditure of general government	18.1	17.8	19.2	20.2	20.1	20.1
Wages	8.6	8.3	8.8	9.0	9.4	9.5
Interest	2.0	2.3	2.6	2.6	2.9	2.9
Other	7.6	7.2	7.7	8.6	7.8	7.8
Official grants	1.8	2.2	2.5	2.3	2.8	3.0
Of which: HIPC assistance from grants	0.8	0.8	0.9	0.8	0.9	0.9
Capital revenue	0.8	0.6	0.1	0.0	0.2	0.2
Capital expenditure	7.1	7.1	8.5	8.5	8.6	7.9
General government	6.9	6.9	8.3	8.4	8.5	7.9
Public enterprises	0.2	0.2	0.2	0.2	0.0	0.0
Pension-related balance (deficit -)	**-4.1**	**-4.5**	**-4.8**	**-5.0**	**-4.9**	**-4.9**
Revenue	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure	4.1	4.5	4.8	5.0	4.9	4.9
Pensions	3.7	4.1	4.4	4.6	4.5	4.5
General government employer contributions	0.4	0.3	0.4	0.4	0.4	0.4
Overall balance (deficit -)	**-3.5**	**-3.7**	**-6.9**	**-8.9**	**-6.5**	**-6.5**
Financing	**3.5**	**3.7**	**6.9**	**8.9**	**6.5**	**6.5**
External 2/	1.9	2.0	3.1	6.1	6.4	6.4
Of which: HIPC assistance from refinancing	0.2	0.2	0.1	0.2	0.2	0.2
Domestic	1.6	1.8	3.9	2.8	0.1	0.1
Central bank	-1.4	0.4	-0.5	1.7	-0.4	-0.4
Commercial banks	-0.2	0.4	0.9	0.2	0.0	-0.1
Pension funds	1.9	1.7	1.7	1.7	1.9	1.9
Other	1.3	-0.7	1.8	-0.7	-1.3	-1.2
Memorandum items:						
Overall balance before grants (deficit -)	-5.3	-6.0	-9.4	-11.2	-9.3	-9.5
Overall balance excluding grants and hydrocarbons (deficit -)	-10.6	-11.1	-14.5	-15.9	-14.8	-14.5
Primary deficit (-)	-1.5	-1.5	-4.3	-6.3	-3.6	-3.6
Savings	2.9	2.8	1.4	-0.4	1.9	1.2
Military expenditure	2.2	2.1	2.4	2.4	...	...
Poverty reducing expenditure 3/ 4/	10.6	10.8	12.2	12.2	12.9	12.7
Total assistance under the HIPC Initiative	1.0	1.0	1.1	1.6	1.6	1.7
Original HIPC	1.0	0.9	0.7	0.5	0.5	0.5
Enhanced HIPC	...	...	0.3	1.1	1.1	1.2
HIPC assistance from stock-of-debt reduction	0.1	0.1	0.2	0.4	0.5	0.5
On interest	0.1	0.1	0.1	0.2	0.2	0.2
On amortization	0.0	0.0	0.1	0.2	0.3	0.3
GDP (in billions of bolivianos)	48.2	51.9	53.0	55.9	58.4	58.4

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

1/ As percent of the program GDP (nominal has been revised upward since the April SBA, due to a statistical revision of real growth for 2000-02).

2/ Includes a US$100 million (1.3 percent of GDP) transfer of foreign liabilities from the central bank to the central government in 2002.

3/ Preliminary data for 2002 and projections for 2003.

4/ Figures have been revised upwards starting in 2002, by Bs. 197.2 mill. in 2002 and by Bs 231.9 mill. in 2003, to include spending on the national emergency employment program (PLANE)

Table 5. Bolivia: Monetary Survey 1/

	1999	2000	2001	2002	2003 Prog.	2003 Rev. Proj. 2/
			I. Central Bank			
			(In percent of currency issue at beginning of period)			
Net international reserves 3/	10.2	-6.0	-7.7	-71.7	16.5	16.5
(Flow in millions of U.S. dollars)	42.3	-23.4	-28.5	-275.4	65.0	65.0
Net domestic assets	-10.2	6.2	19.1	84.2	-8.1	-8.1
Net credit to nonfinancial public sector	-28.0	8.5	-11.1	34.6	-8.5	-8.5
Net credit to financial intermediaries	6.4	-20.6	4.1	4.0	-6.7	-6.3
Of which: open market operations	-2.1	16.0	6.7	5.8	-4.4	-7.3
Medium- and long-term net foreign liabilities	8.1	8.7	16.6	39.1	4.3	1.6
(Flow in millions of U.S. dollars, increase -)	33.3	33.9	61.0	150.1	16.1	5.9
Other	3.4	9.6	9.6	6.4	2.8	5.2
Currency issue	0.0	0.2	11.4	12.5	8.5	8.5
			II. Banking System			
			(In percent of broad money at beginning of period)			
Net short-term foreign assets	5.9	6.6	9.1	-10.8	6.9	6.4
(Flow in millions of U.S. dollars)	221.5	244.4	329.3	-379.2	214.0	198.7
Net domestic assets	-6.6	-8.6	-11.1	0.7	0.6	-1.4
Net credit to the public sector	-3.5	1.7	0.8	4.2	-1.1	-1.2
Credit to the private sector	-1.9	-10.7	-15.2	-9.3	3.7	1.8
Medium- and long-term net foreign liabilities	0.7	3.3	1.5	4.7	0.9	-1.1
(Flow in millions of U.S. dollars, increase -)	27.1	122.7	54.2	164.7	26.3	-33.8
Other	-1.9	-2.9	1.8	1.1	-2.9	-0.9
Broad money	-0.7	-2.0	-2.0	-10.1	7.5	5.0
			(12-month percentage change)			
Broad money 4/	-0.7	-2.0	-2.0	-10.1	7.5	5.0
Liabilities in bolivianos (M2)	-2.5	3.8	13.7	2.6	7.8	11.0
Foreign currency deposits 5/	-0.9	-2.6	-4.6	-12.3	7.5	3.7
Credit to private sector	-1.6	-8.8	-13.4	-9.2	3.6	1.7
Credit in bolivianos	-3.4	-2.3	-14.8	-15.4	3.6	1.7
Foreign currency credit 5/	-1.5	-9.0	-13.4	-9.1	3.6	1.7
Memorandum items:						
			(Average stock in percent of GDP)			
Currency issue	4.2	3.8	4.0	4.1	4.2	4.2
Broad money 4/	45.1	43.3	43.6	38.8	36.6	38.4
Credit to private sector	48.3	52.3	46.9	42.0	38.8	40.5
			(In percent of total deposits or credit at current exchange rates)			
Dollarization (end-period stocks)						
Foreign currency deposits 5/	92.9	92.6	91.5	91.9	92.6	91.9
Foreign currency credit 5/	96.3	96.3	97.1	97.5	97.5	97.5
			(12-month percentage change at current exchange rates)			
Broad money 4/	4.2	3.4	3.4	-3.0	13.4	10.7
Credit to private sector	4.1	-2.6	-8.5	-0.5	10.3	8.3
			(12-month percentage change in U.S. dollars at current exchange rates)			
Broad money 4/	-1.8	-3.3	-3.1	-11.7	6.3	3.8
Credit to private sector	-2.0	-9.0	-14.3	-9.4	3.4	1.5

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 bank, commercial banks, the National Financial Institution of Bolivia and FONDESIF, which are state-owned second-tier banks.

2/ As percent of the program GDP (nominal has been revised upward since the April SBA, due to a statistical revision of real growth for 2000-02).

3/ Include restricted deposits.

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

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

Table 6. Bolivia: Commercial Bank Performance Indicators

(In percent)

	1999	2000	2001 Mar.	2001 Jun.	2001 Sep.	2001 Dec	2002 Mar.	2002 Jun.	2002 Sep.	2002 Dec.	2003 Mar.	2003 Apr. 1/
Profitability												
Ratios to total assets (period average) 2/												
Operating income	4.9	3.5	4.1	4.2	3.9	3.7	3.9	4.2	4.0	4.1	6.0	8.1
Profit before tax	1.2	-0.4	0.4	0.5	0.1	0.0	0.3	0.6	0.5	0.4	0.5	0.7
Ratios to equity capital (period average) 2/												
Profit before tax	13.2	-4.3	3.6	4.6	1.4	-0.5	3.0	5.7	4.5	3.5	3.9	6.5
Profit after tax	8.7	-8.6	-0.5	0.6	-2.4	-4.1	0.2	2.8	1.7	0.6	0.4	1.4
Asset quality												
Ratios to total loans (end-of-period)												
Past due loans up to 30 days	...	1.3	2.7	1.8	2.8	1.8	2.5	2.2	2.7	...	...	....
Nonperforming loans 3/	6.6	10.3	12.7	14.0	15.9	14.4	15.8	16.7	18.9	17.6	20.1	20.3
Nonperforming loans and nonperforming assets	8.6	13.7	16.9	18.9	21.4	20.6	22.4	23.6	26.5	25.7	28.0	28.2
Nonperforming loans net of provisions 3/	2.9	5.2	8.7	8.3	10.2	7.0	8.4	8.5	10.6	6.4	7.4	7.6
Liquidity												
Ratios to total deposits (end-of-period)												
Total loans	112.7	102.4	98.9	97.3	97.1	93.1	95.1	99.1	102.6	94.6	96.5	96.2
Total liquid assets	29.7	27.2	26.9	28.0	24.9	30.2	25.2	28.8	29.5	30.2	31.3	30.3
Capital adequacy												
Ratio of qualifying capital to total risk-weighted assets (end-of-period)	12.2	13.5	13.8	13.8	14.0	14.3	15.5	16.0	16.5	16.1	16.5	15.8

Sources: Superintendency of Banks; and Fund staff estimates.

1/ Provisional data.

2/ Averages in 2001 and 2002 are cumulative from January of each year.

3/ Adjusted to exclude the estimated share of loans overdue by less than one month, which were included in official statistics prior to January 2000; since December 2002, reported nonperforming loans exclude loans overdue by less than a month.

Table 7. Bolivia: Financial and External Vulnerability Indicators

(In percent; end of period; unless otherwise indicated)

	1999	2000	2001	2002	2003
Financial indicators					
Nonfinancial public sector debt/GDP 1/	59.5	58.6	53.6	61.3	67.6
of which in domestic currency (percent of GDP) 1/	2.7	2.2	2.8	3.3	10.1
Lending rate in domestic currency 2/ 3/	15.4	18.0	15.8	12.7	21.9
Lending rate in U.S. dollars 2/ 3/	16.3	15.3	13.5	11.9	9.4
Velocity of money 4/	2.2	2.3	2.4	2.8	2.9
Credit to the private sector/GDP 5/	48.3	52.3	44.5	38.3	36.9
Share of foreign currency deposits in total deposits	92.9	92.6	91.5	91.9	91.9
Share of foreign currency loans in total credit	96.3	96.3	97.0	97.3	97.5
Nonperforming loans/total loans 6/ 7/	6.6	10.3	14.4	17.6	20.3
Loan-loss provisions/nonperforming loans 6/ 7/	55.8	61.4	63.7	63.7	62.5
Risk-based capital-assets ratio 6/	12.2	13.5	14.3	16.1	15.8
Foreign currency deposits at commercial banks (in millions of U.S. dollars)	3,349	3,042	2,891	2,521	2,613
Commercial banks' net short-term foreign assets (in millions of U.S. dollars)	-15	252	610	506	640
Disposable reserves in percent of dollar deposits 8/	37.7	39.5	39.4	31.6	36.1
External indicators					
Exports, U.S. dollars (percent change)	-4.8	18.6	3.1	2.0	9.6
Imports, U.S. dollars (percent change)	-11.5	4.3	-6.7	3.7	-1.6
Terms of trade (percent change)	1.4	3.6	0.5	-1.6	2.8
Real effective exchange rate, (percent change) 9/	2.2	-1.5	-3.4	4.4	-11.1
Current account balance (percent of GDP)	-5.9	-5.3	-3.4	-4.3	-2.8
Capital and financial account balance (percent of GDP)	6.2	4.9	3.2	0.6	3.5
Total external debt (percent of GDP) 10/	...	59.5	46.9	53.3	59.2
Medium- and long-term public debt (percent of GDP) 1/	55.1	53.1	41.4	47.4	54.9
Medium- and long-term private debt (percent of GDP) 10/	...	4.2	3.4	3.6	3.3
Short-term public and private debt (percent of GDP) 10/	...	2.3	2.2	2.3	0.9
Total external debt (percent of exports of goods and services) 10/	...	340.4	247.8	269.2	270.6
Gross international reserves (in millions of U.S. dollars) 11/ 12/	1,498	1,436	1,375	1,073	1,227
Gross official reserves, percent of short-term external debt 11/ 12/ 13/	...	44.4	44.9	39.8	45.7
Gross international reserves, percent of broad money 11/ 12/	40.2	39.7	39.2	34.6	38.2
Gross international reserves (in months of imports of goods and services) 11/ 12/	8.7	8.7	8.1	6.3	6.9
Net international reserves (in millions of U.S. dollars) 11/	1,089	1,066	1,048	810	875

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

1/ Debt indicators reflect assistance under the HIPC Initiative, which first became available after September 1998, as well as the relief under the enhanced HIPC Initiative and beyond HIPC. Includes obligations to the Fund and debt with public guarantee. For 2003, new debt with the pension funds is issued in inflation-indexed units (UFVs).

2/ Financial sector effective interest rates.

3/ Data for 2003 correspond to May 21

4/ Defined as the inverse of the annual average ratio of broad money to annual GDP.

5/ Annual average stock.

6/ Data for 2003 correspond to end of April.

7/ Nonperforming loans are adjusted to exclude the estimated share of loans overdue by less than one month, which were included in official statistics prior to January 2000.

8/ Ratio of central bank gross disposable reserves (excluding gold holdings but including restricted deposits) plus commercial banks' liquid asset requirement (RAL) held overseas to dollar deposits in the banking system.

9/ Weights based on average trade, excluding trade related to natural gas, in 1996-97. Positive variation is an appreciation. Data for 2003 refers to May based on exchange rate data available as of June 5, and Fund staff CPI projections.

9/ Weights based on average trade, excluding trade related to natural gas, in 1996-97. Positive variation is an appreciation.

10/ Staff estimate.

11/ Gross reserves exclude reserves from the Latin American Reserve Fund (FLAR) and include restricted deposits. Import coverage for the following year. From end-2002 on, figures reflect an increase of US$45 million in the valuation of holdings of gold.

12/ Commercial banks' liquid asset requirement (RAL) held overseas added to central bank gross official reserves.

13/ Short-term external debt by remaining maturity, added to foreign currency deposits at commercial banks.

Table 8. Bolivia. Public Sector, External Debt and Debt Service, 2000–08

				Proj.					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
			(in millions of U.S. dollars)						
Total external debt									
By debtor 1/	4,460	3,325	3,725	4,211	4,481	4,552	4,577	4,619	4,708
Nonfinancial public sector	3,960	2,893	3,300	3,705	4,004	4,116	4,240	4,353	4,476
Financial public sector	500	433	425	506	478	436	338	265	231
By creditor	4,460	3,325	3,725	4,211	4,481	4,552	4,577	4,619	4,708
Multilateral	3,077	3,175	3,537	4,046	4,325	4,405	4,430	4,452	4,526
Bilateral	1,364	142	183	149	129	108	110	123	134
Commercial	19	8	6	15	27	39	37	43	47
Total debt service obligations	349	342	409	435	432	475	544	491	445
Principal	213	216	288	293	290	324	387	334	286
Interest	136	126	122	141	142	151	157	157	160
Debt service paid	268	248	253	279	294	327	392	346	314
Principal	173	165	193	196	206	235	294	245	207
Interest	96	83	61	84	89	92	97	101	108
Debt service relief	80	99	159	178	162	154	138	129	124
Principal	39	52	98	108	105	102	90	84	81
Interest	41	47	61	70	56	53	48	45	43
Memorandum items:									
Total HIPC assisance and beyond HIPC relief	80	99	159	178	162	154	138	129	124
HIPC I	79	59	43	39	35	33	27	25	25
HIPC II	1	28	84	87	78	73	66	60	56
Beyond HIPC and other	0	12	32	51	49	48	46	45	43
(In percent of GDP)				(In percent of GDP)					
Total external debt	53.1	41.4	47.7	54.9	57.9	57.0	54.6	52.3	50.9
Nonfinancial public sector	47.1	36.0	42.2	48.3	51.8	51.5	50.5	49.3	48.4
Financial public sector	6.0	5.4	5.4	6.6	6.2	5.5	4.0	3.0	2.5
(In percent of exports of goods and services 2/)				(In percent of exports of goods and services 2/)					
Total debt service obligations	25.3	23.8	27.1	27.5	25.7	26.1	28.1	24.0	20.7
Principal	15.4	15.1	19.0	18.6	17.2	17.8	20.0	16.4	13.3
Interest	9.9	8.8	8.0	8.9	8.5	8.3	8.1	7.7	7.4

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

1/ Total external debt excludes bilateral beyond-HIPC relief which has been granted but not formally signed.

