INTERNATIONAL MONETARY FUND

IMF Country Report No. 15/334

BOLIVIA

December 2015

2015 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; 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 the 2015 Article IV consultation with Bolivia, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its November 20 consideration of the staff report that concluded the Article IV consultation with Bolivia.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on November 20, following discussions that ended on September 15, 2015, 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 November 5, 2015.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Bolivia.

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Press Release No. 15/571
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December 18, 2015

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

IMF Executive Board Concludes 2015 Article IV Consultation with Bolivia

On November 20, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Bolivia.

Benefiting from the commodity boom, Bolivia has achieved strong economic performance and poverty reduction over the past decade. Real GDP growth has averaged about 5 percent since 2006, and the poverty ratio has declined by 16 percentage points. However, given Bolivia's dependence on commodities, lower commodity prices pose significant challenges to deliver the objectives in the Patriotic Agenda 2025, while maintaining debt and external sustainability.

Real GDP growth is projected to stay relatively strong at 4.1 percent in 2015, despite the sharp decline in oil prices that is starting to have an impact. A sizable public investment budget, strong credit growth to the private sector, and robust private consumption are expected to support activity. Growth is expected to decelerate to 3.5 percent over the medium term, as the full impact of the new commodity price normal is felt and given impediments to enhancing private investment. The fiscal deficit is projected to widen and the current account balance to swing into deficit in 2015, and twin deficits are expected to persist over the medium term. The authorities are finalizing a 5-year development plan (Plan Quinquenal), including public investment projects in a number of areas to catalyze growth.

While headline financial indicators are solid, the 2013 Financial Services Law is affecting the allocation of credit flows. Minimum credit quotas to productive and social housing sectors have accelerated loans to those sectors.

Key external risks include a slowdown in key trading partners, additional softness in oil prices, and further dollar strength. Bolivia-specific risks center on uncertainties related to natural gas reserves and long-term export contracts, and large credit cycles under the new financial services law.

[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.

Executive Board Assessment[2]

Executive Directors commended the Bolivian authorities for a prudent macroeconomic management which has supported strong non-inflationary GDP growth and greatly improved social outcomes over the past decade. Looking ahead, Directors agreed that the likelihood of a protracted period of depressed export prices poses challenges to the outlook and risks are tilted to the downside. They noted, however, that the sizable policy buffers built during the commodity upcycle allow for a gradual approach in adjusting to a less favorable external environment, and provide a strong base for further structural and institutional reforms.

Directors concurred that prospective budgetary deficits in the context of slower growth and tighter global financial conditions may have an adverse impact on Bolivia's fiscal position. Accordingly, they encouraged the authorities to improve the non-hydrocarbons fiscal balance through a variety of tax and expenditure measures. A better articulated medium-term fiscal framework centered on a clear fiscal anchor would enhance the credibility of the authorities' fiscal plans. In this regard, Directors also recommended a more comprehensive system for monitoring the quasi-fiscal activities of state enterprises to better manage fiscal risks.

Directors welcomed the effectiveness of the authorities in anchoring inflation expectations and promoting de-dollarization. They shared the view that progress on these fronts would be cemented by granting greater operational independence to the central bank in the new law under preparation. The credibility of monetary policy would also be boosted by relegating direct lending to a separate sovereign wealth fund with transparent investment rules and strong governance. Directors generally saw merit in creating conditions for a move toward greater exchange rate flexibility at an appropriate time to facilitate adjustment to large external shocks and enhance competitiveness.

While noting the overall soundness of Bolivia's financial sector, Directors pointed to risks stemming from some regulations set under the Financial Services Law, particularly credit quotas and interest rate caps. They encouraged the authorities to closely monitor developments and modify the regulations appropriately if financial imbalances emerge. In this context, compilation of a real estate price index would greatly aid policy evaluation and design.

Directors agreed that increasing private investment is essential to support growth both in the near and the longer term. In this regard, they welcomed progress in strengthening the legal framework and recommended further efforts in this area. Directors also encouraged the authorities to address

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[2] 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. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

long-standing structural impediments to private investment, notably inflexible labor markets and pervasive state-intervention in product markets.

Directors commended the authorities for the significant declines in inequality and poverty achieved over the past decade. In order to preserve these gains under an expected tighter fiscal envelope, they recommended well-targeted social transfers with a focus on the quality of education and healthcare.

Bolivia: Selected Economic Indicators

	2010	2011	2012	2013	2014	Proj. 2015	Proj. 2016
	(Annual percentage changes)						
Income and prices							
Real GDP	4.1	5.2	5.1	6.8	5.5	4.1	3.5
GDP deflator	8.8	14.6	7.1	6.0	2.0	-3.1	1.5
CPI inflation (period average)	2.5	9.9	4.5	5.7	5.8	4.3	4.9
CPI inflation (end-of-period)	7.2	6.9	4.5	6.5	5.2	4.2	5.0
	(In percent of GDP)						
Combined public sector							
Revenues and grants	33.2	36.2	37.8	39.1	39.9	35.1	32.6
o/w: Hydrocarbons related revenue	10.2	11.4	13.0	13.5	12.7	7.7	5.5
Expenditure	31.5	35.4	36.0	38.4	43.3	40.4	38.4
Overall balance	1.7	0.8	1.8	0.7	-3.4	-5.3	-5.8
Total gross public debt	38.5	34.7	33.3	32.5	33.0	38.0	42.0
External sector							
Current account	3.9	0.3	7.2	3.4	0.1	-4.5	-5.0
Merchandise export	32.4	34.6	41.3	37.7	36.9	27.2	24.0
Of which: Natural gas	14.1	16.1	20.1	19.8	18.0	11.0	8.5
Merchandise imports	28.3	32.8	31.4	30.2	31.6	29.5	27.6
Gross international reserves							
In millions of U.S. dollars	9,730	12,019	13,927	14,430	15,123	14,143	12,878
In percent of broad money	80.0	83.0	80.0	71.4	64.7	54.2	45.1
	(Changes in percent of broad money at the beginning of the period)						
Money and credit							
NFA of the banking system	8.2	14.7	13.5	4.7	6.0	-1.6	-2.6
NDA of the banking system	1.4	1.6	4.4	11.9	9.4	11.8	10.7
o/w: Credit to the private sector (in percent of GDP)	36.0	36.8	39.0	40.9	43.7	49.0	52.2
Broad money	12.5	17.7	20.2	16.2	15.6	11.7	9.5
Interest rates (percent, end-of-period)							
Deposits in local currency	0.9	1.7	1.2	2.7	2.5	…	…
Loans in local currency	10.4	10.8	10.6	11.4	8.0	…	…

Sources: Bolivian authorities; and IMF staff estimates and projections.

INTERNATIONAL MONETARY FUND

BOLIVIA

STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATION

November 5, 2015

KEY ISSUES

Context. Facilitated by prudent macroeconomic management in the context of a commodity boom, Bolivia has achieved strong macroeconomic performance and poverty reduction over the past decade. However, given Bolivia's large dependence on commodities, the collapse of commodity prices poses significant challenges to the authorities' capacity to deliver on the objectives laid out in the Patriotic Agenda 2025, while maintaining debt and external sustainability. These objectives include eradication of extreme poverty, better access to health and education, and state-led industrialization.

Outlook and risks. Real GDP growth is projected to stay relatively strong at 4.1 percent in 2015, supported by twin deficits, and expected to decelerate to 3.5 percent over the medium term given the new commodity price normal and lingering impediments to private investment. Risks are titled to the downside. Key external risks include a sharp slowdown in key trading partners, additional softness in oil prices, and further dollar strength. Bolivia-specific risks center on uncertainties related to natural gas reserves and long-term export contracts, and excessively large credit cycles under the new financial services law.

Policy recommendations. With the end of the commodity boom, a rethink of policies to anchor strong and durable growth is needed. Two overarching imperatives are to improve the non-hydrocarbons primary balance and allow greater exchange rate flexibility. Given large buffers, the authorities can take a measured approach to meeting these objectives. It will also be important to: adopt a credible medium-term fiscal framework, strengthen the monetary policy framework to uphold the central bank's operational independence and credibility, clarify commodity-related investment regimes, and improve the business climate. Regarding the financial sector, key provisions of the regulations—the credit quotas and interest rate caps—may need to be modified if material risks build up.

Approved By
Krishna Srinivasan and Bob Traa

Discussions took place in La Paz and Santa Cruz during September 2–15, 2015. The team comprised R. Balakrishnan (Head), A. Guerson, D. Heng, S. Ogawa (all WHD), and M. Vargas (RES). F. Bornhorst (Resident Representative) and S. Cardenas (local office) assisted the mission, and E. Tawfik provided research assistance at headquarters. K. Srinivasan (Deputy Director, WHD) joined the concluding meetings and V. de la Barra (OED) participated in the discussions. The team met with private sector participants; think-tanks; academics; donors; senior central government, state, and public enterprise officials; and Presidents of Congress and Senate.