Table 9. Bolivia: Gross Domestic Debt of the Nonfinancial Public Sector, 2000–08
(In million of U.S. dollars)

				Proj.					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
Domestic debt	966.9	1,410.5	1,499.3	1,528.7	1,581.5	1,679.9	1,749.9	1,801.5	1,817.6
Treasury bills and bonds	778.9	1,186.1	1,266.4	1,179.0	1,236.2	1,276.7	1,308.3	1,332.3	1,334.2
Treasury Bills "C"	156.7	162.9	101.7	...	...	...	...	...	...
Commercial banks	88.0	73.6	68.4	...	...	...	...	...	...
Nonbank financial institutions	18.0	83.9	9.1	...	...	...	...	...	...
Nonfinancial private sector	50.7	5.4	24.2	...	...	...	...	...	...
Treasury bonds	622.1	1,023.3	1,164.7	...	...	...	...	...	...
Commercial Banks	21.2	105.8	118.0	...	...	...	...	...	...
Nonbank financial institutions	0.0	19.2	62.9	...	...	...	...	...	...
Nonfinancial private sector	69.2	238.8	163.9	...	...	...	...	...	...
Pension funds (AFPs)	517.0	654.0	819.9	...	...	...	...	...	...
Other 1/	14.7	5.4	...	...	...	...	...	...	...
Credit	81.8	117.4	138.4	...	...	...	...	...	...
Central Bank	68.3	107.5	131.8	...	...	...	...	...	...
Emergency	...	47.6	35.5	...	...	...	...	...	...
Liquidity	...	59.9	96.3	...	...	...	...	...	...
Financial system	13.5	9.9	6.7	...	...	...	...	...	...
Other	106.2	106.9	130.9	...	...	...	...	...	...
Contractors	3.2	0	0	...	...	...	...	...	...
Floating Debt	28.9	47.9	39.3	...	...	...	...	...	...
Current	28.9	17.1	28.3	...	...	...	...	...	...
Wages and salaries	5.6	1.6	17.4	...	...	...	...	...	...
Goods and services	23.2	15.4	10.8	...	...	...	...	...	...
Capital expenditure	0.1	0.1	0.1	...	...	...	...	...	...
Floating debt (hydrocarbons)	...	30.8	11.0	...	...	...	...	...	...
Municipal bonds	3.5	0.0	0.0	...	...	...	...	...	...
Other	70.6	59.0	91.6						
Memorandum items:									
Government deposits	727.8	780.2	615.8	...	...	...	...	...	...
Central Bank	686.8	715.1	574.2	...	...	...	...	...	...
Unofficial deposits	32.7	57.7	34.1	...	...	...	...	...	...
Financial system	8.2	7.5	7.6	...	...	...	...	...	...
Central Bank capitalization bonds 2/	682.6	682.6	682.6	682.6	682.6	682.6	682.6	682.6	682.6
"A"	530.5	530.5	530.5	530.5	530.5	530.5	530.5	530.5	530.5
"B"	152.1	152.1	152.1	152.1	152.1	152.1	152.1	152.1	152.1
(In percent of GDP)				(In percent of GDP)					
Gross domestic debt	11.5	17.6	19.2	19.9	20.4	21.0	20.9	20.4	19.7
Net domestic debt	-8.7	-9.7	-7.9	...	...	...	...	...	...

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

1/ Includes bonds held by FONVIS, and FONDESIF.

2/ Issued for the recapitalization of the BCB.

Table 10. Bolivia: Medium-Term Macroeconomic Framework

	1999	2000	2001	2002	Proj. 2003	2004	2005	2006	2007	2008
	(Annual percentage change)									
Economic growth and prices										
Real GDP at market prices	0.4	2.3	1.5	2.8	2.9	4.3	4.7	5.1	5.4	5.0
Of which: Excluding hydrocarbons	0.7	1.8	1.5	2.6	2.5	2.7	3.6	4.3	4.3	4.3
Real domestic demand 1/	-2.0	1.2	-2.5	1.6	1.2	2.4	3.0	5.5	4.4	4.0
GDP deflator	2.4	5.3	0.7	2.7	3.0	2.3	3.1	3.7	3.3	3.3
CPI (period average)	2.2	4.6	1.6	0.9	2.6	3.1	3.5	3.2	3.0	3.0
CPI (end of period)	3.1	3.4	0.9	2.4	2.8	3.5	3.5	3.0	3.0	3.0
	(In percent of nominal GDP)									
Gross investment	**18.8**	**18.3**	**14.2**	**14.7**	**14.2**	**14.8**	**15.6**	**16.7**	**17.4**	**18.1**
Public investment 2/	5.0	5.2	5.8	5.4	4.9	5.1	5.1	5.1	5.1	5.4
Private investment, including stockbuilding	13.8	13.1	8.5	9.4	9.3	9.7	10.5	11.6	12.3	12.7
Savings	**18.8**	**18.3**	**14.2**	**14.7**	**14.2**	**14.8**	**15.6**	**16.7**	**17.4**	**18.1**
Gross national savings	12.9	13.0	10.8	10.4	11.4	11.8	12.7	13.8	14.5	15.2
Public savings	2.9	2.8	1.4	-0.4	1.2	3.4	4.5	5.2	5.7	6.6
Private savings	10.0	10.2	9.4	10.8	10.1	8.4	8.3	8.6	8.8	8.6
External savings	5.9	5.3	3.4	4.3	2.8	3.1	2.9	2.9	2.9	2.9
Consolidated public sector										
Non-pension balance	0.6	0.7	-2.1	-3.9	-1.6	0.5	1.3	1.9	2.2	2.5
Pension-related balance	-4.1	-4.5	-4.8	-5.0	-4.8	-5.1	-4.8	-4.8	-4.6	-4.4
Overall balance	-3.5	-3.7	-6.9	-8.9	-6.4	-4.6	-3.5	-2.9	-2.4	-2.0
Net domestic financing	1.6	1.8	3.9	2.8	0.1	0.7	1.2	0.8	0.6	0.2
Net external financing	1.9	2.0	3.1	6.1	6.3	3.9	2.2	2.1	1.8	1.8
External sector										
Current account balance	-5.9	-5.3	-3.4	-4.3	-2.8	-3.1	-2.9	-2.9	-2.9	-2.9
Net foreign direct investment	12.2	8.3	8.3	8.4	7.8	10.5	13.2	13.3	10.6	8.4
Memorandum items:										
Nominal GDP (millions of U.S. dollars)	8,298	8,405	8,036	7,812	7,667	7,730	7,984	8,385	8,821	9,239

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

1/ Based on balance of payments figures from the Central Bank of Bolivia, and Fund staff estimates and projections.
2/ Based on information from the Ministry of Finance, and Fund staff estimates and projections.

Table 11. Bolivia: Medium-Term Macroeconomic Framework: Alternative Scenario

	1999	2000	2001	2002	Projections 2003	2004	2005	2006	2007	2008
	(Annual percentage change)									
Economic growth and prices										
Real GDP at market prices	0.4	2.3	1.5	2.8	2.9	3.6	3.6	3.7	3.9	4.0
Of which: Excluding hydrocarbons	0.7	1.8	1.5	2.6	2.5	2.5	2.8	3.1	3.3	3.6
Real domestic demand 1/	-2.0	1.2	-2.5	1.6	1.2	2.7	3.5	3.9	2.6	3.0
GDP deflator	2.4	5.3	0.7	2.7	3.0	2.8	3.2	3.4	3.2	3.2
CPI (period average)	2.2	4.6	1.6	0.9	2.6	3.1	3.5	3.2	3.0	3.0
CPI (end of period)	3.1	3.4	0.9	2.4	2.8	3.5	3.5	3.0	3.0	3.0
	(In percent of nominal GDP)									
Gross investment	**18.8**	**18.3**	**14.2**	**14.7**	**14.2**	**14.4**	**14.7**	**14.9**	**15.2**	**15.4**
Public investment 2/	5.0	5.2	5.8	5.4	4.9	5.1	5.2	5.2	5.3	5.7
Private investment, including stockbuildin	13.8	13.1	8.5	9.4	9.3	9.3	9.5	9.7	9.9	9.7
Savings	**18.8**	**18.3**	**14.2**	**14.7**	**14.2**	**14.4**	**14.7**	**14.9**	**15.2**	**15.4**
Gross national savings	12.9	13.0	10.8	10.4	11.3	11.1	10.3	10.3	10.8	10.9
Public savings	2.9	2.8	1.4	-0.4	1.2	3.1	4.0	4.5	4.8	5.5
Private savings	10.0	10.2	9.4	10.8	10.1	8.0	6.3	5.8	6.0	5.4
External savings	5.9	5.3	3.4	4.3	2.8	3.3	4.4	4.6	4.4	4.4
Consolidated public sector										
Non-pension balance	0.6	0.7	-2.2	-4.0	-1.6	0.2	0.8	1.2	1.2	1.2
Pension-related balance	-4.1	-4.5	-4.8	-5.0	-4.8	-5.1	-4.9	-5.0	-4.8	-4.7
Overall balance	-3.5	-3.7	-7.0	-8.9	-6.4	-4.9	-4.1	-3.8	-3.6	-3.5
Net domestic financing	1.6	1.8	3.9	2.8	0.1	1.0	1.8	1.7	1.7	1.6
Net external financing	1.9	2.0	3.1	6.1	6.3	3.6	2.1	1.9	1.7	1.7
External sector										
Current account balance	-5.9	-5.3	-3.4	-4.3	-2.8	-3.3	-4.4	-4.6	-4.4	-4.4
Net foreign direct investment	12.2	8.3	8.3	8.4	7.8	7.9	11.3	12.5	9.9	7.8
Memorandum items:										
Nominal GDP (millions of US dollars)	8,298	8,405	8,036	7,812	7,667	7,716	7,887	8,145	8,442	8,750

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

1/ Based on balance of payments figures from the Central Bank of Bolivia, and Fund staff estimates and projections.
2/ Based on information from the Ministry of Finance, and Fund staff estimates and projections.

Table 12. Bolivia: External Financing, 2002–08

(In millions of U.S. dollars)

	Prel.	2003		Proj.				
	2002	Prog.	Proj.	2004	2005	2006	2007	2008
Public sector 1/								
Gross disbursements	577	733	733	475	394	412	375	375
Nonconcessional	357	336	316	141	112	145	151	175
Concessional	220	396	417	334	282	267	224	200
Net disbursements	386	452	437	264	147	149	139	142
Nonconcessional	124	80	60	-35	-93	-54	-17	19
Concessional	261	372	377	299	240	202	156	123
Nonfinancial Public Sector (NFPS, net)								
Gross disbursements	570	720	720	473	391	406	370	375
Net disbursements	373	480	457	285	165	164	154	164
World Bank 2/								
Gross disbursements 3/	104	204	190	138	104	101	95	95
Net disbursements	99	178	173	120	85	80	72	69
Inter-American Development Bank (IDB)								
Gross disbursements 4/	99	192	182	178	157	161	143	133
Net disbursements	34	58	91	86	71	79	67	57
Andean Development Corporation (CAF) 2/								
Gross disbursements	324	231	227.2	94	68	58	36	45
Net disbursements	195	112	134.1	10	-56	-69	-71	-47
Other (net)	45	132	59	69	65	74	85	86
Memorandum Items:								
Public sector external grants (excluding HIPC assistanc	**175**	**214**	**225**	**166**	**166**	**221**	**211**	**171**
Of which: nonfinancial public sector 5/	148	146	156.6	...	...	...	...	...
Of which: new grants	...	30	34	...	...	...	...	...
Belgium	...	5	5	...	...	...	...	...
Canada	...	3	3	...	...	...	...	...
Denmark	...	2	2	...	...	...	...	...
Germany	...	2	4	...	...	...	...	...
Netherlands	...	5	5	...	...	...	...	...
Sweden	...	0	7					
Spain	...	3	3	...	...	...	...	...
United Kingdom	...	3	3	...	...	...	...	...
United States	...	7	9	...	...	...	...	...
Public sector								
Nonconcessional borrowing, gross	**357**	**336**	**316**	**141**	**112**	**145**	**151**	**175**
CAF	324	231	252	94	68	58	36	45
IDB	5	4	4.9	3	0	0	0	0
IBRD	...	25	0	18	22	54	84	95
Other	28	76	59	26	23	33	32	35
Nonconcessional borrowing, net	**124**	**80**	**60**	**-35**	**-93**	**-54**	**-17**	**19**
CAF	195	112	134	10	-56	-69	-71	-47
IDB	-56	-60	-60	-62	-57	-47	-39	-38
IBRD	...	25	0	18	22	54	84	95
Other	-15	3	-14	0	-2	9	9	10

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

1/ Excludes Fund disbursements of US$102 million.

2/ The projection assumes that US$70 million nonconcessional borrowing for financial and corporate restructuring takes place in 2004, although the program ceiling would allow it to take place in 2003.

3/ Includes US$65 million balance of payments support in 2003.

4/ Includes US$50 million balance of payments supportin 2003.

5/ Includes US$28 million balance of payments support in 2003.

Table 13. External Financing Requirements and Sources, 2000–08
(In millions of U.S. dollars)

	2000	2001	2002	Proj. 2003	2004	2005	2006	2007	2008
1. Gross financing requirements	**-1,233**	**-1,137**	**-538**	**-951**	**-628**	**-816**	**-971**	**-917**	**-797**
External current account deficit (excl. official trar	-688	-527	-593	-511	-471	-461	-529	-522	-493
Debt amortization	-565	-626	-180	-272	-44	-255	-313	-286	-183
Medium and long term debt	-293	-255	-244	-148	-44	-255	-322	-295	-190
Public sector	-180	-175	-256	-303	-219	-255	-272	-245	-240
Commercial banks (net) 1/	-97	-31	-48	-12	0	0	0	0	0
Corporate private sector (net) 1/	-16	-50	59	167	175	0	-50	-50	50
Short-term debt 2/	-272	-371	64	-124	0	0	9	9	7
Repayment of arrears	0	0	0	0	0	0	0	0	0
Accumulation of gross international reserves 1/	49	46	262	-138	-77	-46	-43	-46	-100
IMF repurchases and repayments	-29	-29	-27	-29	-36	-53	-87	-64	-21
2. Available financing	**1,233**	**1,137**	**538**	**951**	**628**	**816**	**971**	**917**	**797**
Foreign direct investment (net)	701	666	654	600	809	1,053	1,117	937	774
Official creditors and donors 2/	533	615	832	1,027	780	625	695	642	600
Disbursements	292	364	577	733	545	394	412	375	375
Official transfers	242	251	255	294	235	230	283	266	225
Original or Enhanced HIPC	57	65	80	69	69	64	62	55	54
Other official transfers	185	187	175	225	166	166	221	211	171
IMF	15	24	0	102	15	0	0	0	0
Financing gap	0	0	0	0	0	0	0	0	0
Other flows 3/	-16	-168	-948	-778	-976	-862	-841	-661	-577

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

1/ Includes the Latin American Reserve Fund.
2/ Includes both loans and grants.
3/ Includes all other net financial flows, and errors and omissions.

Table 14. Bolivia: Poverty-Reducing Expenditure

	1999	2000	2001	2002	2003	
					Prog.	Proj. 1/
	(In millions of bolivianos)					
Current expenditure	**2,981**	**3,132**	**3,619**	**3,790**	**3,983**	**3,998**
Health 2/	1,150	1,249	1,415	1,465	1,588	1,588
Education (excl. university level) 2/	1,824	1,875	2,196	2,316	2,387	2,401
Other social expenditure 3/	7	9	8	8	9	9
Capital expenditure	**2,125**	**2,473**	**2,817**	**3,035**	**3,564**	**3,441**
Health	241	380	325	407	508	489
Education	446	521	706	827	878	818
Basic sanitation	577	568	490	355	443	433
Urban development	283	309	424	460	546	557
Rural development	578	694	873	986	1,188	1,145
Of which: rural roads	266	269	383	438	495	511
Total poverty-reducing expenditure	**5,106**	**5,605**	**6,436**	**6,824**	**7,547**	**7,439**
	(In percent of GDP)					
Current expenditure	6.2	6.1	6.9	6.8	6.8	6.9
Health 2/	2.4	2.4	2.7	2.6	2.7	2.7
Education (excl. university level) 2/	3.8	3.6	4.2	4.1	4.1	4.1
Other social expenditure 3/	0.0	0.0	0.0	0.0	0.0	0.0
Capital expenditure	4.4	4.8	5.4	5.4	6.1	5.9
Health	0.5	0.7	0.6	0.7	0.9	0.8
Education	0.9	1.0	1.3	1.5	1.5	1.4
Basic sanitation	1.2	1.1	0.9	0.6	0.8	0.7
Urban development	0.6	0.6	0.8	0.8	0.9	1.0
Rural development 4/	1.2	1.3	1.7	1.8	2.0	2.0
Of which: rural roads	0.6	0.5	0.7	0.8	0.8	0.9
Total poverty-reducing expenditure	**10.6**	**10.8**	**12.2**	**12.2**	**12.9**	**12.7**
Memorandum items:						
Poverty-reducing expenditure as a percentage of total public sector expenditure	36.1	36.8	37.4	36.2	38.5	38.6
Poverty-reducing investment (in percent of public investment)	61.8	67.3	62.7	63.6	71.4	73.2
Social expenditure (in millions of bolivianos) 4/	8,026	8,922	10,070	10,844	11,656	11,632
(In percent of GDP)	16.7	17.2	19.0	19.4	20.0	19.9

Source: Ministry of Finance.

1/ As percent of the program GDP.
2/ Excluding health and education spending by the Ministry of Defense.
3/ Social spending by prefectures.
4/ Excludes emergency employment program PLANE (0.4 percent of GDP in 2002 and 2003).
5/ Expenditure on health, education (including universities), and basic sanitation.

Table 15. Bolivia: Status of Actions to Improve Tracking of Poverty-Reducing Expenditure

	Actions	Status (FI/II/NS)[1]	Timing	Comments[2]
				Actions to Strengthen Budget Formulation
1	Development of a medium-term expenditure framework.	II	2004	The development of a MTEF is a government priority. With World Bank assistance, the government aims at having its first multi annual budget starting in 2004.
2	Facilitate systematic incorporation of PDMs and POAs into budget allocation decisions.	II	2004	Both at the national and subnational levels.
3	Introduce reforms on budget formulation	II	2004	To make the national budget a credible and binding tool reflecting the Government's strategic priorities.
4	Publication of the Government's Inter.-sectoral and sectoral policy priorities in advance of preparing the annual budget.	II	2003	To strengthen the link between the national budget and the Government's priorities.
5	Development of effective institutional mechanisms.	II	2005	It is a work in process with the support of the IMF (Customs Reform) and the WB (Institutional Reform Project).
				Actions to Strengthen Budget Execution
1	Follow the classification of poverty-related expenses established in the PRSP.	FI	2002	The 2002 national budget presents a classification according to the PRSP broad categories.
2	Improvement in the inter-governmental transfers system.	II	....	The Government will improve the inter-governmental transfers system within the Decentralization Reform initiative.
3	Strengthen internal and external audit	II	2004	Develop a traditional financial control system and non-traditional measures for performance evaluation.
4	Introduce reforms on budget execution.	II	2004	Make the national budget a credible and binding tool reflecting the Government's strategic priorities.
5	Enhance of social oversight groups.	II	2002	The *Mecanismo de Control Social* (MCS) was created in order to support the implementation of the Bolivian PRSP.
6	Introduction, on a pilot basis, of limits of periodic financing (*cuotas de pago*).	NS	....	The Treasury discarded the option of introducing *cuotas de pago* because of the significant number of line agencies (about 400).

Table 15. Bolivia: Status of Actions to Improve Tracking of Poverty-Reducing Expenditure

	Actions	Status (FI/II/NS)[1]	Timing	Comments[2]
				Actions to Strengthen Budget Reporting
1	Expand SIGMA implementation	II	Jun-05	The implementation of the SIGMA in the municipalities has been delayed
2	Follow the classification of poverty-related expenses as in the PRSP.	FI	2002	Information on the 2002 national budget execution (classified according to the PRSP broad categories) is available.
3	Full implementation of SIGMA system in the Central Government and Prefectures	II	2004	Implemented in the Central Government but not in Prefectures yet
4	Raise of municipal accounting and reporting standards.	II	2002	More municipal governments are following the standardized reporting requirements.
5	Establish bridging mechanism for tracking poverty-related expenditures.	FI	2002	The Unit of Municipal Governments was strengthened with wider institutional support and better coordination between key actors. The *Unidad de Programación Fiscal* (UPF) collects information on municipal expenditures.
6	Publication of the Government's budget execution evaluation.	FI	2002	There is information on public expenditure by functional classification at the Central Government for the 1991–2001 period.
7	Development of effective institutional mechanism.	II	2005	It is a work in process with the support of the IMF (Customs Reform) and the WB (Institutional Reform Project).

1/ FI= Fully Implemented; II=Implementation; NS=Not Started.
2/ Comments may explain any charges in the nature of proposed actions or changes to the timing of their implementation.

BOLIVIA: FUND RELATIONS
(As of May 31, 2003)

I. **Membership Status:** Joined December 27, 1945; Article VIII.

II. **General Resources Account:**	**SDR Million**	**Percent Quota**
Quota	171.50	100.00
Fund holdings of currency	205.52	119.84
Reserve position in Fund	8.87	5.17

III. **SDR Department:**	**SDR Million**	**Percent Allocation**
Net cumulative allocation	26.70	100.00
Holdings	26.97	101.01

IV. **Outstanding Purchases and Loans:**	**SDR Million**	**Percent Quota**
Stand-by arrangements	42.88	25.00
ESAF/ PRGF arrangements	140.30	81.81

V. **Latest Financial Arrangements:**

Type of Arrangement	**Approval Date**	**Expiration Date**	**Amount Approved (SDR Million)**	**Amount Drawn (SDR Million)**
Stand-by	4/02/03	4/01/04	85.75	42.88
ESAF/PRGF	9/18/98	6/07/02	100.96	63.86
ESAF	12/19/94	9/09/98	100.96	100.96

VI. **Projected Payments to Fund (Expectations Basis)**
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2003	2004	2005	2006	2007
Principal	16.50	26.60	35.40	44.09	30.22
Charges/Interest	1.18	1.56	1.38	0.83	0.28
Total	18.68	28.16	36.78	44.93	30.50

Projected Payments to Fund (Obligations Basis)
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2003	2004	2005	2006	2007
Principal	16.50	26.60	24.68	33.37	40.94
Charges/Interest	1.18	1.56	1.43	1.26	0.73
Total	18.68	28.16	26.11	34.63	41.67

VII. Implementation of HIPC Initiative:

		Original Framework	Enhanced Framework	Total
I.	Commitment of HIPC assistance			
	Decision point date	Sep. 1997	Feb. 2000	
	Assistance committed			
	by all creditors (US$ Million) [1/]	448.00	854.00	
	Of which: IMF assistance (US$ million)	29.00	55.32	
	(SDR equivalent in millions)	21.25	41.14	
	Completion point date	Sep. 1998	Jun. 2001	
II.	Disbursement of IMF assistance (SDR Million)			
	Assistance disbursed to the member	21.25	41.14	62.39
	Interim assistance	--	--	--
	Completion point balance	21.25	41.14	62.39
	Additional disbursement of interest income [2/]	--	3.09	3.09
	Total disbursements	21.25	44.23	65.48

[1/] Assistance committed under the original framework is expressed in net present value (NPV) terms at the completion point, and assistance committed under the enhanced framework is expressed in NPV terms at the decision point. Hence these two amounts can not be added.

[2/] Under the enhanced framework, an additional disbursement is made at the completion point corresponding to interest income earned on the amount committed at the decision point but not disbursed during the interim period.

VIII. **Safeguards Assessments:** A full safeguards assessment is in the final stages of preparation, as required under the Fund's safeguards assessment policy. The safeguards assessment is expected to be completed by the time of the Board meeting for the first program review, and its main findings will be communicated to the Board for its consideration.

IX. **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 minimal spreads between the maximum and minimum bids (generally 2 cents of boliviano). On May 28, 2003, the official selling rate was Bs 7.63 per U.S. dollar.

X. **Article IV Consultation:** The previous Article IV consultation and request for the third annual arrangement under the Poverty Reduction and Growth Facility were concluded by the Executive Board on June 8, 2001 (EBS/01/80, SM/01/153). The completion point document for the enhanced Heavily Indebted Poor Countries Initiative (EBS/01/78) was also discussed on this occasion. Bolivia is on the standard 12-month consultation cycle.

XI. **Technical Assistance:**

Dept.	Purpose	Time
FAD	Tax policy	Jan. 1999
FAD	Modernization of customs administration	June 1999
	and follow-up missions including	May 2001, Dec. 2001
FAD	Tax administration	June 1999, Feb. 2000,
		June 2001
FAD	Fiscal decentralization	Dec. 2000
MAE	Central bank operations and domestic capital markets	June 1999
MAE	Vulnerability of the banking system	Oct. 1999, Apr. 2000, Dec. 2000
STA	Money and banking statistics	Jan. 1999, Sep. 2001
STA	Balance of payments statistics	Aug. 1999
MAE	Monetary operations, monetary and exchange rate policy	May 2002
STA	National accounts statistics	Aug. 2002
MAE	FSAP	Nov. 2002, Jan. 2003
FAD	Customs reform	Dec. 2002
FAD	Tax Administration	May. 2003

XII. **Resident Representative:** Mr. Gerardo Peraza, since February 2001.

BOLIVIA: RELATIONS WITH THE WORLD BANK

Recognizing Bolivia's current difficulties, the World Bank's strategy to help the country out of them is divided in two phases. In the first phase—from social unrest of February to the beginning of October—the World Bank would adopt a measured response that balances the need to respond to the crisis with the need to continue with medium-term development objectives. By the end of June, the Bank expects the Government to have revised its PRSP, which would form the basis for the World Bank's Country Assistance Strategy (CAS) over the next four years. Provided the Government is indeed able to complete this task, the World Bank would be able to present the CAS to the Board on October, 2nd.

During the first phase, to respond to the crisis the Bank intends to:

- Present two projects to the Board that would help keep the situation from deteriorating further. One is this Social Cushion SAC that focuses on budget protection of key social sector interventions and includes measures to ensure that the budget will be executed as planned. It will also support the temporary employment programs. The second is a project designed to help the government with its planned banking and corporate restructuring, which will be presented in early FY04 (which starts in July 2003). This project is potentially risky and would only go forward after a careful analysis of the benefits and risks of operating in this area.
- Increase disbursements this year to help the country finance a significant part of the government's investment program. In calendar year 2002, a total of US$ 104 million was disbursed. For calendar year 2003, the World Bank is planning a combination of investment and rapid disbursement loans.
- Help the Government manage more effectively the existing stock and future flows of donations from bilateral agencies and credits from multilateral agencies so as to finance their initiatives to get out of the crisis. There are approximately US$ 1.6 billion in undisbursed funds in existing projects and a yearly flow of approximately US$ 700 million that is expected to be provided to Bolivia over the next four years. Currently, these resources are not adequately aligned to current needs. The World Bank is working with the Government and other donors to bring about a more effective alignment. This will undoubtedly require some restructuring on the part of several donors and the restructuring options will be discussed at a Consultative Group meeting scheduled for early FY04.

To continue with medium-term development objectives the Bank intends to:

- Present the second phase of a Decentralization Programmatic Structural Adjustment Credit (PSAC) that will deepen the reforms in decentralization and will address a looming problem of a build-up of municipal debt. With the Popular Participation Law that transferred 20% of government tax revenue to the municipalities and with the National Dialogue Law that transferred virtually all of the resources from HIPC II debt relief to the municipalities, they are now extremely important actors in implementing the PRSP. If the municipalities and, more generally, the entire decentralization system does not work well, it will be difficult to make much of a dent in poverty reduction.

- Present the first phase of an investment APL that will increase electrification and telecommunications in the rural areas. The APL will have a strong emphasis on helping to develop adequate policies to accelerate coverage rates in these important areas.
- Prepare a Public Expenditure Review (PER) to be discussed with the Government by August 2003. In this PER there will be an update of the analysis of the fiscal sustainability of the existing major reforms, including the pension reform, institutional reforms that modified civil service salaries and education and health reforms. While some analysis of the sustainability of the reforms was carried out at the moment when they were launched, the situation has changed with the drop in the rate of growth and the unexpected outcomes of negotiations with different sectors. The PER will also develop a Medium-Term Expenditure Framework and will review the efficiency, equity and sustainability of government programs in health, education, social protection and infrastructure.
- Update the 2001 Poverty Report. Given the likely emphasis that Bolivia's revised PRSP will place on improving the productive capabilities of the poor, the update will include an expanded treatment of the problems of generating pro-poor growth.

During the second phase, the World Bank would:

- Prepare its CAS that would be based on revisions to Bolivia's PRSP (which will take place after the third National Dialogue planned sometime in mid-year). The CAS would then be presented to the Board in early October 2003. The CAS will be prepared jointly with the IFC, which is expected to take on a larger role in promoting more effective private sector development. Work on the CAS has already begun.
- The PRSC will also be an important instrument to support Bolivia's PRSP and it will be presented jointly with the CAS in early October. Current plans for the PRSC are to have three main components that support: (a) pro-poor growth; (b) achievement of MDGs; and (c) participatory monitoring and evaluation of the PRSP, with a heavy focus on tracking results.

The Bank's work on the CAS and PRSC will be ready for the budget negotiations that will take place in Bolivia from late October to the middle of December. The Government will attempt to use these negotiations to reach agreement with different sectors on the direction that Bolivia will take not only for 2004, but for the next 3-4 years.

Bank-Fund collaboration in specific areas

As part of its overall assistance to Bolivia, the Bank has strengthened its close collaboration with the Fund. Specific examples of joint work for the near future cover the following areas:

Overall Financial Sector Assessment: The missions of coordinated Bank/Fund teams for the Bolivia FSAP took place in mid-November 2002 and January 2003. As a complement, the Bank will prepare a Report on the Observance of Standards and Codes (ROSC) focusing on insolvency and creditor rights systems, contingent on government approval.

Poverty and Social Impact Analysis (PSIA): The Bank and the Fund are supporting the completion of a PSIA through its policy analysis unit, UDAPE.

Joint Staff Assessment (JSA) of the Government's PRSP Progress Report. The Bank and the Fund have reviewed a draft of the authorities' PRSP progress report. The draft signals the authorities' commitment to the PRSP framework, their changes of emphasis and policy priorities for the poverty reduction strategy, and its consistency with the government's economic program. The JSA will be prepared on the basis of the final version of the PRSP progress report.

Governance issues: The transition from one government to another has put significant stress on the institutional reform process and there has been some concern with regard to future progress. Recently, the new government reassured the Bank that reforms will continue. Therefore, the Bank will continue to lead institutional reform efforts in close coordination with the Fund. The agenda states the need to consider starting reforms in the judicial area.

Medium-term strategy on dollarization and exchange rate policy issues: The Fund will take the lead in this area in close coordination with the authorities and with continuous dialogue with the Bank. A first MAE technical assistance report has already been completed and made available to the authorities.

Prepared by World Bank staff.
Questions may be addressed to Mr. Vicente Fretes-Cibils, Lead Economist at 473-1969.

BOLIVIA: RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

Background

As of May 30, 2003, the Inter-American Development Bank (IDB) had approved loans to Bolivia amounted to US$3.2 billion, of which cumulative disbursements amounted to US$2.4 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 Poverty Reduction Strategy Paper presented to the IDB on June 2001. This strategy, focuses on: (i) promoting sustained growth and increased employment opportunities in the productive infrastructure sectors, micro enterprise, and rural development; (ii) supporting direct actions to improve access to the basic social services; and (iii) governance. The impact of the regional crisis on Bolivia's economic performance since 1999, has weakened growth in labor intensive sectors pushing unemployment to 11.9 percent and increasing poverty incidence in urban and rural areas. The economic slowdown together with higher than expected pension related fiscal deficit and increased fragility of the financial system, has amplified the exposure of the country to an extended period of economic, social and political distress. In this context, the Bank assistance in 2003 will focus on supporting efforts to stabilize the economy, protect investments in key sectors from further deteriorating (roads and basic infrastructure), continue programs that are in the critical path to achieve the Millennium Development Goals, and create better conditions for rural and urban development.

The proposed IDB lending program for Bolivia for 2003 consists of nine loans for a total of US$217.0 million, of which US$100.0 million will support policies to promote fiscal sustainability and competitiveness. The IDB Board of Directors has assigned US$229 million in concessional resources for Bolivia for the period 2002–03, US$18.8 million of which were approved in the year 2002.