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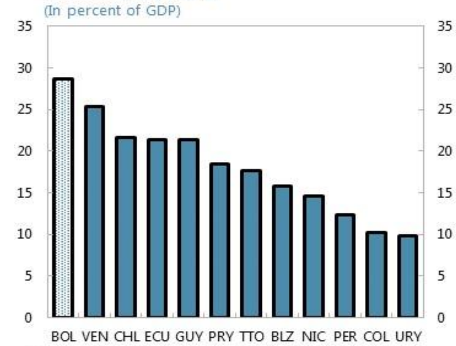
ANNEXES

CONTEXT AND RECENT DEVELOPMENTS

1. After a decade of admirable macroeconomic performance and poverty reduction, Bolivia's policies are being challenged by the end of the commodity boom. Facilitated by prudent macroeconomic management, in the context of a commodity boom, Bolivia has registered average annual real GDP growth of about 5 percent since 2006, when President Evo Morales and his party (Movimiento al Socialismo—MAS) took power. The poverty ratio has also declined by 16 percentage points. However, given Bolivia's large dependence on commodities (among the highest in the region, text chart), the end of the commodity boom poses significant challenges.[1] The key one will be to deliver on the government's policy objectives laid out in the Patriotic Agenda 2025—including eradication of extreme poverty, better access to health and education, and state-controlled industrialization—while maintaining debt and external sustainability.

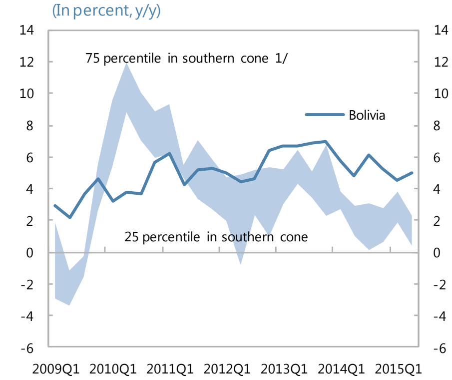
Commodity Exports 1/
(In percent of GDP)



Sources: UN Comtrade; Gruss (2014); IMF, World Economic Outlook; and IMF staff calculations.
1/ Average ratios to GDP for 2010-12. Excludes precious metals and re-exports. Venezuela data refer to net oil exports.

2. Although President Morales has a strong mandate, a referendum on his ability to be reelected is looming on the horizon. President Morales was sworn in for a third term in January 2015 with a two-thirds majority in both houses of Congress. A national referendum on a constitutional change allowing him to run for the Presidency again is slated for February 2016.

Real GDP Growth
(In percent, y/y)

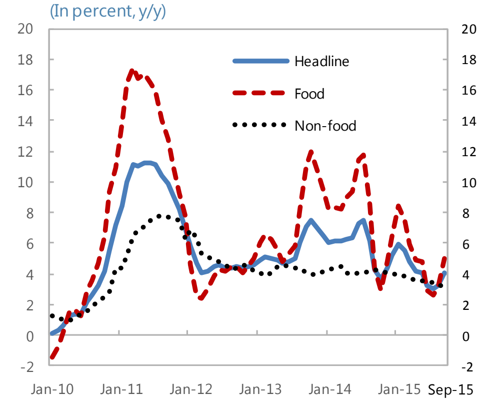


Source: Haver Analytics, Inc.
1/ Includes ARG, BRA, CHL PER, PRY and URY.

3. The expansion continued in the 1st half of 2015 but imbalances are developing given lower commodity prices:

- *Real GDP growth has remained robust and high relative to the rest of Latin America.* Economic activity decelerated but remained strong at 5.5 percent in 2014 (chart). The momentum was maintained in 2015, with a growth rate of 4.8 percent through Q2. There are some recent signs of deceleration, however, with economic activity indicators growing only 2.4 percent and 3.9 percent in July and August, respectively (Figure 1).

CPI Inflation
(In percent, y/y)



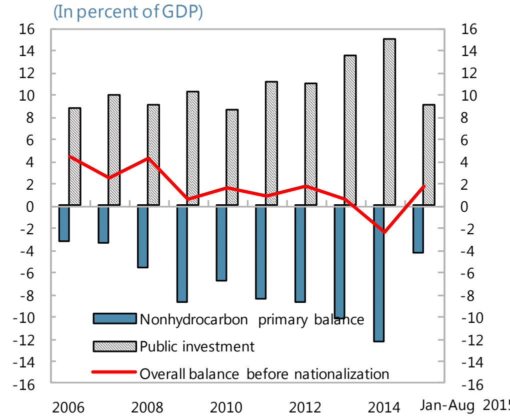
Source: IMF staff calculations based on national authorities' data.

[1] The recent drop in commodity terms of trade is estimated to have resulted in about 7 percentage points of GDP loss for Bolivia. See Regional Economic Outlook: Western Hemisphere (October 2015), chapter 2 for more detail.

- *Inflationary pressures have subsided.* Abstracting from seasonal patterns, monetary conditions started to loosen in the 1st half of 2014 as liquidity declined and the inflation rate fell (Figure 2). By September 2015, inflation had declined to 4.1 percent y/y, in part also helped by declines in import prices given the relative strengthening of the Boliviano against the neighboring currencies (chart, Box 1).

- *The fiscal balance has swung into deficit and the non-hydrocarbons balance continues to worsen*. The fiscal deficit of 3.4 percent of GDP in 2014 partially reflected record-high capital expenditure coinciding with general elections that year and regional elections in March 2015 (Figure 3). The non-hydrocarbons primary balance has also deteriorated by 9.1 percentage points of GDP since 2006 (to -12.3 percent of GDP in 2014) as the hydrocarbons revenue bonanza led to a major ramp up of public spending (chart). So far in 2015, the fiscal balance has stayed in surplus (1.8 percent of GDP through August), similar to the situation in 2014. The increase in tax collections, especially of corporate income tax, has offset the decline in hydrocarbon-related revenues.

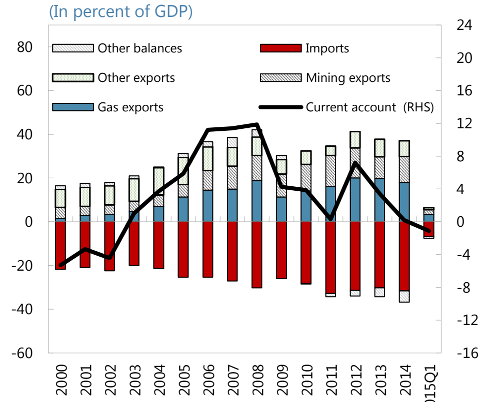
Fiscal Balance and Public Investment
(In percent of GDP)



Source: IMF staff calculations based on national authorities' data.

- *The current account balance has worsened substantially*. Having been in significant surplus since 2003, the current account surplus declined to 0.2 percent of GDP in 2014 and slipped into a deficit of 1.4 percent of GDP in 2015Q1 (chart). Lower international oil prices started to feed into gas export prices in the 1st half of 2015 (export prices were down 34.2 percent y/y), while real import growth remained robust given the continued economic expansion and real currency appreciation.

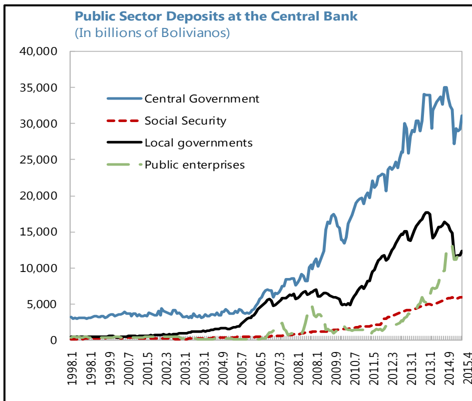
Current Account
(In percent of GDP)

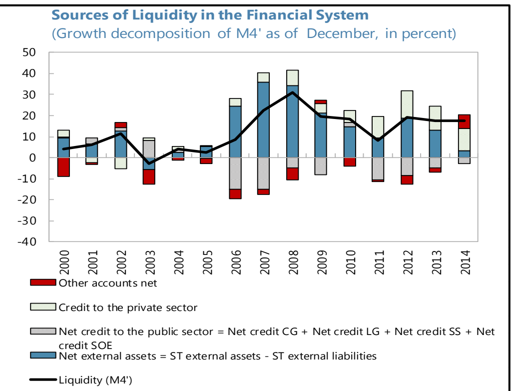


Source: Central Bank of Bolivia.