Recent economic and sector work

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 is currently working on a new strategy for the period 2003–07. Economic studies have been completed on fiscal sustainability, HIPC debt relief and poverty, pension reform and descentralization.

IDB nonreimbursable technical cooperation and small projects

The IDB portfolio also includes active projects for US$25.3 million in nonreimbursable technical cooperation, and US$1.9 million in non-reimbursable small projects.

Bolivia: Relations with the Inter-American Development Bank

(In millions of U.S. dollars)

Reference	Projects	Number of Loans	Approved	Disbursed	Undisbursed
	I. Statement of IDB loans (as of May 30, 2003)				
Totally disbursed (less cancellations)			**1,955.5**		
Sectors		**31**	**954.1**	**383.6**	**547.0**
Roads		4	222.0	107.1	114.9
698/OC	Beni-La Paz Peruvian Border Corridor		55.0	51.5	3.5
893/SF	Cotapata - Santa Barbara		40.0	39.8	0.2
1039/SF	Ventilla-Tarapaya		52.0	15.8	36.2
1101/SF	Trade Corridor Sta. Cruz - Puerto Suarez		75.0	-	75.0
Tourism		1	10.0	-	10.0
1098/SF	Sustainable Tourism Development Program		10.0	-	10.0
Agriculture and Envrionment		5	102.1	34.1	44.5
1099/SF	Env-Soc. Protection Santa Cruz - Pto. Suarez		21.0	-	21.0
1116/SF	Emergency Attention Plan: Fire Cordillera Sama-Tarija		2.5	-	2.5
929/SF	Protection of environment		19.0	13.3	5.7
964/SF	Irrigation and drainage		25.6	15.4	10.2
1057/SF	Agricultural Services Program		34.0	5.4	28.6
Sanitation		2	110.0	44.0	66.0
987/SF	Urban Sanitation PRODURSA		70.0	41.8	28.2
1050/SF	Urban Sanitation Small Municipalities		40.0	2.2	37.8
Social sectors		6	251.0	139.7	111.3
931/SF	Education Reform		80.0	61.8	18.2
995/SF	Programa de Atención al Menor		20.0	6.9	13.1
1006/SF	Apoyo a Política de Vivienda		60.0	18.0	42.0
1031/SF	Epidemiological Shield and Sector Reform		45.0	12.4	32.6
1093/SF	Strengthening Technical Education		6.0	0.7	5.3
1097/SF	Support Poverty Reduction Strategy		40.0	39.9	0.1
Institutional strengthening		10	112.0	36.4	75.6
976/SF	Governability Support		12.0	11.9	0.1
993/SF	Descentralization SNIPPRE		7.0	3.3	3.7
1038/SF	Loan TC Civil Society Access to Justice		2.7	0.6	2.1
1043/SF	Institutional Stregthening National Tax Agency		3.2	1.7	1.5
1046/SF	National Census Preparation Support		7.4	7.2	0.2
1056/SF	Customs reform and Modernization		5.0	3.0	2.0
1075/SF	Local Development and Fiscal Adjustment		47.0	3.4	43.6
1091/SF	Modernization Municipal Financial Administration		20.0	5.3	14.7
1121/SF	Disaster Prevention Program		2.7	-	2.7
1118/SF	Institutional Support to Strengthen Trade		5.0	-	5.0
Multisectoral onlending		1	35.0	22.3	12.7
1020/SF	Micro and Small Enterprises		35.0	22.3	12.7
Private Sector		2	112.0	-	112.0
1431/OC	Telecomunication Network Redibol		37.0	-	37.0
1444/OC	Transredes (Gas)		75.0	-	75.0
Technical assistance		**46**	**25.3**	**16.8**	**8.5**
Total			**2,934.9**	**2,355.9**	
Repaid				**835.1**	
Outstanding				**1,504.0**	

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

	Amount	In Percent of Total
II. Proposed IDB Lending Program 2003		
Number of loans	**9**	
Total loan amounts	**217.0**	**100.0**
Human development and access to social services	**36.0**	**16.6**
Education Reform II	36.0	16.6
Growth and creation of opportunities	**111.0**	**51.2**
Rural Development Program	10.0	4.6
Land titling	20.0	9.2
Revitalization of the Center of La Paz	20.0	9.2
Support to Competitiveness	35.0	16.1
Support to Bolivian Competitiveness System	10.0	4.6
Roads maintenance and Rehabilitation	16.0	7.4
Governance and consolidation of reforms	**70.0**	**32.3**
Justice Sector Reform	5.0	2.3
Support to Fiscal Sustainability	65.0	30.0

Source: Inter-American Development Bank.

BOLIVIA: STATISTICAL ISSUES

The timeliness and coverage of economic statistics in Bolivia is generally adequate for monitoring purposes. Significant advances have been made in recent years, but there is a need for improvements in a number of areas, as noted below. Many ministries and other official institutions, including the National Institute of Statistics (INE), post statistical information on the Internet. Bolivia has participated in the GDDS since November 2000.

I. Real Sector

National accounts

The authorities have decided to revise the national accounts statistics, changing the base year from 1990 to 2003, based on the *1993 SNA*. Large fluctuations in stockbuilding statistics result from its computation as a residual in the national accounts. There are discrepancies between INE's figures for public sector investment, consumption, and savings and the fiscal accounts produced by the Fiscal Programming Unit (UPF) of the Ministry of Finance, primarily because the UPF's public investment data includes all expenditures in physical and human capital, whereas INE's data only includes expenditures on new physical capital and its maintenance. A STA mission on national accounts statistics found in August 2002 that efforts to improve the quality of the real sector statistics were hampered by an inadequate statistical law and insufficient resources to undertake censuses and surveys.

Quarterly GDP accounts for production and demand are published with a variable lag; as of end-May 2003, data were available through the fourth quarter of 2002. INE also produces monthly production indices (IMAE).

Labor market

The annual household survey, *Encuesta Integrada de Hogares* (1989-95) was replaced in 1996 by the *Encuesta Nacional de Empleo* (ENE), with a broader coverage, including data on rural areas. Three surveys were conducted: in February and November 1997, and November 1997 (in 1998, no survey was conducted). In 1999, the MECOVI replaced the ENE, adding a new module on household expenditures and improving the health, education, and migration data (the last MECOVI was performed in November 2002.) The quality of the household surveys has improved since the mid-1990s, but it would be desirable to have more timely employment and wage data, as the last observations are for 2001. Furthermore, there is a lack of quarterly information on employment and wages.

Prices

The consumer price index (CPI) covering the four largest cities has a base year of 1991, and is to be revised on the basis of a household budget survey that will be conducted over a 12-month period that began in June 2, 2003. Industrial producer price indices and external trade unit values are compiled by INE, but are in need of revision as regards their coverage, product breakdown, and base year (1990=100).

II. Fiscal sector

The staff is provided with timely information on revenue, current and investment spending, and financing for the consolidated general government (central government and decentralized entities), public enterprises and the central bank, with appropriate disaggregation, on a monthly basis. 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 *Government Finance Statistics Yearbook*. However, these data do not cover all operations of decentralized agencies and operations channeled through special funds. The ongoing 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 IDB and the World Bank are funding the project.

III. External Sector

The central bank provides data to STA for publication in the *Balance of Payments Statistics Yearbook* and the *International Financial Statistics (IFS)*. The classification of accounts are broadly in accordance with the fifth edition of the *Balance of Payments Manual*. To date, data are submitted to STA only once a year (around September, with quarterly data for the previous calendar year), but the authorities have stated that they will begin to provide data submissions on a quarterly basis. The authorities are working on a data base on gross flows of short and medium-term private debt.

The BCB also provides monthly trade data to the Fund, but the import data are available only with a lag of up to six months. Upon request, the authorities also provide Fund staff with quarterly and annual information on the balance of payments, including disbursements and debt service by creditor and debtor and type of debt (i.e., concessional, nonconcessional); data on assistance under the HIPC Initiative, and medium-term debt projections.

IV. Monetary Sector

Monetary data are provided on the central bank balance sheet, commercial bank balances, and the balances of two state-owned second-tier banks, *Nacional Financiera Boliviana* (NAFIBO), and *Fondo de Desarrollo del Sistema Financiero* (FONDESIF). Data on the monetary survey are available with a short lag. Commercial bank data are collected by the Superintendency of Banks and they become available with a lag of six to eight weeks. The coverage of banks in the monetary survey is comprehensive, and the central bank also provides Fund staff with data on the operations of nonbank financial institutions. The central bank has been introducing changes to its monetary survey, following the recommendations of a STA advisory mission in September 2001, including the distinction of FONDESIF operations from the central bank's balance sheet. Other changes in the accounting systems, and an expanded coverage of the nonbank financial institutions, are yet to be introduced.

The central bank has recently improved information on holdings of open market documents by nonresidents, and starting end-1996, the definition of net international reserves has been changed to exclude the counterpart of these short-term liabilities to nonresidents.

Bolivia—Core Statistical Indicators

As of June 3, 2003

	Exchange Rates	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/Debt Service
Date of Latest Observation	Jun 2	May 30	May 29	May 29	Mar 03	May 21	May 03	Mar 03; Q4 2002	Q1 2003	Mar 03	Q4 2002; 2001	Dec 02
Date Received	Jun 3	Jun 3	Jun 3	Jun 3	May 21	May 22	Jun 3	May 03	May 03	May 03	May 03; Apr 02	May 03
Frequency of Data 1/	D	D	D	D	W	W	M	M; Q	Q	M	Q; A	Q
Frequency of Reporting 1/	D	D	D	D	W	W	M	M; Q	Q	M	Q; A	Q
Source of Data 2/	A	A	A	A	A	A	A	A	A	A	A	A
Mode of Reporting 3/	O (web site)	C	C	C	C	C	E	E	E	E	E	O
Confidentiality 4/	C	B	B	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, E-electronic transfer, 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.

BOLIVIA: DEBT SUSTAINABILITY ANALYSIS

Bolivia's debt indicators are much less favorable than envisaged in 2001 at the completion point under the Enhanced HIPC Initiative, reflecting large increases in the fiscal deficit in 2001–02 that were financed by domestic and nonconcessional external borrowing (Figure 1). The NPV of nonfinancial public sector debt remained at its end-2000 level of 45 percent of GDP, compared with a sharp drop to 34 percent of GDP that was envisaged under the enhanced HIPC Initiative.

Public sector debt is now projected to decline over the medium term in response to sustained fiscal adjustment (see Table 10). The NPV of public debt projected for 2015 is to exceed the one third higher than was projected at the time of the enhanced HIPC Initiative. The projection of debt service as a percentage of public sector revenue as of 2015 is now more than 3 times higher than projected at the time of the completion point.

Medium-term stress tests

The stress tests presented in the staff report for the SBA request (EBS/03/37) were repeated with observed end–2002 updated data on the debt stock and exchange rates. The stress tests show that debt could become unsustainable in the absence of the planned fiscal adjustment and also that debt indicators are sensitive to low growth rates, current account adjustments, export prospects, and an exchange rate depreciation.

In the program projections, the net present value (NPV) of public debt relative to GDP peaks in 2004, but falls subsequently and the ratios of debt service and interest to revenue improve (Figure 1, top right and bottom panels). Stress tests show the following results (Figure 2 and Table 2):

- A "GDP shock" (stress test 3), which reduces the growth rate to the historical average of five years (2.4 percent) minus two standard deviations (one standard deviation is 1.7 percent) in 2003 and 2003, has the least impact.

- Under a "fiscal shock" (stress test 4), the fiscal program goes off track by one standard deviation (2.1 percent of GDP) in each year through 2008. In this case, the debt to GDP ratio levels out at about 79 percent over the medium term.

- A large shock to the debt stock would come from the "status quo" stress test (stress test 1) assuming that the real interest rate, the real GDP growth rate, and the primary balance would remain in 2003-08 at their average of the past five years. In this case, public debt would continue to rise, exceeding 90 percent of GDP by 2008.

- In an "exchange rate shock" stress test, the exchange rate depreciates by 30 percent in 2003 (stress test 6). Since 95 percent of public debt is denominated in foreign currency, this shock has a large impact on the debt to GDP ratio, which rises to

87½ percent in 2004.[1] The ratio subsequently falls, assuming that the program's fiscal adjustment path is achieved, but remains high at 81 percent in 2008.

- A picture similar to that with the "exchange rate shock" emerges from a stress test that assumes that the debt ratio in 2003 would rise by an additional 30 percent of GDP (stress test 7). While the debt stock would still stand at about 92 percent of GDP in 2008, it would decline from about 100 percent in 2004.

Similar stress tests were applied to the external debt projections (Table 1).

- If natural gas exports remain constant at the level of 2003, rather than expanding as projected in the baseline (stress test 1), the ratio of the NPV of debt to exports in 2007 would increase from 135 percent in 2003 to 156 percent in 2008, rather than falling to 140 percent under the program projection. The nominal external debt to GDP ratio would decrease from 55 percent in 2003 to 52 percent in 2008 (compared with 51 percent in the program), reflecting the impact of lower exports on GDP.

- If interest rates, growth, inflation, the non-interest current account, and non-debt flows remain during 2003-08 at the average of the past five years (stress test 2), the nominal debt to GDP ratio increases sharply from 54 percent in 2003 to 80 percent in 2008, with the increase mostly due to the non-adjustment of the current account.

- If real GDP growth in 2003-4 is set to the average of the preceding five years (2.4 percent) minus two standard deviations (one standard deviation is 1.7 percent) (stress test 3), the debt to GDP ratio increases to 63 percent in 2004, but then falls to 56 percent in 2008.

- If the current account deficit excluding interest in 2003-04 is set to the program projection minus two standard deviations (one standard deviation is 1.4 percent of GDP) (stress test 4), the debt to GDP ratio falls from 2005 onward, but remains high at 56 percent in 2008 compared with 58 percent in 2003.

- A 30 percent depreciation in 2003 enlarges the ratio of debt to GDP (stress test 5), peaking at 75 percent in 2004, but debt remains sustainable and falls to 67 percent in 2008.

Long-term stress tests

The stress test analysis above to analyze the long-term on external debt indicators effects reduced access to lending on concessional terms and the pending liquefied natural gas (LNG) and gas-to-liquids (GTL) project.

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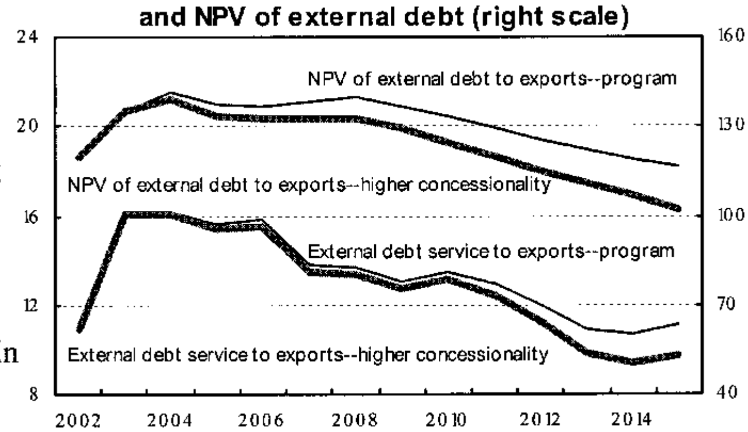
[1] The assessment excludes the contingent liabilities related to the impact that a depreciation would have on the banking system.

- Bolivia's loss of access to concessional aid flows will keep its external debt service indicators at relatively high levels. The program assumes that nonconcessional financing will increase from about 40 percent of total external financing in 2003 to over 80 percent in 2013, which would result in a moderate decline in the NPV of external debt to exports to 117 percent in 2015 from 135 percent in 2003. If the share of nonconcessional financing in total financing were unchanged after 2003, the NPV of external debt to exports would decline more rapidly, to slightly over 100 percent in 2015.

Impact of higher share of concessional donor flows--Ratios to exports of external debt service (left scale) and NPV of external debt (right scale)



- If two major gas projects (LNG and gas-to-liquids) are not implemented, the NPV of external debt in percent of exports would decline slowly over the medium term.

Impact of the LNG and GTL projects--ratios to exports of external debt service (left scale) and NPV of external debt (right scale)

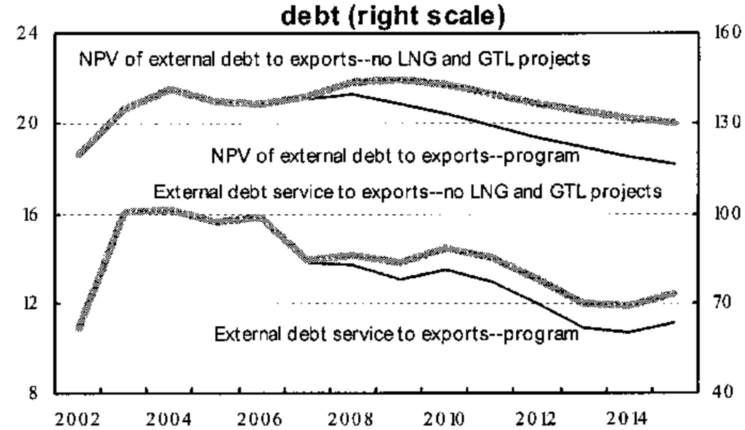
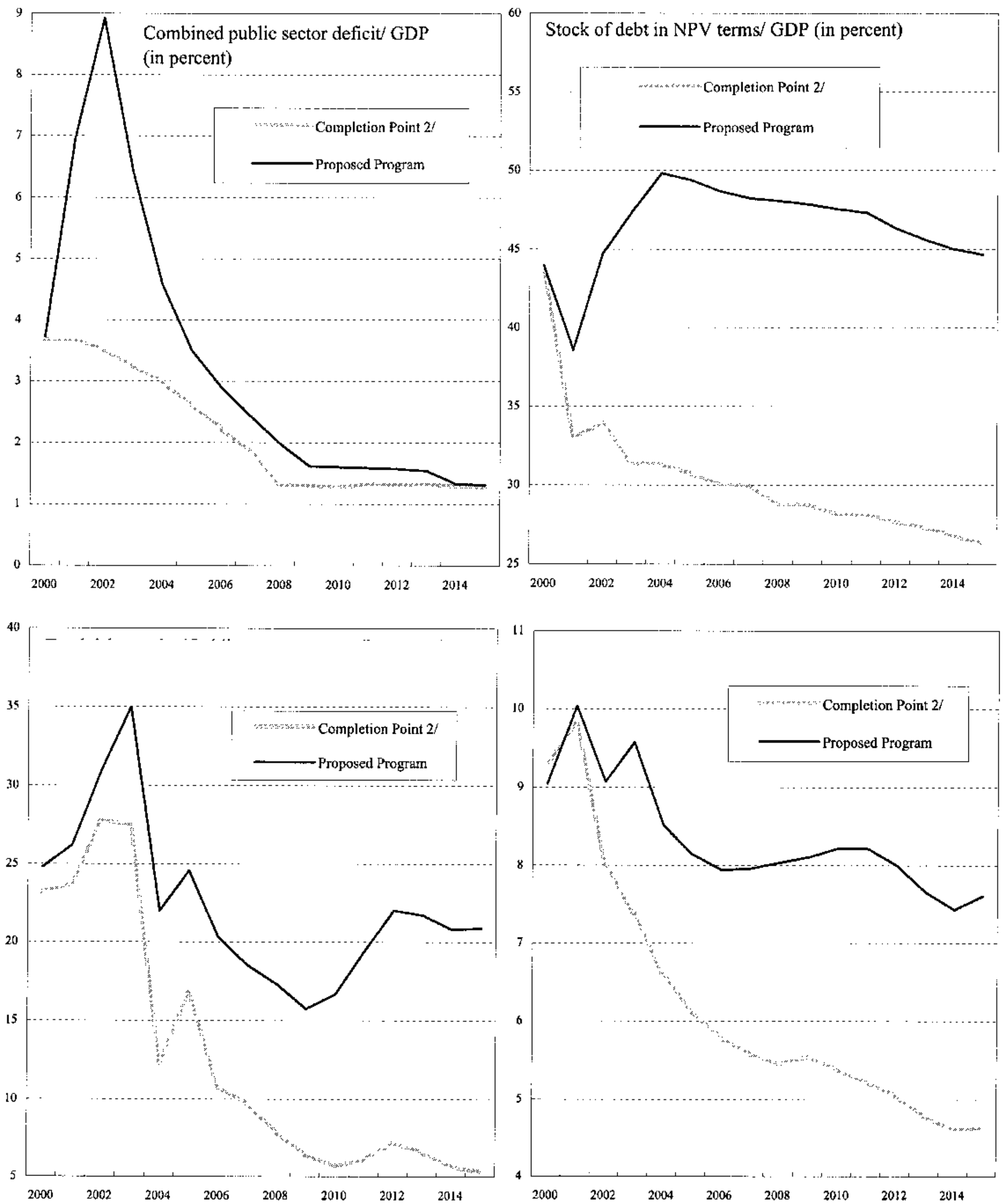


Figure 1. Bolivia: Debt and Debt Service Indicators for Medium- and Long-Term Public Sector Debt, 2000–15 1/

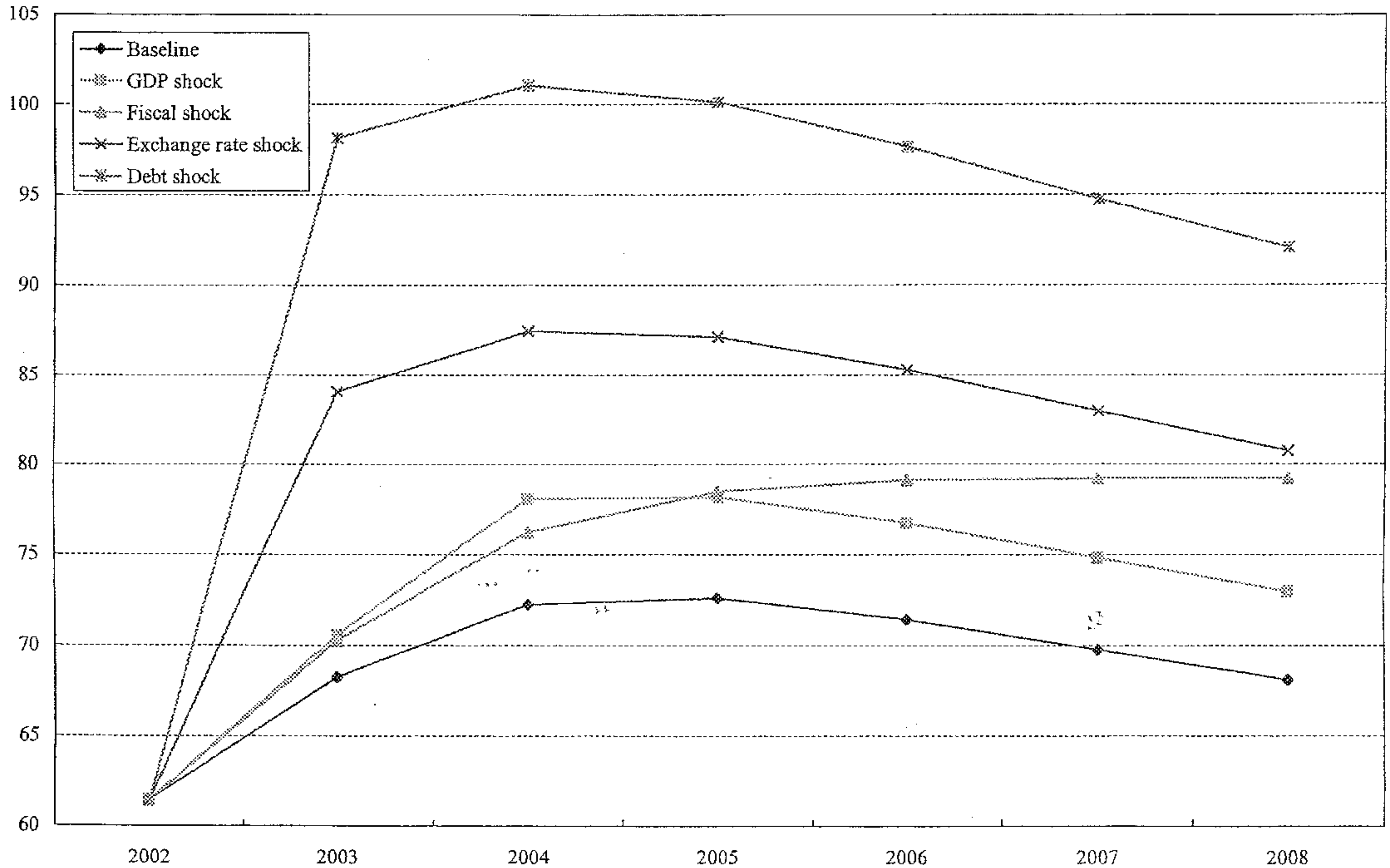


Sources: Central Bank of Bolivia; and Fund staff estimates and projections.

1/ Coverage consists of the nonfinancial public sector.

2/ From the debt sustainability analysis for the completion point under the HIPC Initiative (EBS/01/78). Numbers include HIPC and beyond-HIPC relief. The domestic debt projection at completion point is imputed.

Figure 2. Bolivia: DSA Stress Tests--Nominal Public Debt to GDP Ratio 1/



1/ Refers to nonfinancial public sector debt; see Table 2 of Annex V for a definition of stress tests.

Annex V, Table 1. Bolivia: External Sustainability Framework, 2000–08

	Actual			Projections					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
I. Baseline Medium-Term Projections									
1 Nominal external debt/Exports of G&S	303.4	218.7	241.1	251.1	245.9	231.9	226.9	215.0	204.5
2 Nominal external debt/GDP 1/	53.1	41.4	47.7	54.9	57.9	57.0	54.6	52.3	50.9
3 Change in external debt/GDP	-2.0	-11.7	6.3	7.2	3.0	-1.0	-2.4	-2.2	-1.4
4 Net debt-creating external flows/GDP (5+9+12)	-3.6	-3.1	-3.5	-3.1	-7.9	-12.1	-13.1	-10.4	-7.8
5 Current account deficit, excluding interest payments/GDP	4.2	2.5	3.6	1.9	2.0	1.8	1.8	1.7	1.7
6 Deficit in balance of G&S/GDP	9.5	7.4	7.7	6.1	6.9	6.1	6.4	5.5	-2.6
7 Exports of G&S/GDP	17.5	18.9	19.8	21.9	23.6	24.6	24.0	24.3	24.9
8 Imports of G&S/GDP	27.0	26.3	27.4	27.9	30.5	30.7	30.4	29.8	22.3
9 Minus net non-debt creating capital inflows/GDP	-8.3	-8.3	-8.4	-7.8	-10.5	-13.2	-13.3	-10.6	-8.4
10 Net foreign direct investment, equity/GDP	8.3	8.3	8.4	7.8	10.5	13.2	13.3	10.6	8.4
11 (r-g-(ρ+gρ))/(1+g+ρ+gρ))debt/GDP (14/13)	0.6	2.8	1.2	2.8	0.6	-0.7	-1.6	-1.5	-1.2
12 Adjustment factor: 1+g+ρ+gρ	1.0	1.0	1.0	1.0	1.0	1.0	1.1	1.1	1.0
13 (r-g-(ρ+gρ))debt/GDP (15+16+17)	0.6	2.7	1.2	2.7	0.6	-0.7	-1.7	-1.6	-1.2
14 r (interest rate) times debt/GDP	1.2	0.9	0.7	1.0	1.1	1.2	1.2	1.2	1.2
15 minus g (real GDP growth rate) times debt/GDP	-1.3	-0.8	-1.1	-1.4	-2.4	-2.7	-2.9	-3.0	-2.6
16 minus (ρ + gρ) (ρ = U.S. dollar value of GDP deflator, growth rate) times debt/GDP	0.7	2.5	1.7	3.1	1.9	0.8	0.0	0.1	0.1
17 Residual, incl. change in gross foreign assets/GDP (3-4)	1.5	-8.6	9.8	10.3	10.9	11.2	10.7	8.2	6.4
Memorandum items: key macro and external assumptions									
Nominal GDP (In billions of bolivianos)	51.9	53.0	55.9	59.3	63.3	68.3	74.4	81.1	87.9
Nominal GDP (In billions of U.S. dollars)	8.4	8.0	7.8	7.7	7.7	8.0	8.4	8.8	9.2
Real GDP growth (in percent per year)	2.3	1.5	2.8	2.9	4.3	4.7	5.1	5.4	5.0
Nominal GDP deflator (in U.S. dollars, change in percent per year)	-1.3	-4.7	-3.9	-6.3	-3.3	-1.4	-0.1	-0.2	-0.2
External interest rate (percent per year)	2.1	1.8	1.7	2.1	2.0	2.0	2.1	2.2	2.4
Growth of exports of G&S (U.S. dollar terms, in percent per year)	12.2	3.4	1.6	8.5	8.7	7.7	2.7	6.5	7.1
Growth of imports of G&S (U.S. dollar terms, in percent per year)	7.2	-6.9	1.4	-0.1	10.0	4.1	4.1	3.1	-21.6
NPV of external debt (In billions of U.S. dollars)	2.7	1.4	1.8	2.1	2.4	2.5	2.6	2.8	3.0
NPV of external debt to exports of G&S (3-year backward moving average)	199.3	100.2	119.4	134.9	141.5	137.1	136.8	138.0	139.7
Debt service to exports ratio	20.4	18.1	12.5	17.0	17.0	17.4	19.6	16.1	13.8
II. Sensitivity Analysis for Nominal External Debt-to-GDP Ratio									
1. Natural gas exports remain at the level in 2003				54.9	59.0	58.8	56.1	53.7	52.2
NPV of external debt to exports (three-year backward moving average)				134.9	145.4	147.3	152.5	155.3	155.5
2. If interest rate, real GDP growth rate, US$ GDP deflator growth, non-interest current account, and non-debt flows (in percent of GDP) are at average of past 5 years				53.5	60.0	66.9	73.5	77.7	80.2
3. If real GDP growth rate in 2003 and 2004 is average minus two standard deviations, others at baseline				56.9	63.1	62.1	59.5	57.1	55.6
4. If current account is average plus two standard deviations for two years				57.7	63.5	62.5	59.9	57.5	56.0
5. One time 30 percent depreciation in year 2003 (-30% GDP deflator shock), others at baseline.				72.0	75.2	74.1	71.2	68.5	66.7
Memorandum items									
Current account deficit, excluding interest payments (percent of GDP, average of past 5 years)			4.3						
Current account deficit, excluding interest payments (percent of GDP, standard deviation of past 5 years)			1.4						
Net non-debt creating capital inflows (percent of GDP, average of past 5 years)			9.7						
Interest rate (average of past 5 years)			2.1						
Interest rate (standard deviation of past 5 years)			0.6						
Real GDP growth rate (average of past 5 years)			2.4						
Real GDP growth rate (standard deviation of past 5 years)			1.7						
GDP deflator, U.S. dollar terms (average of past 5 years)			-2.2						
GDP deflator, U.S. dollar terms (standard deviation of past 5 years)			2.9						

1/ Coverage consists of medium- and long-term debt of the public sector. The projection assumes that US$70 million nonconcessional borrowing for financial and corporate restructuring takes place in 2004, although the program ceiling would allow it to take place in 2003.