Box 1. Monetary Policy and Inflation in Bolivia[1/]

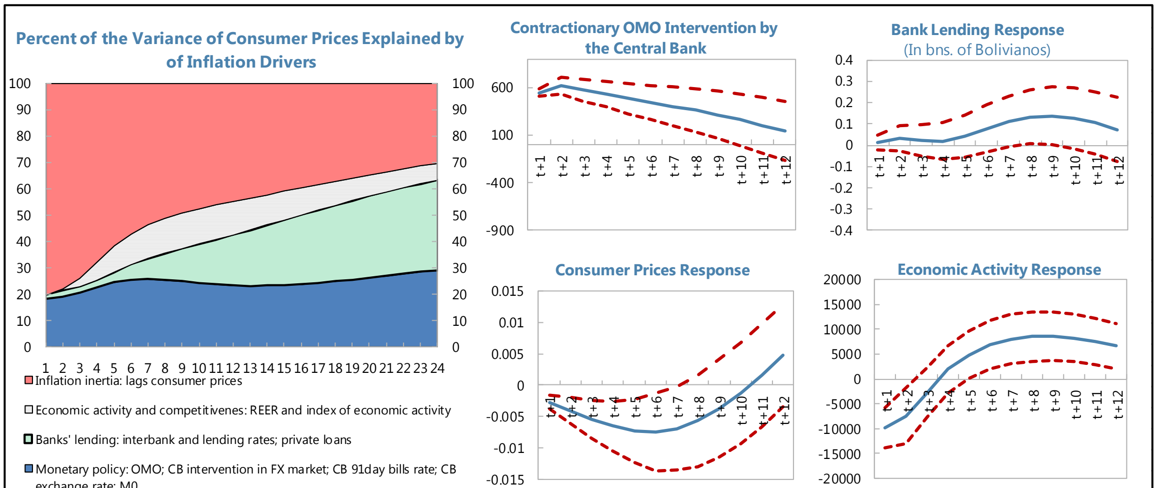
Inflation has remained low and stable in the last few years, anchored by a stable exchange rate and central bank intervention in money markets to control the level of liquidity. Open market operations (OMOs) are the main operational instrument. The central bank monitors the growth rate of monetary aggregates; mainly net domestic credit of the central bank and excess reserves of the banking sector. It also intervenes in the foreign exchange market through daily auctions at a set U.S. dollar exchange rate, within a narrow buy-sell spread band. This exchange rate at the central bank window has remained virtually unchanged since 2008, with a de-facto stabilized regime since 2011. Central bank policies have so far been effective in managing inflation, especially given ample liquidity related to the significant increase in public investment spending. This is associated with the nationalization of hydrocarbons in 2006 and the subsequent boom in oil prices.





Source: Central Bank of Bolivia and staff calculations.

Staff estimates indicate that the central bank has been able to control about 30 percent of consumer inflation variability with timely monetary policy reactions affecting money markets and bank lending activities. These estimates are based on an empirical model including (a) the central bank's monetary policy instruments; (b) the exchange rate and base money as long-term nominal anchors; (c) the interbank interest rate and banks lending rate and credit as monetary policy transmission channels; and (d) consumer and core prices, the economic activity index and the real effective exchange rate as ultimate indicators of the effects on the real economy.

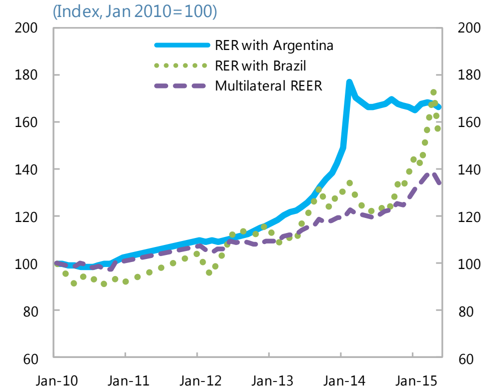


Source: Central Bank of Bolivia and staff calculations.

[1/] Prepared by A. Guerson. See "Inflation Dynamics and Monetary Policy in Bolivia," IMF Working Paper (forthcoming).

4. The Boliviano is assessed to be stronger than warranted by medium-term fundamentals and desirable policies in 2015 (Annex I). The de-facto stabilized exchange rate against the dollar combined with significant dollar appreciation—especially against the Brazilian real and the Argentine peso—has led to an appreciation of more than 40 percent in real effective terms since 2010. Competitiveness has also deteriorated, on the back of sizable minimum and average wage increases (the former nearly fourfold in the last decade), which have been significantly above productivity growth, and scarce investments in non-traditional export sectors. International reserves are more than adequate by any metric at US$14.2 billion (42 percent of GDP) as of September 2015, although they have fallen by nearly US$0.9 billion since end-2014.

Real Exchange Rates
(Index, Jan 2010=100)

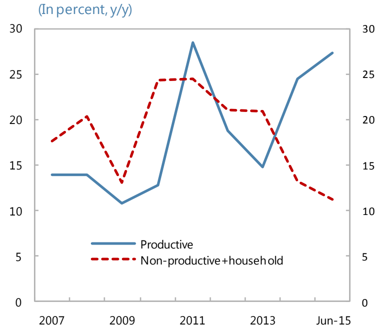


Source: Central Bank of Bolivia.

5. Headline financial indicators are solid, although vulnerabilities are beginning to develop and likely to increase as growth slows and lower oil prices bite (Annex II). Banks' overall capital adequacy ratio stood at 12.7 percent in June 2015, with all major banks above the regulatory minimum of 10 percent, and the aggregate leverage ratio is around 8 percent. Profitability continues to decline, although it remains adequate with the return-on-equity at 13.8 percent as of June 2015. NPLs remain among the lowest in the region (around two percent). Dollarization of deposits continues to decrease, standing at about 20 percent as of August. However, while credit growth to the private sector has moderated somewhat to around 15 percent (y/y), the credit-to-GDP ratio has picked up considerably. It stood at above 45 percent of GDP in June 2015, 3½ percentage points more than a year ago and suggestive of potential vulnerabilities on the rise.

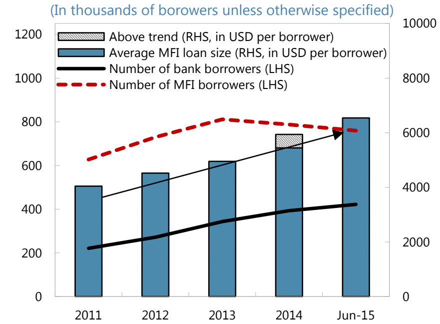
6. The Financial Services Law appears to be altering the allocation of credit flows, and could pose risks to financial stability and inclusion (Box 2). For 2015, the minimum credit quotas to productive and social housing sectors are being met by most financial institutions. Meeting the quotas, however, has required a sharp acceleration of loans to the productive sector and for social housing (growth of 26 percent since December 2014), and a reduction in credit growth to the service and commerce sectors (chart). The interest rate caps seem to be having a material effect on microfinance institutions, which have increased loan sizes above trend to reduce operational costs while the number of borrowers has declined (chart).

Credit Growth
(In percent, y/y)



Source: Financial System Supervisory Authority (ASFI).

Number of Borrowers and Loan Size
(In thousands of borowers unless otherwise specified)



Source: Financial System Supervisory Authority (ASFI).

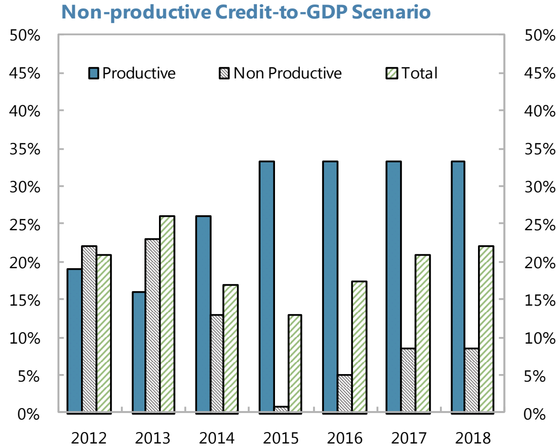
Box 2. The Impact of the Financial Services Law[1/]

The Financial Services Law aims to promote financial inclusion, preserve financial stability, and enhance credit to housing and productive sectors. Productive sectors are defined broadly as non-service sectors, including agriculture, mining, and manufacturing. Supreme Decrees issued in 2013 and 2014 set the floor on deposits rates and ceilings on lending rates for social housing (5.5–6.5 percent), for corporate and SME loans to productive sectors (6–7 percent), and microfinance loans (11.5 percent). Full service banks are also required to direct at least 60 percent (50 percent for SME banks) of their loan portfolios to social housing and productive sectors within five years, guided by intermediate annual targets. Guarantee funds were created from a 6 percent tax on banks' 2014 profits to finance down payments for productive sector and social housing loans.

Looking ahead, achieving the 60/40 target by 2018 could imply rapid credit growth, raising concerns about concentration risks, compromised asset quality, and over-indebtedness in the productive sector. If the share of non-productive sector credit to GDP were to remain constant, total credit growth needs to be around 18 percent with productive sector credit growth (including for social housing) of 33 percent ("Non-productive Credit-to-GDP Scenario"). If credit growth for non-productive sectors continues at the rates seen in 2014, the 60/40 target by 2018 implies annual overall credit growth of about 25 percent and productive sector credit growth of 42 percent ("Credit Growth Trend Scenario"). In each scenario, the credit to GDP gap, a measure of whether credit growth is excessive or not, is high, indicating the buildup of financial stability risks. An alternative scenario would be to meet the credit quotas by balance sheet reduction, implying a credit crunch in the non-productive sector as banks reduce lending to it.

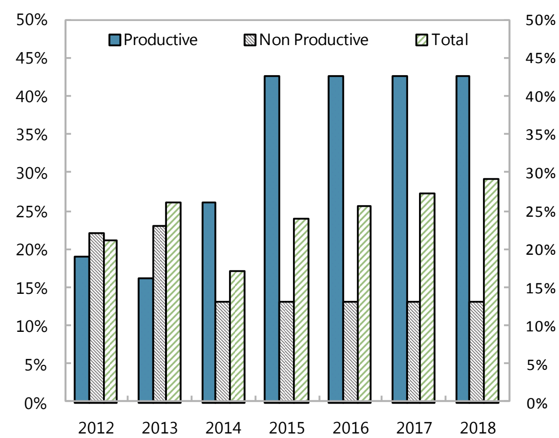
A July 2015 modification to expand the scope of the "productive sector" helps address the credit growth pressure but may lead to other risks. This change allows the inclusion of the tourism sector and intellectual property. The risks, however, could simply be shifted to loan quality and the supervisory burden given increasing complexity and scope for circumvention.