Annex V, Table 2. Bolivia: Public Sector Debt Sustainability Framework, 2000–08 1/

	Actual			Projections					
	2000	2001	2002	2003	2004	2005	2006	2007	2008
I. Baseline Medium-Term Projections				(Ratios in percent)					
1 Public debt (nominal)/revenues	233.3	208.5	236.3	250.2	253.5	252.2	249.0	246.0	241.2
2 Public debt (nominal)/GDP	58.6	53.6	61.4	68.2	72.2	72.6	71.4	69.7	68.1
3 Change in public debt/GDP	-9.2	-5.1	7.9	6.2	4.6	0.3	-1.2	-1.7	-1.6
4 Net debt-creating flows/GDP (5+6)	-0.2	5.5	7.1	3.2	-0.2	-2.1	-2.8	-3.2	-3.2
5 Overall deficit, excluding net interest payments/GDP (=primary deficit)	1.9	4.8	6.6	3.8	2.1	1.2	0.6	0.2	-0.3
Revenue and grants/GDP	25.1	25.7	26.0	27.0	28.5	28.8	28.7	28.3	28.2
Noninterest expenditure/GDP	27.1	30.5	32.6	30.8	30.6	29.9	29.3	28.5	27.9
6 $((r - \pi) - g(1+\pi))/(1+g+\pi+g\pi))$debt/GDP (8/7) 2/	-2.1	0.7	0.5	-0.6	-2.4	-3.2	-3.4	-3.4	-3.0
7 Adjustment factor: $1+g+\pi+g\pi$	1.1	1.0	1.0	1.1	1.1	1.1	1.1	1.1	1.1
8 $((r - \pi) - g(1+\pi))$debt/GDP (9+10)	-2.3	0.7	0.5	-0.7	-2.5	-3.5	-3.7	-3.7	-3.2
9 $(r - \pi)$ times debt/GDP	-0.6	1.6	2.0	1.2	0.5	0.0	0.1	0.3	0.4
10 minus $g(1+\pi)$ times debt/GDP	-1.6	-0.9	-1.5	-1.8	-3.0	-3.5	-3.8	-4.0	-3.6
11 Residual, incl. asset changes and privatization receipts (negative)/GDP (3-4)	-9.1	-10.6	0.8	3.6	4.8	2.4	1.6	1.5	1.6
Memorandum Items: Key macro and external assumptions									
Nominal GDP (in billions of Bolivianos)	51.9	53.0	55.9	59.3	63.3	68.3	74.4	81.1	87.9
Real GDP growth (in percent per year)	2.3	1.5	2.8	2.9	4.3	4.7	5.1	5.4	5.0
Exchange rate (Bolivianos per U.S. dollar)	6.4	6.8	7.5	8.0	8.4	8.7	9.0	9.4	9.7
Nominal appreciation of Boliviano against U.S. dollar	-6.3	-6.3	-8.9	-6.3	-4.8	-3.8	-3.4	-3.4	-3.4
CPI (change, in percent per year)	4.6	1.6	0.9	2.6	3.1	3.5	3.2	3.0	3.0
Average interest rate on public debt (percent per year)	3.7	4.4	4.7	4.5	3.8	3.5	3.4	3.4	3.5
Average real interest rate (nominal rate minus change in CPI, percent)	-0.9	2.8	3.7	1.9	0.7	0.0	0.2	0.4	0.5
Growth of revenues (deflated by GDP deflator, in percent per year)	-1.0	3.8	4.1	6.9	10.0	5.7	4.8	4.2	4.6
Growth of noninterest expenditure (deflated by GDP deflator, in percent per year)	0.2	14.3	9.8	-2.6	3.7	2.3	2.9	2.6	2.9
NPV of debt (in billions of U.S. dollars)	3.7	3.1	3.5	3.6	3.9	3.9	4.1	4.3	4.4
Budgetary debt service to revenue	24.8	31.6	31.0	35.0	22.0	24.6	20.3	18.5	17.3
II. Stress Tests	Nominal public debt in percent of GDP, unless indicated otherwise								
1. If real interest rate, real GDP growth rate, and primary balance (in percent of GDP) in 2003-2008 are at average of past 5 years				66.5	74.4	80.0	84.6	89.2	93.8
(In NPV terms)				46.2	54.8	60.3	66.0	72.6	79.7
2. If real interest rate in 2003 and 2004 is average plus two standard deviations, others at baseline				70.3	78.8	78.9	77.4	75.5	73.6
3. If real GDP growth rate in 2003 and 2004 is average minus two standard deviations, others at baseline				69.9	78.0	78.1	76.7	74.8	72.9
4. If primary balance (in percent of GDP) in 2003-08 is at baseline plus one standard deviation				69.6	76.2	78.5	79.1	79.2	79.2
5. Combination of 2-4 using one standard deviation shocks				72.1	85.0	84.8	83.1	80.8	78.7
6. One time 30 percent real depreciation in 2003, others at baseline 3/				83.4	87.5	87.1	85.3	82.9	80.7
7. If debt ratio in 2003 rises by (additional) 30 percent of GDP, others at baseline				97.5	101.0	100.1	97.6	94.7	92.0
Memorandum items				(In percent)					
Primary deficit excluding interest (percent of GDP, average of past 5 years)			3.5	3.5	3.5	3.5	3.5	3.5	3.5
Primary deficit excluding interest (percent of GDP, standard deviation of past 5 years)			2.1	2.1	2.1	2.1	2.1	2.1	2.1
Real interest rate (nominal rate minus change in GDP deflator, average of past 4 years)			1.9	1.9	1.9	1.9	1.9	1.9	1.9
Real interest rate (nominal rate minus change in GDP deflator, standard deviation of past 4 years)			2.5	2.5	2.5	2.5	2.5	2.5	2.5
Nominal interest rate (average of past 5 years)			4.2	4.2	4.2	4.2	4.2	4.2	4.2
Nominal interest rate (standard deviation of past 5 years)			0.5	0.5	0.5	0.5	0.5	0.5	0.5
Real GDP growth rate (average of past 5 years)			2.4	2.4	2.4	2.4	2.4	2.4	2.4
Real GDP growth rate (standard deviation of past 5 years)			1.7	1.7	1.7	1.7	1.7	1.7	1.7
GDP deflator, percent change (average of past 5 years)			3.4	3.4	3.4	3.4	3.4	3.4	3.4
GDP deflator, percent change (standard deviation of past 5 years)			2.1	2.1	2.1	2.1	2.1	2.1	2.1

1/ Coverage consists of the nonfinancial public sector including pensions, excluding bonds issued for the recapitalization of the central bank.
2/ Defined as: r = interest rate; π = GDP deflator, growth rate; g = real GDP growth rate.
3/ Real appreciation is approximated by nominal appreciation against U.S. dollar plus increase in domestic GDP deflator.

BOLIVIA: LESSONS FROM THE PREVIOUS PRGF ARRANGEMENT

1. **The mission met with the authorities, donors, and representatives of the civil society to discuss lessons which could be learned from the previous PRSP and the last IMF supported program.** The following provides summary background to the lessons for future policy design noted in Section IV.A of the present report.

2. **The main objectives of Bolivia's previous program with the Fund[1] were to increase growth and reduce poverty** through prudent fiscal and credit policies and a deepening of structural reforms. GDP growth was expected to rise from 4½ percent in 1998 to 6 percent in 2002 with inflation declining from 6½ percent to 4½ percent, supported by a reduction in the fiscal deficit from 4 percent to 2 percent of GDP.

3. **The authorities agreed that program implementation had been disappointing, particularly in view of Bolivia's past record of stabilization and structural reforms.** Significant external shocks have hit the country, growth has been sluggish, the fiscal position significantly worsened, and structural reforms stalled during 2000–02. The reviews of the third year arrangement were not completed, as the fiscal program went off track soon after the arrangement was approved in June 2001, and there was a lack of progress with fiscal structural reforms.

4. **The PRSP process, though broadly participatory, did not yield the expected benefits in terms of country ownership but, instead, raised unrealistic expectations.** Ownership of the PRSP even within the government was limited, and it did not become the central guide to economic policy that was envisaged. The National Dialogue was conducted through the channels of a participatory democracy (civil society organizations, the Catholic Church), with little involvement by the traditional institutions of a representative democracy (congress, political parties). Also, the dialogue was perceived as focusing on how enhanced-HIPC assistance should be used, and by whom. The result was elevated expectations by CSOs about affecting public policy, and difficulties in trying to establish clear priorities within the existing budget constraints. In addition, rising social tensions and political divisions reduced the government's capacity to implement its poverty reduction strategy.

5. **The relaxation of fiscal policy in 2001–02 in the face of economic slowdown was counterproductive.** It worsened fiscal debt indicators substantially without fostering the hoped-for recovery of economic activity.

6. **The fiscal decentralization and transfer of resources to the local governments was not accompanied by a strengthening of their institutional capacity** to effectively set expenditure priorities and properly controlling the use of resources.

7. **The contraction of the financial system, reflecting the structural weaknesses of the corporate sector**, has limited the credit available to the private sector. Programs for loan restructuring have only postponed the problems, as they did not tackle the underlying weaknesses of the corporate sector.

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[1] The program, originally under ESAF, was first approved on September 18, 1998, and was subsequently converted into a program under the PRGF, that expired on June 7, 2002.

La Paz, Bolivia
June 20, 2003

Dear Mr. Köhler:

On April 2, 2003, the Executive Board approved a stand-by arrangement for Bolivia. This letter informs you of progress made and supplements the understanding specified in our letter of March 21, 2003. We remain fully committed to the economic program for 2003 aimed at stabilizing the economy, calming social tensions, and laying the foundation for comprehensive medium-term reforms.

In support of the policies described in our supplementary memorandum of understanding, the Government of Bolivia requests the completion of the first review under the Stand-By Arrangement. All quantitative performance criteria for end-March 2003 and the continuous performance criterion were met. Also, two structural performance criteria were met through the submission to Congress of the tax code and draft laws on bankruptcy and the corporate debt workout mechanism. Two other structural performance criteria were implemented with a technical delay of one week, for which we request waivers. The structural performance criterion concerning the consistency of the budget with the fiscal program was not met, since approval of revenue measures has been delayed. We describe in our memorandum the actions we have taken to meet the fiscal objectives of the program, and we request a waiver for the nonobservance of this performance criterion.

We stand ready to take additional measures necessary to keep the program on track, including additional revenue and spending measures. We are actively working on a medium-term economic program that would allow us to request a new arrangement under the Poverty Reduction and Growth Facility from the Fund before the end of October.

To raise domestic confidence and ensure full transparency, we intend to publish the attached memorandum.

Sincerely yours,

/s/
Javier Comboni
Minister of Finance

/s/
Juan Antonio Morales
President, Central Bank of Bolivia

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

Attachment: Supplementary Memorandum of Economic Policies

Supplementary Memorandum of Economic Policies of the Government of Bolivia First Review Under the Stand-By Arrangement

1. The government continues to be guided by the macroeconomic and structural reform program described in our memorandum of March 21, 2003. Our policies since then have been successful in calming social tensions, containing the fiscal deficit, rebuilding deposits in the banking system, and advancing banking and corporate sector reforms. We have also initiated a national dialogue to discuss medium-term reforms to enhance growth and reduce poverty.

2. The macroeconomic framework for 2003 is being maintained. We still expect GDP growth of almost 3 percent, led by the hydrocarbon and manufacturing sectors and a boost to agriculture from a large soybean harvest.

3. All quantitative performance criteria for end-March 2003 were met and we are implementing policies consistent with meeting the end-June quantitative performance criteria. We propose setting performance criteria for end-September and end-December 2003 identical to the existing indicative targets (Table 1).

A. Fiscal Policy

4. The 2003 budget was approved on April 3 with a deficit of 6.5 percent of GDP, in line with the program. Subsequently, however, we revised downward our projection of public revenue by about 0.4 percentage point of GDP, owing to lower import-related taxes and the impact of higher than expected international oil prices on fuel excise taxes. Also, some tax measures that were included in the budget as modifications to Law 843 have not yet been approved (yield of 0.4 percentage point of GDP).

5. To ensure consistency of the 2003 budget with the deficit target of 6.5 percent of GDP, a number of actions are being taken:

- To reduce current spending, compared with the original fiscal program, we have curtailed outlays on goods and services, particularly on contracted services (0.15 percent of GDP).

- We have cut/delayed low-priority public investment amounting to about 0.65 percent of GDP through a systematic identification process that gives priority to projects that are already underway, aims at reducing poverty, and is tied to concessional financing. We are maintaining our objective of increasing poverty-reducing expenditure in 2003 relative to GDP.

6. We remain committed to securing the approval of the tax bill now in Congress, which will raise revenue by adjusting the tax base for fuel excises and increasing the taxation of business services. We will take administrative measures to broaden the coverage of taxes such as on alcoholic beverages and hydrocarbon products. Together, these measures are

expected to raise revenues by 0.15 percent of GDP, compared with the original tax bill's yield of 0.4 percent of GDP. Once these revenue measures are passed, there would be room for a somewhat higher level of public investment spending.

7. The tax procedures code was submitted to Congress on April 30. To ensure that the tax regularization scheme is approved at the same time as the tax code, it was included as part of the same legislative package. The tax regularization scheme would be approved only in combination with the tax code.

8. We are aiming to reduce pension costs through administrative efforts, control of fraudulent claims, and strict enforcement of streamlined eligibility criteria. As part of our efforts to reduce pension costs, we have brought the minimum pension into closer alignment with the minimum wage for new retirees under the old pension system. In addition, in early June we set up an agency for the oversight of the pay-as-you-go pension system; the objectives are to control costs and improve administration.

9. To protect the fiscal program, we have identified an additional list of public investments, following the same selection criteria as described in paragraph 5, which would be cut on a timely basis if needed to achieve the deficit target. The revenue-sharing mechanism currently in place also provides for lower spending of local governments in the event that revenue falls behind projections.

10. We are continuing to consider approaches to strengthen public debt management. We have requested technical assistance from the IMF to evaluate the impact and appropriateness of a possible operation involving a change in the currency denomination of the central bank's holdings of Series A and B Treasury bonds from foreign to domestic currency. Any financial impact associated with such a change would need to be consistent with the monetary program under the stand-by. We will not take any decision in this regard until after taking account of the recommendations of the IMF's technical assistance report.

B. Monetary and Exchange Rate Policies

11. Monetary policy, while ensuring adequate liquidity for the financial system, remains consistent with the targeted gradual buildup of international reserves. A modest but steady rise in bank deposits since late February has led to an increase in international reserves in line with the program. The central bank's benchmark interest rate in U.S. dollars has been maintained at a rate that is intended to encourage a preference for the domestic currency, and the yield on 3-month dollar-denominated treasury bills has risen by more than 230 basis points since late January, to just under 4 percent. Inflation has remained contained, but we continue to stand ready to raise rates further if there are any signs of rising inflationary pressures. Regulations for the liquidity support of banks were issued on April 29, 2003 by the Board of the Central Bank.

12. The boliviano has depreciated in real effective terms in recent months, owing to a strengthening of the currencies of our main regional trading partners. We intend to preserve the recent gains in competitiveness, which have more than offset the small real effective

appreciation of the boliviano in 2002. The real effective exchange rate is currently at its most competitive level since 1996.

C. Financial and Corporate Sector Restructuring

13. The regulatory framework of the financial sector has been substantially strengthened in recent months.

- The government issued a supreme decree on May 6, 2003 that clarifies the roles of the different institutions with oversight over the financial sector, and defines the areas of banking regulation that should be determined by the banking superintendency.

- The banking superintendency on May 9, 2003 issued the final regulations for the bank resolution and prompt corrective action mechanisms. These new regulations have already been applied with the successful intervention and transfer of liabilities of a small savings and loans institution in mid-May.

14. The draft laws on corporate bankruptcy and informal debt workout mechanisms were submitted to congress, as expected, by end-April. They are designed to expedite procedures by moving responsibilities from the judicial into the administrative sphere. Since the drafts were sent to congress, we have explained the content and objectives of the laws to creditors, debtors, lawyers, and other stakeholders. This process has allowed us to gain support, and we will evaluate and include suggestions from stakeholders—including the possibility of framing these legal changes within the existing Commercial Code—and also incorporate changes to address the possibility of dissenting creditors challenging the constitutionality of the draft laws. The drafts of the corporate bankruptcy and informal workout laws have been included in the agenda for the second extraordinary congress, which started on June 3, and are expected to be approved by September 30, 2003.

15. Based on the rules for provisioning requirements that took effect by end-March and that do not allow for any regulatory forbearance, we have analyzed the solvency situation of individual financial institutions and will continue to monitor them closely. The government remains committed to taking all steps needed to maintain and enhance confidence in the financial system.

16. A high-level management team was formed in April to coordinate the strategy for the corporate and financial sectors. Under the guidance of the team, which meets weekly:

- We have assembled a comprehensive database on the liabilities of large corporations, including debts to financial institutions, tax and customs administration, and pension funds. Over the next few weeks we plan to further improve the database and complete a preliminary diagnosis of the impact of corporate restructuring on banks, and to deepen such analysis in the coming months with World Bank technical assistance.

- We are developing a comprehensive strategy—which is being discussed both at the technical and political levels—to strengthen the corporate and financial sectors, while ensuring the stability of the payments system and minimizing fiscal costs.

17. We are developing a framework, in collaboration with the World Bank, for the use of public funds for bank restructuring or corporate workouts that will be ready by the time of the second program review. Once congress has approved the bankruptcy and informal workout laws, we will promptly issue the relevant regulations and set up the needed administrative bodies to accelerate the corporate restructuring strategy.

18. Finally, in line with these changes, the President has nominated a Special Appointee to promote judicial reforms, including the strengthening of the judicial system's ability to deal with the complexities of bankruptcy and corporate workout procedures.

D. Preparation for PRGF

19. The government will conduct a national dialogue in June-August, which will feed into Bolivia's new PRSP. As a basis for discussion, we have prepared a preliminary PRSP progress report, which analyzes the shortcomings of our 2001 PRSP. We are also preparing a document outlining possible strategies for increasing growth and reducing poverty. These documents together with an updated macroeconomic framework will be combined in a final version of the PRSP Progress Report by early August, which could provide the basis for a PRGF arrangement. We will then finalize the new PRSP, reflecting the results from the National Dialogue, which we intend to have ready by the time of the Consultative Group meeting programmed to take place by the beginning of the fourth quarter of 2003.