Non-productive Credit-to-GDP Scenario



Source: IMF staff calculations based on national authorities' data.

Credit Growth Trend Scenario



Source: IMF staff calculations based on national authorities' data.

1/ Prepared by D. Heng. See "Impact of the New Financial Services Law in Bolivia on Financial Stability and Inclusion" IMF Working Paper (forthcoming).

7. The authorities are finalizing a 5-year development plan (*Plan Quinquenal*) centered on sizable public investments playing a catalytic role in the growth process. These will be in a vast number of areas, including public infrastructure, productive activities, health, education, and technology. Key commodity related projects cover discovery/exploration of gas and oil reserves, petro-chemical plants, thermo- and hydro- electricity plants, and large iron ore and lithium mines. While details are still being finalized, fiscal and external deficits will likely persist under the plan, with a sizable share of external financing expected.

8. Policies implemented in recent years have been partially in line with previous Fund advice (Table 2). Pro-cyclical fiscal stimulus has been avoided, and the authorities have taken some important steps towards adopting a medium-term fiscal framework. Inflation pressures have also been contained and there have been significant increases in public infrastructure spending. Recommendations to improve the non-hydrocarbons fiscal balance, discontinue central bank lending to public enterprises, and gradually allow greater exchange rate flexibility have gained less traction.

OUTLOOK AND RISKS

9. Against the background of a sober global outlook and a new commodity price normal, economic momentum in 2015 is being maintained at the cost of twin deficits. Given the lags in the adjustment of gas prices in the export contracts to Brazil and Argentina, the full impact of the oil price decline on gas exports and hydrocarbon revenues will be felt in the second half of 2015. Nonetheless, with a sizable public investment budget, strong credit growth to the private sector (13 percent y/y), and robust private consumption, growth is projected at 4.1 percent in 2015—relatively high for the region but still below the authorities' forecast of around 5 percent. Fiscal and current account balances are expected to deteriorate significantly, registering deficits of 5.3 and 4.5 percent of GDP respectively.

10. The outlook for Bolivia is increasingly challenging in the medium term. In the staff baseline, which assumes significant public investment and credit growth (average annual growth of around 10 percent y/y), GDP growth is forecast to remain robust at about 3.5 percent in 2016 and beyond.[2] This is in line with potential growth, which has been revised down from 5 percent to 3½ percent, reflecting the lower commodity price normal and a reassessment of prospects for private investment and total factor productivity (TFP) growth.[3] Given oil prices are currently forecast

[2] The credit growth assumption is consistent with financial institutions trying to meet the credit quotas under the financial services law in part by allowing the ratio of nonproductive credit to GDP to gradually decline.

[3] One-third of the downgrade is because of lower private and public investment, but there has also been a more general reassessment of TFP growth. This is consistent with the findings of the October 2015 *World Economic Outlook* on the impact of commodity price cycles on growth and potential growth, which points out that commodity booms can raise TFP through faster adoption of technology and higher spending on research and development. The *Bolivia Selected Issues Paper* (2013) also suggests that the estimated strong TFP growth since 2006 could reflect the

(continued)

to recover only moderately over the medium term, the fiscal and external accounts are projected to remain in significant deficits, leading to a drawdown of international reserves, although they should remain adequate (14 percent of GDP and 6 months of imports in 2020). Financing the fiscal deficits will also likely involve recourse to existing public sector deposits and direct lending from the central bank.

11. In line with the global context, risks for Bolivia are tilted to the downside. These include: (i) a sharper slowdown in Brazil; (ii) further dollar appreciation, which would exacerbate the overvaluation of the Boliviano given the de-facto stabilized exchange rate against the dollar; (iii) U.S. interest rate normalization, which may lead to rising NPLs given many bank loans are indexed to a variable reference interest rate;[4] (iv) the combination of credit quotas and interest rate caps under the Financial Services Law leading to a credit crunch in the nonproductive sectors and/or excessive credit growth in the productive sector and for social housing; and (v) additional softness in energy prices over the medium-term. There could also be a perfect storm where Bolivia's large buffers disappear steadily if a failure to discover and explore significant new hydrocarbons reserves and/or renew the Brazil gas contract in 2019 is combined with a weakening of the fiscal position and an undermining of central bank credibility.

12. There are, however, important upside risks. A quicker and larger than expected recovery in international oil prices would improve the fiscal and external accounts, and could result in greater foreign investment to discover new hydrocarbons reserves if combined with a more attractive investment regime. Various commodity-related projects could also pay off more than expected in the staff baseline. And the ramp up in infrastructure spending could have a significant impact on potential growth if used efficiently.

impact of the commodity price boom on the hydrocarbon sector that is not captured fully in the stock of physical and human capital. Moreover, estimated TFP growth in the 25 years before 2006 was much lower than subsequently.

[4] The 2011 FSAP stress testing exercise didn't have sufficient data to carry out an interest rate risk stress test. It did argue, however, that duration mismatch was not likely to be a problem given both assets and liabilities are mostly of short duration. Any rise in interest rates may also be somewhat mitigated given limited external funding to the banking sector.

Table 1. Bolivia: Risk Assessment Matrix[1/]

Source of Risks	Likelihood	Expected Impact	Policy Responses
External risks			
A sharper slowdown in Brazil	High	M/H (↓) Brazil accounts for about ⅓ of Bolivia's exports. While a growth slowdown may not reduce short-term demand for natural gas, it could still impact activity via other trade and non-trade channels.	Accommodative macro policies, including fiscal stimulus within the available policy space, accommodative monetary policy, and exchange rate flexibility.
Persistent dollar strength	High	L/M (↓) Further dollar appreciation would exacerbate the overvaluation of the boliviano, impeding diversification away from commodity sectors.	Exchange rate flexibility and improving business climate will help absorb terms-of-trade shocks and enhance competitiveness.
U.S. interest rate normalization	High	L/M (↓) Many bank loans are indexed to a variable reference interest rate (TRE) and a sharp increase in interest rates could lead to a rise in NPLs. It could also negatively impact future international placements of sovereign bonds.	Vigilant financial sector supervision and regulation. Enhancing policy credibility and improving the business climate will help maintain sovereign access to international financial markets.
Persistently low energy prices	Medium	H (↓) Prices lower than current baseline would further weaken the fiscal and external accounts, and reduce already low incentives of foreign energy companies to invest in the exploration of new oil and gas reserves.	Exchange rate flexibility and gradual fiscal adjustments. Large international reserves provide some buffer. While the industrialization of natural gas helps increase value-added, further diversification beyond natural resource sector will be beneficial.
Country-specific risks			
Financial Services Law	Medium	L/M (↓) The combination of credit quotas and interest rate caps could lead to a credit crunch, and could start a vicious negative feedback loop between credit and growth. Alternatively, there could be excessive credit growth to the productive sector and for social housing, leading to a spike in NPLs and bank capital impairment with a lag.	Modifying key provisions of the norm via decrees if material risks build up. Greater financial inclusion could also be achieved by relying primarily on market-based signals, such as partial credit guarantees.
Failure to discover significant new hydrocarbons reserves and/or to renew the Brazil gas contract	Low/Medium	M/H (↓) Doubts remain regarding how successful efforts to discover/explore gas reserves will be. Negotiations to renew the Brazil contract, which will start soon, will depend on the energy supply situation in Brazil and the guarantees Bolivia can give regarding production capacity beyond the mid-2020s.	Finalize legal reforms to the hydrocarbon sector and clarify the incentives for investment to encourage exploration activities. It is critical to press ahead with negotiations with Brazil before current long-term contract expires in 2019.
Delay in policy adjustments	Medium	M/H (↓) Delays in policy adjustments could exhaust external and debt buffers that currently exist.	Improving non-hydrocarbon fiscal balances is critical in maintaining fiscal and debt sustainability.

[1/] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively.

POLICY RECOMMENDATIONS

Changes to the global outlook and the lower commodity price normal necessitate a rethink of policies to anchor strong and durable growth. Two overarching imperatives are to improve the non-hydrocarbons primary balance and allow more exchange rate flexibility. Given large buffers, the authorities can take a measured approach to meeting these objectives. Many of the recommendations of previous Article IV Consultations remain valid (Table 2).

A. Anchoring Fiscal Sustainability and Strengthening the Fiscal Framework

13. An incomplete adjustment to the new commodity price normal would raise concerns about Bolivia's debt sustainability. Preserving fiscal sustainability is critical for the achievement of the governments' development objectives. Under a passive scenario of no policy change and assuming public investment to GDP remains at 2014 levels, the overall fiscal deficit could widen to about 10 percent of GDP and public debt could reach 70 percent of GDP by 2020. This is above the threshold marking a high risk of debt distress for LICs (Annex III).[5]

14. Improving the non-hydrocarbons fiscal balance is essential, but a gradual approach can be taken given large buffers and development needs. The non-hydrocarbons primary deficit has widened from 3.2 percent of GDP in 2006 to a whopping 12.3 percent of GDP in 2014 (text table). In addition to the short horizon of Bolivia's current proven gas reserves, lower international oil prices and uncertainties related to the long-term export contract with Brazil add to the urgency for improving the non-hydrocarbons primary balance. Nonetheless, given Bolivia's low level of net public debt and the need to improve infrastructure and further reduce poverty, the authorities can pursue a calibrated approach and adjust the path to respond to future shocks as needed.[6]

Bolivia: Fiscal Balances and Public Debt

	2014	2015	2016	2017	2018	2019	2020
		Projections					
	(in percent of GDP)						
Baseline scenario							
Overall balance	-3.4	-5.3	-5.8	-5.5	-5.1	-4.6	-4.3
Non-hydrocarbon primary balance	-12.3	-10.1	-8.7	-8.5	-8.3	-8.0	-7.8
Public debt	33.0	38.0	42.0	44.1	45.8	46.8	47.6
Active scenario							
Overall balance	-3.4	-5.2	-5.3	-3.1	-1.4	-0.1	1.3
Non-hydrocarbon primary balance	-12.3	-10.1	-8.2	-6.2	-4.6	-3.5	-2.2
Public debt	33.0	38.0	41.5	41.3	39.5	36.6	32.5

Sources: Ministry of Economy and Public Finances and staff projections.

15. The baseline projection builds on a moderate consolidation of the non-hydrocarbons primary deficit over the medium term. In 2015, the consolidation is based on a capital budget execution rate of around 80 percent, consistent with outturns in years before 2014 (an election year).

[5] Under the baseline scenario, Bolivia shows low risk of debt distress for total and external public debt.

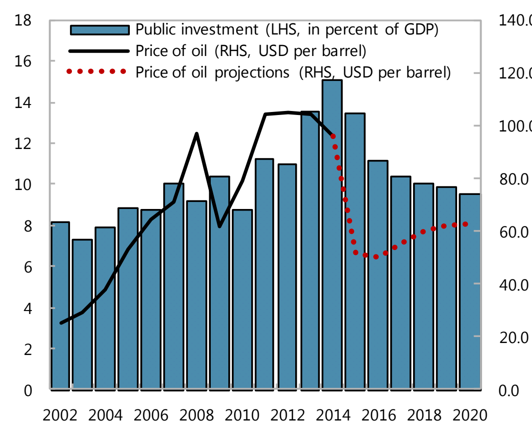
[6] The 2016 Budget is expected to be presented to Congress in November.

Thereafter, public investment continues to decline and stabilizes at around 9¼ percent of GDP by 2020. This reflects capacity constraints, more conservative expectations regarding official financing, and lower hydrocarbons revenues. The non-hydrocarbons primary deficit shrinks by 4½ percent of GDP to 7.8 percent of GDP in 2020, with public debt stabilizing at around 50 percent of GDP.

16. Staff, however, recommends a more ambitious consolidation to build fiscal buffers. The baseline scenario projects a relatively high level of debt in the medium term for a low income country like Bolivia. An active policy scenario targets a more ambitious but still gradual reduction of the non-hydrocarbons primary deficit to 2.2 percent of GDP by 2020, with debt declining to 32½ percent of GDP. If credibly implemented, automatic stabilizers could be allowed some play around this path. Measures to adjust the non-hydrocarbons primary balance by an additional 5½ percent of GDP could include:

- ***Revenue***. Introducing a progressive personal income tax (PIT) or reforming RC-IVA (the complementary VAT regime), as well as establishing rules to deal with transfer pricing practices and preparing the tax administration to control them. A fully fledged PIT could bring additional revenue of around 1 percent of GDP and improve the equity and efficiency of the tax system, in addition to rendering the tax system more progressive. While it may have a negative revenue impact in the short term, ensuring transparent and incentive compatible hydrocarbons and mining fiscal regimes is essential to discovering new reserves/deposits and generating commodity-related revenues in the longer term.

Price of Oil and Public Investment



Source: IMF Global Assumptions (GAS) and staff calculations based on authorities' data.

- ***Expenditure***. Public investment has scope to decline further and still remain above the average level in 2006–12 (chart). Prioritization should be based on economy-wide returns, with a focus on the quality of investment. Reducing energy subsidies could yield over 1 percent of GDP. There is also scope to reduce the wage bill, which is high by low-income country standards, and rationalize goods and services expenditures to pre-2014 levels.

17. Staff reiterates the importance of introducing a medium-term fiscal framework. The Ministry of Finance has taken some welcome steps in this regard, including creating a Macro-Fiscal unit that produces fiscal projections, enhancing coordination with the Central Bank regarding the overall macroeconomic framework, and instructing public enterprises to prepare multi-annual budgets during the formulation of the 2015 Budget.[7] These steps should be built on to implement a fully fledged medium-term fiscal framework. Key aspects of this are a multi-year budget and setting

[7] Bolivia received an IMF technical assistance mission on implementation of a medium-term fiscal framework in October 2014.

a fiscal target for the non-hydrocarbons primary balance that is consistent with long-term debt sustainability, taking into account the state of the business cycle and oil price volatility.

18. State-owned enterprises and their quasi-fiscal activities pose additional fiscal risks, requiring a credible monitoring framework to assess their financial health. (Annex IV. I.) There exist some important quasi-fiscal activities conducted through subsidiaries of strategic public enterprises which are currently classified as outside the Non-Financial Public Sector (NFPS). In addition, the Plan Quinquenal will likely have further significant investments in manufacturing activities and the creation of more SOEs. To manage these contingent risks, the authorities should start monitoring and publishing SOEs' financial operations and balance sheets as a first step to including them in the fiscal accounts of the NFPS. More broadly, the legal requirement that SOEs should "generate surpluses", or otherwise be subject to closure, should make sure that surpluses more than offset capital depreciation.

B. Improving Exchange Rate and Monetary Policies

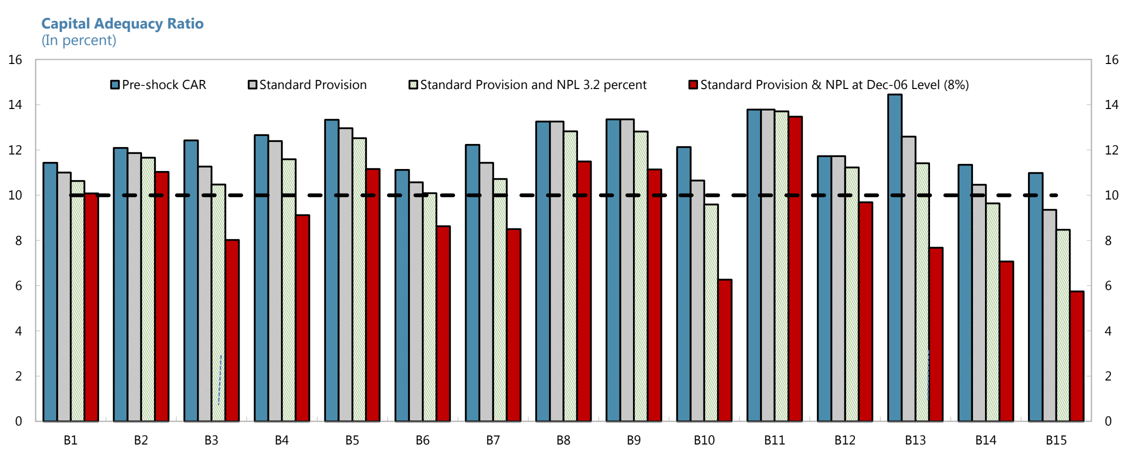
19. Creating conditions for greater exchange rate flexibility is critical. This would help facilitate adjustment to the large terms of trade shock and to future external shocks. And it is especially important given the assessed overvaluation of the Boliviano and potential for further dollar appreciation. In staff's view, the tremendous progress in de-dollarizing the economy is one important pre-condition for an orderly transition to a more flexible exchange rate regime. Country experiences also suggest that cementing de-dollarization usually requires migration to an exchange rate regime that allows for two-way flexibility. This helps internalize exchange rate risks and reduce incentives for dollarization (Annex IV. II.). Any transition would need to be carefully crafted, however, including credibly anchoring inflation expectations and ensuring that the appropriate monetary policy instruments and money markets' infrastructure are in place.

20. An effective monetary policy framework which anchors inflation expectations will require central bank credibility and fiscal sustainability. The new central bank law under preparation should maintain the bank's operational independence and preserve its capital base. To this end, the practice of direct lending by the central bank to public corporations or trust funds for development objectives should be discontinued. The direct lending, started in 2009, has expanded to US$2.9 billion (equivalent to 8.4 percent of GDP) as of mid-2015, of which about 60 percent are directed to YPFB (the state oil and gas company). In addition, the "Fondo para la Revolución Industrial Productiva (FINPRO)" was established in 2012, with lending and grants from the central bank totaling US$1.2 billion. Staff recommends that lending activities are stripped from the central bank balance sheet and consolidated in a separate fund for development. This fund would need transparent investment rules, a strong governance structure, and a clearly-stated development mandate. This separation would contribute to enhancing central bank credibility by eliminating the possibility of conflicting objectives: price stability should be clearly stated as the central bank's first priority. An effective monetary policy transmission would also benefit from a revision of the targets in the Financial Services Law that distort interest rates and credit allocation.