Table 1. Bolivia: Quantitative Performance Criteria, 2003 1/

	End-Mar. 2003				2003 Performance Criteria		
	Perf. Crit.	Adj. Target 2/	Actual	Margin	End-June	End-Sep.	End-Dec.
(Cumulative amounts from December 31, 2002 in millions of bolivianos)							
Deficit of the combined public sector	800	831	718	113	1,450	2,250	3,793
Net domestic financing of the combined public sector	500	650	608	42	-200	-25	73
(Cumulative changes from December 31, 2002 in millions of bolivianos)							
Net domestic assets of the central bank	725	725	262	463	250	-500	-245
Of which : central bank net credit to the nonfinancial public sector	350	350	311	39	175	-325	-82
(Cumulative changes from December 31, 2002 in millions of U.S. dollars)							
External debt of the public sector with maturities up to one year	15	15	6	9	10	10	0
Nonconcessional external debt of the public sector (net)	15	15	-44	59	50	100	150
Net international reserves of the central bank 3/	-170	-170	-110	60	-90	0	65
External arrears, stock at end of period (continuous performance criterion)	0	0	0	0	0	0	0

1/ All definitions and adjusters provided in the Technical Memorandum of Understanding signed on March 21, 2003 and its attached Table 1 are applicable.
2/ Adjusted according to the provisions of the Technical Memorandum of Understanding signed on March 21, 2003.
3/ Excluding restricted deposits, which increased from US$34.0 million on December 31, 2002 to US$35.5 million on March 31, 2003.

Table 2. Bolivia: Structural Performance Criteria for the First Review of the 2003 SBA 1/

Policy Measure	Original date	Status
Public Sector Reform and Financing		
Approval of 2003 budget, which together with the proposed revenue measures described in para. 11 of the TMU is consistent with a combined public sector deficit equal to or less than 6.5 percent of GDP.	April 15, 2003	Budget approved on April 3, 2003 but tax bill was delayed. Alternative measures to meet the fiscal target have been taken. Waiver requested.
Submission to congress of a tax procedures code consistent with para. 12 of the TMU.	April 30, 2003	Met.
Financial Sector and Corporate Sector		
Issuance of the final regulations for the bank resolution and prompt corrective action mechanisms introduced by the financial sector law of 2001 consistent with para. 14 of the TMU.	April 30, 2003	Implemented on May 9, 2003. Waiver requested.
Issuance of supreme decree(s) (i) clarifying the roles of the different institutions with oversight over the financial sector (includes ensuring a technical basis for issuing prudential norms), and (ii) defining certain areas of banking regulation that should be determined by the superintendency consistent with para. 13 of the TMU.	April 30, 2003	Implemented on May 6, 2003. Waiver requested.
Submission to congress of draft bankruptcy law and draft law for corporate debt workout mechanism, prepared in consultation with Fund staff and consistent with paras. 15 and 16 of the TMU.	April 30, 2003	Met.

1/ References in the table are to the relevant paragraphs of the Technical Memorandum of Understanding signed on March 21, 2003.

Table 3. Bolivia: Structural Conditionality Under the Stand-By Arrangement, July–December 2003 1/

Condition	Policy Measure	Timetable for Implementation 1/
	Public Sector Reform and Financing	
Benchmark	Approval by congress of a tax procedures code consistent with para. 12 of the TMU	September 30, 2003
	Financial Sector and Corporate Sector	
Benchmark	Approval by congress of law on corporate workout mechanism consistent with para. 16 of the TMU	September 30, 2003
Benchmark	Approval by congress of bankruptcy law consistent with para. 15 of the TMU	September 30, 2003

1/ References in the table are to the relevant paragraphs of the Technical Memorandum of Understanding signed on March 21, 2003.

INTERNATIONAL MONETARY FUND

BOLIVIA

Staff Report for the 2003 Article IV Consultation, First Review Under the Stand-By Arrangement, and Request for Waiver of Performance Criteria

Supplementary Information

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

Approved by Charles Collyns and Michael T. Hadjimichael

July 3, 2003

This supplement provides information that has become available since the staff report was issued on June 25[1]. This information does not affect the staff appraisal.

1. Recent Economic and Financial Developments

Economic activity and inflation. Real GDP rose by 1.4 percent in the first quarter of 2003, compared with a year earlier, with strong contributions from the agriculture and manufacturing sectors more than offsetting weak mining and construction activity and the impact of the tragic events of February. This growth rate is consistent with the program projection of 2.9 percent for the year as a whole. The 12–month rate of inflation was 3.2 percent in June, virtually unchanged from April-May 2003.

Fiscal performance. The cumulative fiscal deficit over January-May was above fiscal program projections, mainly due to shortfalls in tax revenue and lower than expected grants. The authorities explained that, in recent weeks, they have taken offsetting actions to control spending, particularly on investment, and expect to observe the June deficit ceiling.

External financing. Disbursements from the World Bank (program loans for decentralization and social sector protection) and the Inter-American Development Bank (program loan for tax administration and pension reform) totaling US$81 million were received in June, as envisaged in the program.

Financial system. Deposits have continued a moderate but steady recovery, following the sharp drop in February. As of June 27, 2003, deposits were US$130 million above the end-February level, although still US$19 million below their level at end–2002.

[1] A mission visited La Paz during the period June 25–27, 2003.

International reserves. Gross official reserves have increased steadily in June and, as of June 27, were US$891 million, about US$37 million higher than at end–2002. The end-June target for net international reserves is expected to have been met by a large margin.

2. Policy Developments

The authorities have taken a series of steps in recent weeks to build consensus for the passage of key economic legislation. A team from the ministry of finance met with bankers, business associations and parliamentarians to receive feedback on the drafts of the proposed new tax code, bankruptcy law, and informal workout mechanism (the approval of these laws is subject to end-September structural benchmarks). In addition, a joint finance committee from both legislative chambers is undertaking a consultation process with the aim of securing broad consensus for the early passage of these laws.

In the context of the corporate restructuring strategy, a comprehensive database has been completed on the liabilities of large corporations. The authorities have begun using information on corporate debts by sector, region, and creditor to assess the impact on banks of alternative approaches to corporate restructuring.

A short mission that visited La Paz during June 25–27 met with the donor community to discuss the schedule for the PRSP process. A PRSP progress report is expected to be completed by early August that would include the broad structure of a revised PRSP. The progress report would form the basis of continued discussions with the staff on a possible PRGF-supported program.

3. Safeguards Assessment

The safeguards assessment of the Central Bank of Bolivia (CBB) has just been completed. It has concluded that there are no systemic risks in the safeguards of the CBB. It raised issues related to the CBB's reporting of NIR and identified possible risks to Fund resources stemming from recent interference by the government over the CBB's budget and credit operations.

The assessment, referred to in paragraph 58 of the staff report, identified a few anomalies in the CBB's reporting of the stock position of NIR at December 31, 2002. Specifically:

- The measure of NIR included (i) a series of deposits that are reported as restricted assets in the audited financial statements and (ii) a foreign asset denominated in Andean Pesos that may not be readily convertible to usable foreign currency.

- The measure of NIR excluded long-standing CBB debts owed to two countries in the region. However, the audited financial statements refer to these as "reserve liabilities", putting into question the maturities of the underlying debts. The maturities will need to be clarified to determine whether these debts should be included as part of NIR liabilities.

The authorities and staff are in a process of addressing the anomalies in NIR reporting identified in the safeguards assessment. Staff has subsequently excluded the deposits classified as restricted assets when determining the cumulative flow of NIR for the March 31, 2003 test date and the authorities have agreed with this treatment. After this adjustment, NIR and NDA performance criteria for end-March continue to be met. Staff continues its investigation of the broader consequences of the data reporting issues and further clarifications will be sought from the authorities in the period ahead. As additional precaution, the staff has proposed that the CBB conduct internal reviews of the reconciliation of the monetary program data prepared for the IMF with the audited accounting records.

The staff saw potential risks from recent intervention by the government over the central bank's budget and credit operations. These actions included requests for central bank liquidity credits to the government, proposals for increased profit transfers from the CBB, and the reduction in the CBB's wage bill. To minimize these risks and increase central bank autonomy, the staff has proposed that the Minister of Finance and the CBB President formally endorse a Memorandum of Understanding guaranteeing the CBB's operational and budgetary independence. This issue will be discussed with the authorities at the next review.

INTERNATIONAL MONETARY FUND EXTERNAL RELATIONS DEPARTMENT

Press Release No. 03/103
FOR IMMEDIATE RELEASE
July 7, 2003

International Monetary Fund
Washington, D.C. 20431 USA

IMF Completes First Review of Bolivia's Stand-By Arrangement, Approves US$15 Million Disbursement

The Executive Board of the International Monetary Fund (IMF) today completed the first review of Bolivia's performance under a one-year, SDR 85.75 million (about US$121 million) Stand-By Arrangement, which was approved on April 2, 2003 (see Press Release No. 03/46). The completion of this review enables the release of SDR 10.72 million (about US$15 million) to Bolivia.

The Executive Board also approved Bolivia's request for waivers of the non-observance of certain performance criteria and of the applicability, until July 17, 2003, of quantitative performance criteria for end-June 2003.

Following the Executive Board discussion on Bolivia, Anne Krueger, First Deputy Managing Director and Acting Chair, said:

"Performance under Bolivia's economic program supported by the Stand-By Arrangement so far has been encouraging. Despite the difficult political and social environment, the economic situation remains under control, there are some signs of recovery in the agricultural and manufacturing sectors, bank deposits are almost back to end-2002 levels, and inflation remains subdued.

"The policy framework for 2003 is establishing a basis for sustained growth. A central element of the framework is a substantial reduction in the fiscal deficit needed to achieve fiscal sustainability, while protecting spending on poverty alleviation programs. Timely fiscal adjustments have been made to keep the 2003 fiscal program on track, mainly through better targeting of public investment and current spending. The government is continuing its efforts to push ahead with its fiscal reform agenda, including by proposing a modern tax procedures code to Congress, controlling the high transitional costs of the pension reform, and improving the effectiveness of fiscal decentralization.

"Progress is being made toward putting in place a comprehensive strategy for restructuring the corporate and financial sectors. Initial steps include the issuance of regulations for bank resolution and for prompt corrective action for banks with problems, and the appointment of a high-level team to oversee the overall strategy. Further steps in the authorities' agenda for 2003 entail the approval by Congress of a modern bankruptcy law and an appropriate voluntary debt workout mechanism, and strengthening the judicial system's ability to handle bankruptcy proceedings. The restructuring of the financial and corporate sectors is essential for the resumption of bank credit and sustained economic growth.

"Effective utilization of Bolivia's abundant natural gas resources is crucial to ensure favorable longer term growth prospects. The government is working to develop public support for proceeding with the LNG export project in a way that maximizes the project's contribution to realizing Bolivia's growth potential.

"The authorities are building upon the progress made under the Stand-By Arrangement by developing a medium-term economic program aimed at fostering a higher rate of growth and poverty reduction. They plan to request support under the IMF's Poverty Reduction and Growth Facility during the last quarter of 2003," Ms. Krueger stated.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 03/102
FOR IMMEDIATE RELEASE
August 20, 2003

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

IMF Concludes 2003 Article IV Consultation with Bolivia

On July 7, 2003, the Executive Board concluded the Article IV consultation with Bolivia.[1]

Background

Economic activity has been sluggish since 1999, but has shown some signs of recovery in 2002 and early 2003. Real GDP growth averaged only 1.4 percent during 1999–2001, dampened by the regional slowdown and an appreciation of the real exchange rate, as well as the impact of the coca eradication program. Growth increased to 2.8 percent in 2002, boosted by the building of a new pipeline to Brazil as well as public works and transportation projects, although other domestic demand remained weak. Unemployment has risen in the last three years to 8½ percent, and about half of the labor force remains underemployed. As of 2002, about two thirds of the population lived below the poverty line, with one-third in extreme poverty.

The fiscal deficit increased sharply in 2001-02. The combined public sector deficit rose to nearly 9 percent of GDP in 2002 (from about 3½ percent of GDP in 2000). Fiscal revenues weakened because of sluggish domestic demand, delays in tax reforms, and a freeze on domestic fuel prices since mid-2001. The fiscal deficit also reflected an increase in net pension outlays from 4½ percent to 5 percent of GDP during this period.

Nonfinancial public sector debt increased from 58½ percent of GDP in 2000 to 61¼ percent in 2002, including substantial increases in domestic financing and in nonconcessional foreign borrowing. As a result, despite the enhanced HIPC debt relief received in June 2001 which, by

[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.

itself, reduced the net present value (NPV) of external debt by 15 percentage points of GDP, the NPV of public debt as of end–2002 remained at its end–2000 level of 45 percent of GDP.

The contraction of financial system activity, which began in 1999, became more pronounced in 2001-02, contributing to a loss in international reserves. Bank credit and deposits have declined as political uncertainty and sluggish growth have weakened confidence in the banking system and resulted in more cautious behavior by banks. Since the end of 1998, bank credit has declined by more than 30 percent in U.S. dollar terms, and deposits by some 24 percent. Two episodes of heavy withdrawals of deposits (in mid-2002 and in February 2003) were halted after the central bank supplied liquidity. The coverage of broad money by gross international reserves declined from over 40 percent at end-1999 to 34½ percent at end-2002. Monetary policy was eased over 2001–02 in the face of increased government financing needs and liquidity requirements of the banking system, before being tightened in recent months.

Several years of financial disintermediation and economic stagnation have added to vulnerabilities in a highly dollarized financial system. (Around 92 percent of deposits and 97 percent of loans are denominated in US dollars.) The nonperforming loan ratio rose to 20 percent as of end-May, largely as a result of the corporate sector's weak cash flow. Banks' capital adequacy ratios exceed the minimum requirement, partly reflecting a recapitalization in December 2001 of three banks through subordinated loans guaranteed by the public sector.

The central bank stepped up the pace of currency depreciation against the US dollar to 10 percent in 2002 in response to domestic and external shocks, including the political uncertainties that prompted a 15 percent reduction in bank deposits in June-July 2002. The boliviano appreciated in real effective terms by more than 4 percent in 2002 because of the weakness of the currencies of the main regional trading partners. With the neighboring countries' currencies gaining strength in recent months, the boliviano depreciated by 11 percent in real effective terms during the first five months of 2003, while the rate of crawl against the US dollar slowed to an annual rate of 4 percent.

The authorities' economic program for 2003 focuses on stabilizing the economy and laying the basis for a higher rate of sustained growth. The program projects a gradual economic recovery, with real GDP growth reaching about 3 percent, led by an expansion of natural gas production, a strong performance in the agriculture sector, and a boost to manufacturing, particularly textiles, from the expanded preferential access to the U.S. market for the Andean countries. The external current account is projected to improve by 1½ percent of GDP as a result of higher exports on natural gas, soybean products, and textiles. The fiscal program aims to reduce the combined public sector deficit to 6.5 percent of GDP in 2003.

Executive Board Assessment

Executive Directors noted that difficult economic and political circumstances have heightened the Bolivian economy's vulnerabilities, and welcomed the government's emphasis on regaining fiscal sustainability, strengthening the corporate and financial sectors, and achieving sustained growth and poverty reduction. Directors encouraged continued efforts to secure broad political and social support for their policy agenda, and welcomed their intention to adopt a PRGF-supported program soon.

Directors expressed concern about the rising external debt and the increasing pressure toward nonconcessional borrowing. They commended the policy actions taken by the authorities to put in place a prudent fiscal framework that would set the debt ratio on a firm downward path. These actions have included politically courageous decisions to defer low-priority spending and begin the process of broadening the tax base. Directors highlighted the importance of building on these initial actions and broadening fiscal reforms to underpin medium-term fiscal consolidation.

Directors saw room for further improving the efficiency of public spending and its targeting to support poverty alleviation. They commended the authorities' plans for deepening tax reform and improving tax administration through a modern tax procedures code, and urged the authorities to work at building public support in these endeavors, and to continue efforts to secure congressional approval of revenue measures. Controlling pension reform costs and enhancing the effectiveness of fiscal decentralization also were seen as key to achieving fiscal sustainability. While supportive of steps to promote inflation-indexed savings instruments, Directors concurred on the need to reduce reliance on pension funds for government financing. A few Directors felt that the use of inflation-indexed bonds would lead to a better matching of assets and liabilities and the greater use of market interest rates.