C. Ensuring Financial Sector Stability and Enhancing Financial Inclusion

21. The Financial Services Law includes several reforms recommended in the FSAP. The setting up of a deposit insurance scheme and a credit registry are welcome steps, as are the implementation of some Basel II and III principles (such as adding market risk to capital requirements and completing the guidance on operational and interest rate risk). The creation of a Financial Stability Council—which met for the first time in August 2015—is another important step. Developing a framework to monitor systemic risks and a macroprudential toolkit will further strengthen financial sector surveillance. The recent advances in AML/CFT are expected to culminate in the publication of a national strategy in late 2015.

22. The Law, however, could pose risks to financial stability and reduce financial inclusion. While meeting the 2015 credit quotas appears manageable, trying to reach the medium-term targets could lead to excessive credit growth in productive sectors (including social housing) and/or a credit crunch in nonproductive sectors. And staff VAR analysis suggests that credit dynamics have a significant impact on growth, with a 1 p.p. increase in real credit growth raising GDP growth by 0.2 p.p. the following year. Overall, scenario analysis points to credit growth rates potentially in excess of 30 percent for the productive sectors to meet the 5-year credit quotas (Box 2). This could lead to deterioration in asset quality and rising NPLs. Stress tests suggest a doubling of NPLs is manageable for most banks but a spike to peak levels reached over the last decade would cause many banks to be significantly below regulatory capital thresholds (chart).[8] The above-trend increase in the average loan size of microfinance institutions and the declining number of borrowers point to adverse effects of the interest rate caps on financial inclusion. This may also result in increased activity of unregulated lenders as they attract the non-productive sectors and small borrowers no longer serviced by microfinance institutions.



Source: IMF staff calculations based on national authorities' data.

[8] The stress tests also adjust provisioning levels to international standards given that the 2011 FSSA highlighted this as an important issue (the "standard provision" test). For the higher NPL test, the increase in NPLs is provisioned at 50 percent, which is reflected fully in risk-weighted assets and capital.

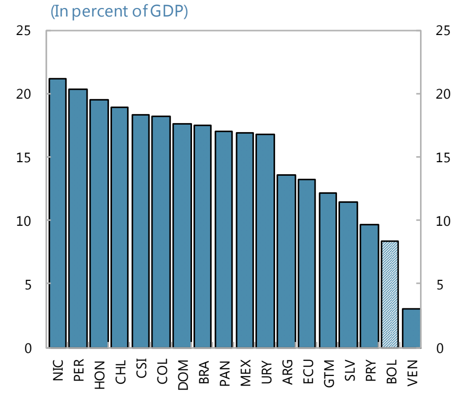
23. Key provisions of the regulations should be modified if material risks build up, and greater financial inclusion could be achieved by relying primarily on market-based signals. The interest rate caps and credit quotas were set by decrees and hence can also be modified as needed, although clear and transparent rules regarding changes are critical to avoid creating regulatory uncertainty. Indeed, the recent expansion of the definition of productive sectors likely increases the scope for circumvention of the quotas, effectively watering them down but also increasing the supervisory burden to police them effectively. Staff strongly recommends the creation of a real estate price index to have a better idea of risks building up in the real estate sector. This is especially important given the inclusion of social housing in the credit quotas and the associated lack of need for a down payment. Staff also reiterates that financial inclusion could be better attained by more limited and carefully-designed state intervention, such as further use of partial credit guarantees.

D. Increasing Potential Growth and Inclusiveness

24. Increasing private investment is central to medium-term prospects. The share of private investment to GDP has long been one of the lowest in the region, and is currently around 8 percent (chart). Bolivia also ranks among the lowest in Latin America and the Caribbean in terms of economic diversification and complexity.[9] Indeed, raising Bolivia's complexity score—reflecting how knowledge intensive or sophisticated its exports are—to the average in Latin America and the Caribbean would increase growth by about 0.4 p.p. (chart). Addressing the key impediments listed below will be essential to ensuring the complementarity between public and private investment, and enhancing diversification (Annex IV. III.).

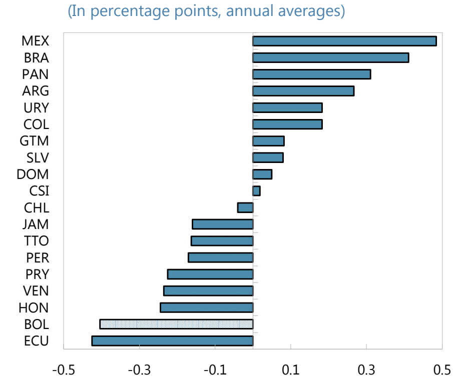
- *Regulatory uncertainty*. There has been important progress in adapting the legal framework to the new Constitution (including the Investment Promotion Law in April 2014, the Mining Law in May 2014, and the Arbitration Law in June 2015). Some of these laws, however, do not fully resolve regulatory uncertainty. For example, the Arbitration Law exempts many key sectors, while the right of the Bolivian state to ultimately accept or reject the verdicts of external tribunals could weaken the purpose of the law. More generally, important aspects of the legal framework are left to decrees, many of which are still pending or can be modified. Finally, a few key laws are still pending, such as the

Private Investment, 2014
(In percent of GDP)



Source: IMF World Economic Outlook. (WEO).

Net Impact on Predicted GDP per Capita Growth Rates: Own Complexity Versus LAC Average Complexity
(In percentage points, annual averages)



Source: Rodrigues Bastos and Wang (2015).

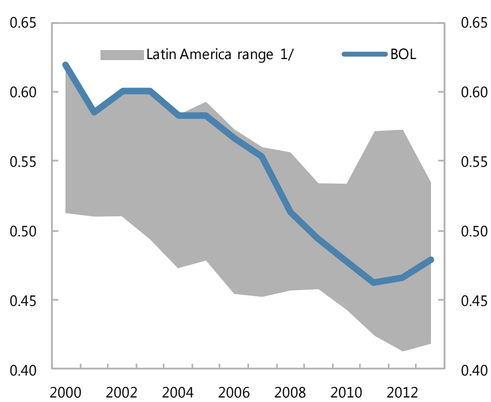
9 See IMF (2015), "Long-Run Growth in Latin America and the Caribbean: The Role of Economic Diversification and Complexity", Regional Economic Outlook: Western Hemisphere (April 2015) for more detail.

hydrocarbons and labor laws, a new tax code, and sectoral incentive laws. This creates uncertainty.

- *Other impediments*. Competitiveness is being further crimped by high real wage growth and other mandated bonuses, which have led to real income growth exceeding productivity growth. Meanwhile, labor market inflexibility and pervasive informality continue to undermine productivity and SME financial access. Importantly, the government's increasing incursion into product markets through price controls and public enterprises crowds out private investment, given that public enterprises are less bound by competitive forces and efficiency levels needed in the private sector.

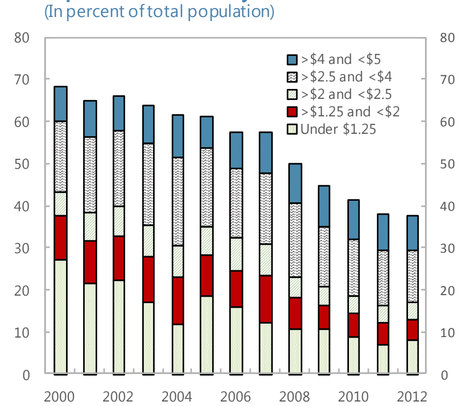
25. Bolivia has registered some of the largest declines in inequality and poverty in the region over the last decade, but further progress will be challenged by the end of the commodity boom (charts). Social transfers to the elderly, pregnant and school kids benefit about 30 percent of population, and have helped improve primary schooling, maternal health, and reduce extreme poverty especially in rural areas. However, most of the reduction in poverty and inequality is explained by declining wage inequality as the skills premium has fallen, and not larger transfers (Box 3). Importantly, labor market policies have played a role through sustained minimum wage increases and salary caps in the public sector. The skills premium could well increase as the spillovers to low skill workers from the commodity boom go into reverse. Given a tighter revenue envelope, it is essential to ensure that the social transfers are well designed and targeted and there is a focus on the quality of education and healthcare.

Gini Inequality Index



Source: SEDLAC (CEDLAS and The World Bank)
1/ Includes ARG, BRA, ECU, SLV, HON, MEX, PRY, PER and URY.

Population Under Poverty Lines 1/
(In percent of total population)



Source: World Bank Development Indicators (WDI).
1/ 2005 Purchasing Power Parity USD.

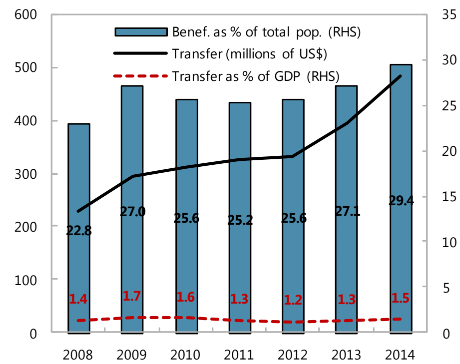
Box 3. Inequality and Poverty Reduction[1/]

The tremendous inequality and poverty reduction in Bolivia over the last decade has a few potential explanations: i) changes in the levels of average labor income, which are explained by sustained economic growth fueled by favorable terms of trade and high levels of public investment; and ii) changes in the distribution of total income, which in turn respond to changes in the skills premium, transfers and social programs, and specific labor market policies such as the sustained increase in the real minimum wage.

Targeted public policies have played an important role. Redistributive policies hinged on transfers to specific population groups: school age kids (Bono Juancito Pinto), elderly people (Renta Dignidad) and pregnant women and newborns (Bono Juana Azurduy). Together, these three programs benefited just under 30 percent of the total population, and totaled 1.5 percent of GDP in 2014.

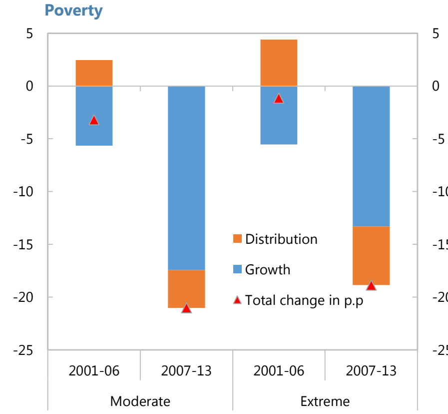
A closer analysis suggests that fast growth was the main driver behind poverty reduction; while a declining skills premium drove down inequality. During 2007–2013, nearly 70 percent of the decline in extreme poverty is explained GDP growth, while the remaining 30 percent is associated with changes in the distribution of income. Moreover, real labor income increased rapidly for low skilled workers, while it declined for high skilled workers (this was something also seen in Ecuador and Peru, although Bolivia had the highest decline for high skilled workers). This declining skills premium was the main factor behind the drop in the Gini coefficient, while the effect of changes in non-labor income (transfers) was limited, notwithstanding an important impact for some groups such as for the elderly poor after the introduction of Renta Dignidad.

Bolivia: Renta Dignidad, Bono Juancito and Bono Juana Azurduy 1/

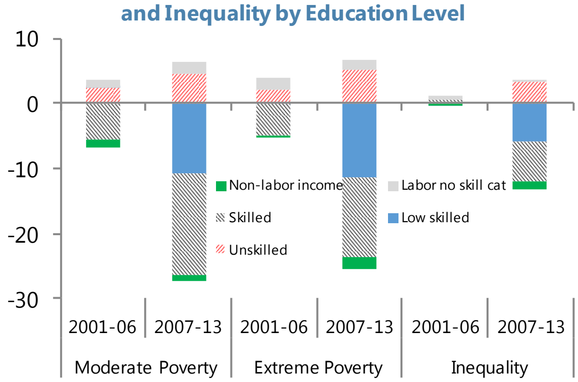


Source: APS Bolivia; IMF staff calculations.
1/ 2015 includes data to May. Number of beneficiaries correspond to the average number of payments.

Datt-Ravallion Decomposition of Changes in Poverty

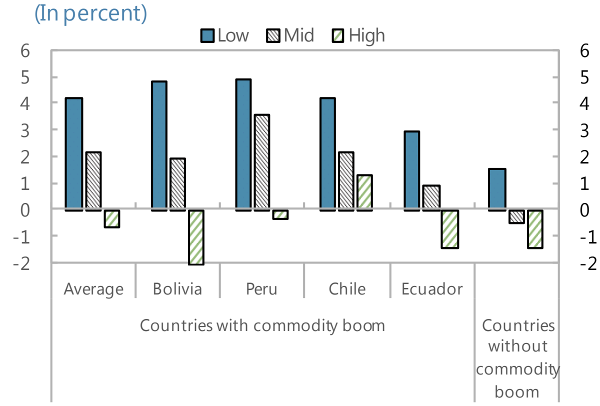


Decomposition of reductions in Poverty and Inequality by Education Level



Source: IMF staff calculations using Bolivia's Household Surveys.
Gini coefficient change based on re-scaled gini coefficients in the range (0-100)

Annualized Real Wage Growth by Education Level
(In percent)



Source: SEDLAC (CEDLAS and the World Bank).

[1/] Prepared by M. Vargas. See "Explaining Inequality and Poverty Reduction in Bolivia," IMF Working Paper (forthcoming).

E. Authorities' Views

26. **The authorities strongly disagreed with staff's growth outlook for the short and medium term, and rejected staff's proposed consolidation of the non-hydrocarbons primary deficit**. They expect growth to be around 5 percent in 2015 and that high public investment in productive sectors will pay off and lead to growth averaging about 5¾ percent during 2015–20, significantly above staff's growth forecasts for 2015 and beyond. They also forecast a fiscal deficit of about 4 percent of GDP in 2015. They indicated, however, that the deficit target would be lower for 2016. The authorities did not see the need for cutting back on public investment as they believe that revenues—both non-hydrocarbons and hydrocarbons related—will pick up in the coming years.

27. **The authorities disagreed with the need for greater exchange rate flexibility at this juncture or for operational independence of the central bank**. They argued that greater exchange rate flexibility would not help competitiveness given that export volumes of hydrocarbons and mining sectors are largely supply-determined, and also given the limited response of nontraditional exports to exchange rate dynamics. Moreover, they argued that the majority of imports were capital goods needed for development. The authorities were of the view that central bank independence was not needed in the case of Bolivia, given the existing coordination between the Ministry of Finance and central bank to ensure macroeconomic stability and the political consensus on the importance of a low inflation rate. They indicated that the central bank should play an important development role, and therefore direct lending to public corporations will remain an important financing source for public investment.

28. **The authorities agreed that financial regulations can be adapted as needed, but disagreed about the potentially adverse impact of the credit quotas and interest rate caps**. The authorities argued that banks will achieve the 60 percent share of productive loans to total loans without the risk of excessive credit growth. They explained that the credit quotas have so far proved effective in redirecting flows away from bank profits and towards productive loans, while NPLs remained the lowest in the region. They emphasized that banks remain profitable and that the decreasing number of microfinance borrowers did not reflect reduced financial inclusion, but a reclassification within the financial sector, with some of these borrowers now classified as bank customers. The authorities concurred on the necessity to construct a house price index and to modify the credit quotas and interest rate caps if systemic risks build up.

29. **The authorities agreed on the need to increase private investment going forward, but did not share staff's analysis regarding the impediments** . They emphasized progress made in aligning key laws to the new Constitution, and pointed to the investment projects in the pipeline. In particular, they argued that the Investment Promotion and Arbitration Laws contributed to improving the business environment and effectively modernized the framework governing investment in Bolivia. The authorities expected that foreign private investment will play a greater role in the coming years. They highlighted the recent rapprochement with the domestic private sector. The authorities further rejected the need for labor market reforms, arguing that their labor policies are an important tool for redistribution and have contributed to reducing poverty and inequality. The authorities are convinced of the public sector's catalytic role in increasing the

productive capacity of the economy and facilitating the functioning of markets through direct intervention.

30. The authorities expect to build on the tremendous inequality and poverty reduction registered over the last 15 years. They highlighted the role of Renta Dignidad as an effective redistributive policy, as well as other pro-poor policies such as the large and sustained increase in the minimum wage. They also stressed that while other conditional transfers, such as Bono Juancito Pinto and Bono Juana Azurduy have positive effects on inequality and poverty, their main aim is to improve human capital. The authorities disagreed with the conclusion that the inequality decline partially reflected declining wages for skilled workers given that wages increased across the board.

STAFF APPRAISAL

31. Following a decade of strong macroeconomic performance, poverty reduction, and de-dollarization, the Bolivian economy is at a point of inflexion. Bolivia has recorded strong economic growth and built up significant fiscal and external buffers over the past decade, supported by prudent macroeconomic management in the context of a commodity boom. It has also achieved some of the largest declines in poverty and inequality in the region. The global outlook has changed, however, and Bolivia faces a challenge of adjusting to the new commodity price normal while preserving and building on the economic and social gains achieved in recent years. The authorities can pursue a measured approach to this adjustment given sizable buffers.

32. The impact of the commodity price declines is already being felt, with the outlook becoming increasingly challenging in the medium term. Growth for 2015 is projected to remain relatively high, at 4.1 percent, supported by a sizable public investment program and strong credit growth to the private sector. The outlook for 2016 and beyond, however, is increasingly challenging, as the full impact of lower international oil prices is expected to widen fiscal and external deficits further, absent an adjustment. Moreover, the short horizon of current proven reserves of natural gas adds to the urgency to implement measures to improve competitiveness and promote the development of non-commodity sectors.

33. Key policy imperatives are to improve the non-hydrocarbons primary balance and allow greater exchange rate flexibility. The latter would help facilitate adjustment to the large terms of trade shock and to future external shocks. It will also be important to adopt a credible medium-term fiscal framework which includes activities of SOEs more systematically, and strengthen the monetary policy framework to uphold the central bank's operational independence and credibility. If and when it does take place, any transition to greater exchange rate flexibility needs to be carefully crafted to ensure that inflation expectations remain well anchored and to preserve the de-dollarization achieved so far. Important conditions to make the transition an orderly process include central bank credibility and its primary focus on price stability, and fiscal sustainability. Regarding the financial sector, key provisions of the regulations—the credit quotas and interest rate caps—should be modified via decrees if material risks build up.