Directors supported the policy of gearing monetary policy towards maintaining low inflation and a gradual build-up of international reserves, and welcomed the recent stability of deposits in the banking system. They noted that a shift toward monetary tightening would be needed if inflation pressures were to develop. Directors noted with concern the constraint on policy-making and risks to the financial system stemming from high dollarization, and supported steps toward gradual and voluntary de-dollarization. These would include consistent monetary policy implementation to make clear the government's commitment to low inflation; and implementation of measures to promote boliviano-denominated savings, including bringing small depositors into the banking system. Directors stressed the importance of maintaining the central bank's financial strength. They therefore expressed concern about the authorities' proposal to alleviate the treasury's cash flow position through increased transfers of central bank profits to the treasury. They encouraged consultation with the Fund before proceeding with these transfers.

Directors welcomed the authorities' support for an independent central bank, and the authorities' prompt response in having begun to address the weaknesses identified in the safeguards assessment. They commended the authorities' efforts to combat money laundering and terrorism financing, and encouraged further action, such as strengthening the financial intelligence unit. Directors were also impressed by the performance of microfinance institutions noting their low non-performing loan ratio and their significant contribution to financial deepening and poverty reduction in disadvantaged areas.

Directors believed that the depreciation of the boliviano in real effective terms since late 2002 would help to bolster Bolivia's competitiveness. They supported the authorities' strategy to move toward a more flexible exchange rate regime in the medium term but stressed that the transition should be handled carefully in view of the high degree of dollarization and the related financial and corporate vulnerabilities. Directors agreed that the central bank should maintain a high level of international reserves to strengthen its lender-of-last resort capability.

Directors welcomed the progress made in developing a comprehensive strategy for restructuring the financial and corporate sectors. Regulations governing bank resolution and corrective action for banks with problems have been issued, along with a decree that clarifies the roles of the different institutions charged with oversight of the financial sector. Directors also endorsed the authorities' plan to implement a new corporate bankruptcy law and a voluntary restructuring framework as soon as they receive congressional approval. They encouraged continued momentum on financial and corporate restructuring through development of a framework for the use of public funds for restructuring, putting in place procedures for responding to bank failures, and refining the draft legislation.

Directors supported the government's plan to develop a medium-term economic program aimed at fostering a higher rate of sustained growth and poverty reduction. Such a program should focus on removing the obstacles to growth in Bolivia, including inefficient infrastructure, labor market rigidities, inadequate investment in human capital, and governance problems. Directors welcomed the coca eradication program, and stressed that alternative employment opportunities and a social safety net need to be provided for the former coca farmers. Directors urged the authorities to move quickly on large natural gas projects, including by building a public consensus for proceeding with the LNG export project on economic grounds, which would be important for realizing Bolivia's growth potential. Directors encouraged steps to reduce corruption in order to promote foreign direct investment. They also encouraged firms to take advantage of U.S. preferential access for Andean countries to boost export growth.

Directors noted the authorities' intention to request the IMF's support through the PRGF for their medium-term program in the coming months. They expressed satisfaction that the authorities are addressing the shortcomings of the 2001 Poverty Reduction Strategy Paper (PRSP), particularly with regard to the participatory process. They stressed that the Congress should play a more central role in the participatory process of the PRSP, and welcomed the authorities' consensus-building strategy to gain greater country ownership of the economic strategy.

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 2003 Article IV Consultation with Bolivia is also available.

Bolivia: Selected Economic Indicators

	1999	2000	2001	2002	Proj. 2003
(Annual percentage change, unless otherwise indicated)					
Income and prices					
Real GDP	8.0	2.3	1.5	2.8	2.9
Real domestic demand	-2.0	1.2	-2.5	1.6	1.2
CPI (end of period)	3.1	3.4	0.9	2.4	2.8
Bolivianos/U.S. dollar (end of period) 1/	6.00	6.40	6.83	7.50	7.67
REER (percentage change during year) 2/	2.2	-1.5	-3.4	4.4	-11.1
(In percent of GDP)					
Investment and savings					
Gross domestic investment	18.8	18.3	14.2	14.7	14.2
Gross national savings	12.9	13.0	10.8	10.4	11.4
External savings	5.9	5.3	3.4	4.3	2.8
Combined public sector					
Nonpension balance	0.6	0.7	-2.1	-3.9	-1.6
Pension-related balance	-4.1	-4.5	-4.8	-5.0	-4.8
Overall balance	-3.5	-3.7	-6.9	-8.9	-6.4
External financing	1.9	2.0	3.1	6.1	6.3
Domestic financing	1.6	1.8	3.9	2.8	0.1
Nonfinancial public sector debt	59.5	58.6	53.6	61.3	67.6
(Annual percentage change)					
Money and credit					
Broad money (in U.S. dollars at current exchange rates)	-1.8	-3.3	-3.1	-11.7	3.8
Credit to private sector (in U.S. dollars at current exchange rates)	-2.0	-9.0	-13.6	-9.5	1.5
External sector (US$ million)					
Current account	-488	-446	-276	-338	-218
(Percent of GDP)	-5.9	-5.3	-3.4	-4.3	-2.8
Capital and financial account	515	408	255	45	265
Of which: foreign direct investment	1,014	701	666	654	600
Overall balance	26	-39	-21	-293	48
Exceptional financing	16	15	9	17	17
Gross international reserves 3/					
(Months of imports of goods and services)	8.7	8.7	8.1	6.3	6.9
(In percent of broad money)	40.2	39.7	39.2	34.6	38.2

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

1/ Official (sell) exchange rate; July 4 for 2003.
2/ Weights based on average trade, excluding trade related to natural gas, in 1996-97. Positive variation is an appreciation.
3/ Equal to central bank's gross official reserves plus commercial banks' liquid asset requirement (RAL) held overseas; excludes reserves from the Latin American Reserve Fund (FLAR). End-2002 figures reflect an increase of US$45 million in the valuation of holdings of gold; import coverage for the following year.

Statement by Guillermo Le Fort, Executive Director for Bolivia and Alonso Segura, Assistant to Executive Director
July 7, 2003

Key Points

- Conditionality under the program has been mostly met. Two technical waivers for a few days delay in approval of measures are requested. A waiver for revenue measures, still pending approval of Congress,is also requested.
- Contingency measures have been implemented to maintain the fiscal program on track. However, unexpected delays in disbursement of grants are adding pressure on expenditure cuts and domestic financing.
- Financial and corporate restructuring mechanisms remain a priority. Major pieces of legislation have been submitted to Congress.
- A PRSP progress report is due in August 2003, in line with a request for a new PRGF Arrangement in October 2003.

Overview and Recent Developments

1. We thank the Staff for a thorough set of papers that clearly presents the challenges faced by Bolivia at the current juncture. The Stand-By Arrangement underway is envisioned by the Bolivian authorities as a bridge program that will enable them to stabilize the economy and garner broader consensus for structural reforms and a medium-term economic program, in the midst of a difficult political and social environment. This one-year SBA is also allowing my authorities to demonstrate their ownership of the program, and build the necessary conditions for a prompt transition towards a PRGF arrangement.

2. My authorities have devoted their efforts to tackling the obstacles to economic growth and stability, which have been considered at the core of the program conditionality approved by the Fund last April. All quantitative performance criteria for end-March have been met, as well as all, but one structural performance criterion, which has been missed due to reasons out of the control of the Executive Branch. However, my authorities remain committed to push forward any necessary substitutive measures to attain the envisioned goal in this regard. In addition, two other SPCs were technically missed, due to a few days delay in the approval and publication of the corresponding regulations. On the challenging agenda, important advances have been made in fiscal consolidation, pension reform, banking and corporate restructuring, governance improvement and drafting a PRSP progress report which, together with the launching of a national dialogue will be conducive to a new PRSP. Furthermore, the authorities agree in setting performance criteria identical to the existing indicative targets for end-September and end-December 2003.

Fiscal Policy and Debt Dynamics

3. The Bolivian authorities reaffirm their commitment to correct the fiscal slippages of 2001 and 2002, by attaining fiscal consolidation according to the medium-term convergence path outlined in the program, which requires a cumulative adjustment of over 5 percent of GDP to be gradually achieved through 2008. In the short-term, given the delays in Congressional approval of important revenue measures, my authorities have proceeded to activate their contingency measures by cutting back non-priority spending, while ensuring that social spending in 2003 will continue to increase as a share of GDP, as considered in the program. Further contingency plans are being delineated, in order to ensure compliance with the fiscal targets under the SBA. It is worth noting that grants are not being disbursed with the desired swiftness; these delays are forcing the authorities to rely disproportionately on domestic financing and exerting additional pressure on expenditure cuts to meet end-June targets.

4. The modified budget for 2003 was passed by Congress, but the accompanying tax bill has not been approved yet and is still under discussion, resulting in the non-compliance of a structural performance criterion, for which the authorities are asking for a waiver. The tax bill has faced strong opposition in Congress, forcing the withdrawal of some measures such as taxes on travel, alcoholic beverages, cell-phones and cable TV, among others. However, as already underlined, compensatory expenditure cuts have been effected, so as to maintain the fiscal program on track. The implementation of a new tax procedure code (benchmark for end-September), remains a pillar of the fiscal reform, since it will allow the authorities to address the problem of widespread tax evasion. While acknowledging the drawbacks of tax regularization schemes, in my authorities' view, this one-off measure will enable troubled corporate taxpayers to fulfill their obligations over the medium-term, given the current juncture of corporate distress, by smoothing-out payments over a five year period, and will facilitate passage of the tax bill. My authorities are fully aware on the need for an urgent approval of the tax bill as the uncertainty during its discussion in Congress is affecting tax compliance.

5. On the expenditure side, along with the aforementioned cuts in current and specially non-priority investments, several measures have been taken to control the rising pension costs. In line with a previous Buff Statement, tighter administrative controls, aimed at eliminating fraudulent claims and for a strict enforcement of the eligibility criteria are being introduced, and regulations to switch the indexation of pensions from the exchange rate to inflation have also been enacted, among other measures to rein on pension expenditures. A comprehensive action program for the transition to the capitalization in individual accounts is being developed with the advice of the IADB. Moreover, a newly-created Vice-Ministry will monitor the process adequately. It is important to keep in mind that reforming the pension system was a crucial step in the process of structural adjustment, whose benefits will still be reaped in the medium-term.

6. We thank staff for their useful analysis on debt sustainability. Under the envisaged baseline scenario, public debt would follow a sustainable medium-term path, provided fiscal consolidation is attained, even though external debt indicators would be higher than anticipated when reaching the decision point under the Enhanced HIPC Initiative. As pinpointed in the previous discussion, the Bolivian authorities are well aware of the risks highlighted in the stress tests, one of these being the high degree of dollarization of the public debt. Its reduction, however, is seen as a long process, buttressed by monetary stability and handled through market incentives towards a greater voluntary acceptance of the Bolivian currency (the "boliviano"), like regulations in the financial and pension systems and mainly by sustaining monetary stability over long periods.

   It is also important to stress that while financing from the IADB has been secured for the next five years, Bolivia's sustained access to multilateral and alternative (bilateral) sources of concessional funding would translate in a significant medium-term ease on fiscal accounts and on the debt, as shown in the staff's sensitivity analysis.

7. With respect to the recent concerns expressed by Staff on the switch of roughly half the stock of dollar-indexed public bonds held by pension funds (AFPs) for inflation-indexed bonds, the returns on those bonds are well above current market returns, since rates have not been adjusted since 1997 (while they could have adjusted annually), and also would provide a better matching for AFPs liabilities given the recent indexation of pensions (starting in 2004) to inflation. However, my authorities are aware of the need, in the medium-term, of reducing the AFPs financing share of the fiscal deficit. Preparatory work is underway to deal with both issues, conversion to inflation-indexed bonds and allocating a smaller share of bonds to the AFPs, simultaneously.

Monetary and Exchange Rate Policy

8. As noted in the safeguards assessment, recently conducted at the Banco Central de Bolivia (BCB), controls currently in place are generally adequate to safeguard BCB´s resources and IMF disbursements and no sources of systemic risks in the BCB´s safeguards could be identified. My authorities are taking the necessary steps to implement the recommendations raised by the Staff, as stated in their response letter, to correct the identified weaknesses. It is worth highlighting two issues. First, the Bolivian authorities reaffirm their commitment and support for an independent and autonomous Central Bank, as stated in the Bolivian Legislation. As a proof of this stance, they are requesting technical assistance to the Fund, in the issue related to the transfer of BCB's profits, spanned by capital gains associated to foreign exchange holdings, to the Treasury, prior to any decision. Discussions between the BCB and the Ministry of Finance are underway, in order to agree on the terms of the recommended Memorandum of Understanding. Second, while the suggested amendments to the Central Bank Law (Law 1670) are accepted, my authorities believe that it is not opportune to open this law for discussion, given the political context.

9. The Bolivian authorities agree on the benefits of moving towards a more flexible exchange regime on the medium-term. As it has been recently reviewed, the difficulty in dealing with de facto highly (financially) dollarized economies is worthy of mention. They are aware that by reducing the exposure of the economy to exchange rate risk, a greater flexibility could be accomplished in consistency with macro-economic and financial stability. Consequently, my authorities are devoted to gradually inducing a greater use of domestic currency in the economy. They have started with the promotion of the new inflation-indexed unit of account (UFV), that is being already applied to pensions and taxes and is to be extended gradually to financial instruments like bank deposits and loans. Also they will take other market-friendly measures to disincentive dollar-based financial intermediation, like increasing the minimum reserve requirement for dollar deposits, in the same line, the central bank liquidity assistance in dollars to banks already commands high interest rates. Furthermore, there are plans for commercial banks to internalize, by way of loan provisions, the risks derived from currency mismatches of their borrowers.

Structural Reforms

10. The Bolivian authorities have been dealing intensively with the fragile situation of the corporate and banking sectors. Many of the core recommendations of the FSSA have already been implemented, including the clarification of roles between supervisory institutions in the financial sector. On the banking sector, provisioning requirements by banks have already been met (as of March 2003), under a decree issued previously. The authorities have taken note of the assessments contained in the FSSA regarding the recent weakening of prudential regulation and the required standards for banks. Capital ratios and provisions have increased overall and have been effective in avoiding a systemic crisis, even under the strong pressure of the two deposit runs in the past year. Banks′ liquidity has been increasing as a precautionary measure, and is deemed to be at adequate levels. Yet, it is unavoidable that some institutions will have less liquidity than others. Therefore, the BCB stands ready to provide liquidity support, if needed, under the pre-specified conditions. For this purpose, we want to emphasize the high external liquidity of the BCB with gross official reserves substantially above 40 percent of short-term external debt, and disposable reserves (of BCB and banking system), including banks′ required liquid assets held abroad exceeding 32 percent of dollar denominated deposits. Both reserves and deposits have been growing steadily since February. In addition, there are available back-up lines from FLAR that amount to US$ 190 million, equivalent to approximately 20 percent of gross reserves.

11. On the corporate front, major pieces of legislation have been submitted to Congress (benchmarks to the program), which would provide the legal framework to develop orderly out-of-court corporate workouts and bankruptcy procedures, which have been developed with the participation of the World Bank. It is expected that the legislation will be approved by end-September, as envisaged under the program. A contingent plan based on changes to the Code of Commerce will be implemented alternatively, if the draft bankruptcy law meets a too strong opposition in Congress.

12. With respect to sources of growth, negotiations between Pacific-LNG and potential buyers in North America for the LNG-gas project are on good track. It is expected that once an agreement is reached between these parties, the authorities will be able to announce the port of shipment for gas exports to California. Social and political concerns with regard to the port of shipment have lately receded and more weight is given to technical and cost efficiency considerations. Also, it is the authorities' intention to preserve the recent gains in competitiveness with the real effective exchange rate, which together with a plan to benefit from the recently approved Andean Trade Preferences and Drug Eradication Act (ATPDEA) by the U.S., would provide an important engine for non-energy export growth.

PRGF Arrangement

13. The Bolivian authorities are in the process of designing a PRSP progress report, addressing the causes that led to the derailing of the previous PRGF in 2001, as well as containing a sensible strategy to attain sustainable growth and poverty reduction. The progress report is expected by August 2003, consistent with a request to the Board for a new PRGF arrangement by October 2003. The authorities are devoting their utmost efforts to foster wide participation, and again are launching a National Dialogue, in order to incorporate the civil society's, donors', political parties', and other actors' point of view, in the government's strategy. Also, proper attention is being given to governance issues, as highlighted by the Staff.

14. The Bolivian authorities have demonstrated a strong commitment to the program, despite the prevailing adverse political and social scenario that gave rise to the events of last February. Conditions have improved, but remain fragile. Still most of the conditionality under the program has been met. There are risks and challenges lying ahead, but the authorities' response to incipient program deviations by introducing compensatory measures show their commitment to keep ongoing their ambitious reform program. Bolivia can show a solid track record as the basis for granting the requested waivers and conclude the first review.