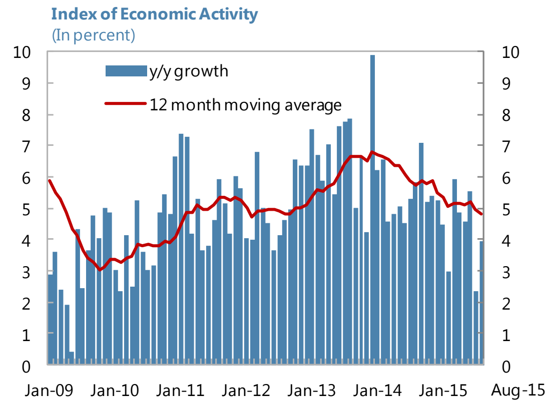
34. Increasing private investment is central to medium-term prospects, while preserving the reduction in inequality will be challenging given the end of the commodity boom. Measures to increase private investment include resolving remaining legal and regulatory uncertainty, ensuring transparent and incentive compatible hydrocarbons and mining fiscal regimes, reducing government incursions into product markets, and reducing labor costs and increasing labor market flexibility. Regarding maintaining the inclusiveness of growth, given a tighter fiscal envelope, it is essential to ensure that social transfers are well designed and targeted, and that there is a focus on the quality of education and healthcare.

35. Data provision is broadly adequate for surveillance, although has some shortcomings. Notable progress has been made to further strengthen the quality and timeliness of statistics, including working towards full subscription of the Special Data Dissemination Standard (SDDS). Improving data on quasi-fiscal activities of subsidiaries of SOEs outside the fiscal accounts, and the creation of a real estate price index would be further important steps.

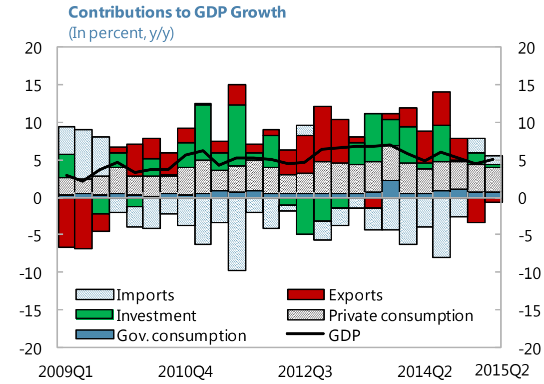
36. It is proposed that the next Article IV consultation with Bolivia be held on the standard 12-month cycle.

Figure 1. Bolivia: Real and External Sector Developments

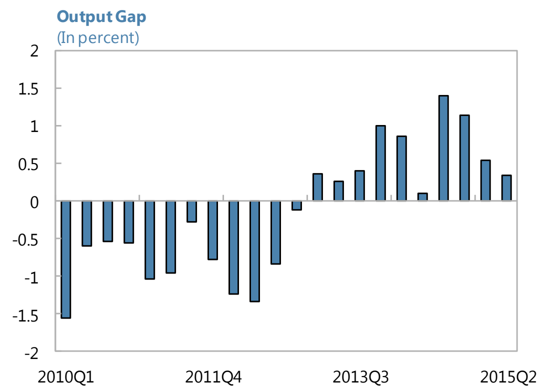
Growth remained robust, albeit with some deceleration in early 2015.



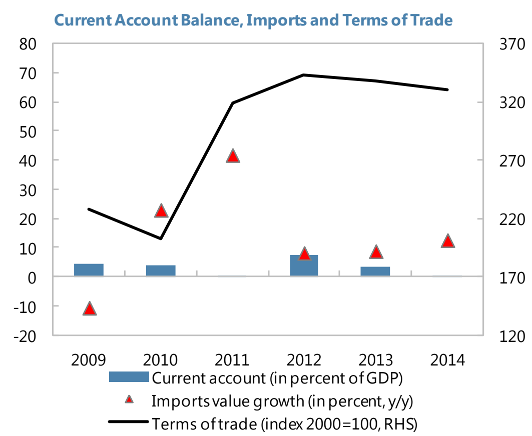
The contribution of exports has turned negative…



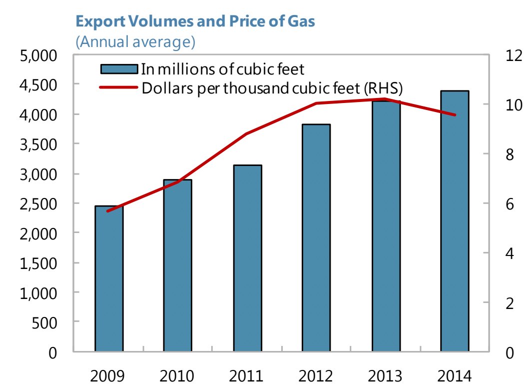
…and the output gap has started to shrink.



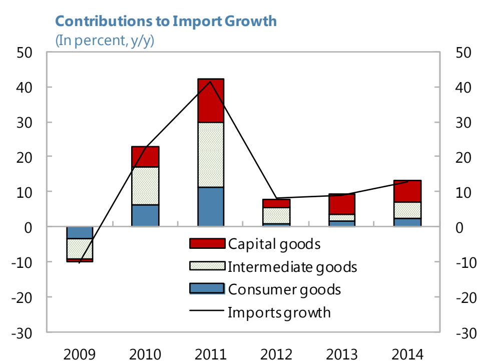
The current account surplus narrowed in 2014…



…as natural gas export prices started to drop.



Imports continued to grow, driven mainly by capital goods.

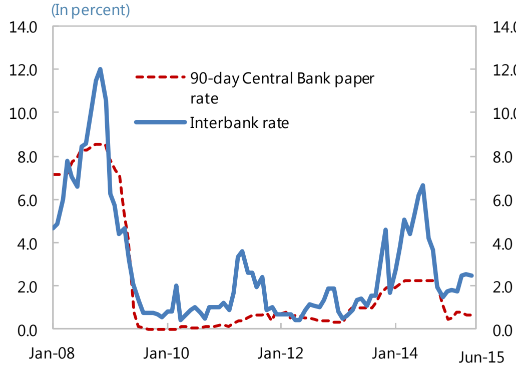


Sources: National Institute of Statistics, Central Bank of Bolivia, and Fund staff calculations.

Figure 2. Bolivia: Monetary Developments

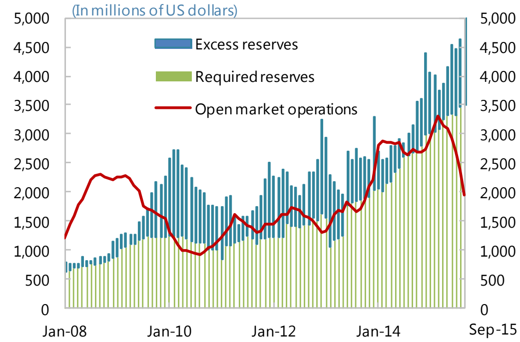
Monetary policy eased in 2015…

Policy Rate and Exchange Rate
(In percent)



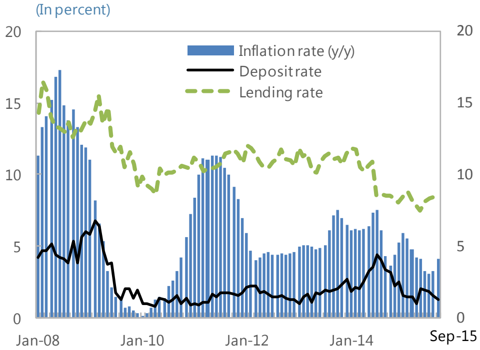
…including through the reduction of the stock of the central bank bills.

Bank Reserves and Open Market Operations
(In millions of US dollars)



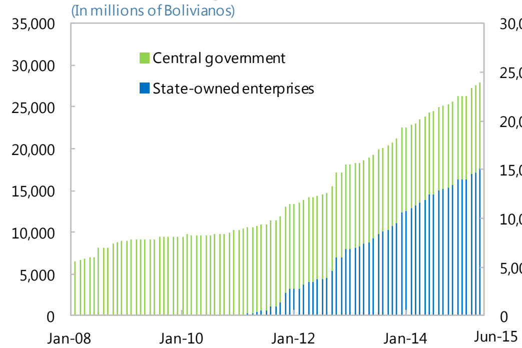
Inflationary pressures have subsided.

Interest Rates and Inflation
(In percent)



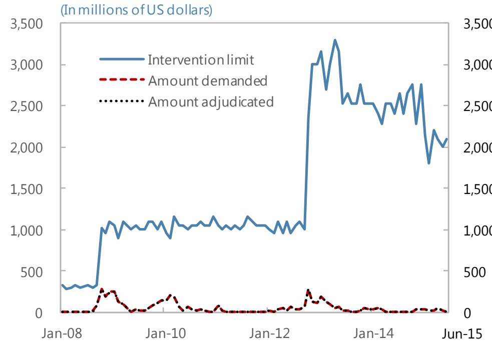
Central bank credit to state-owned enterprises continued to expand.

Central Bank Lending to the Public Sector
(In millions of Bolivianos)



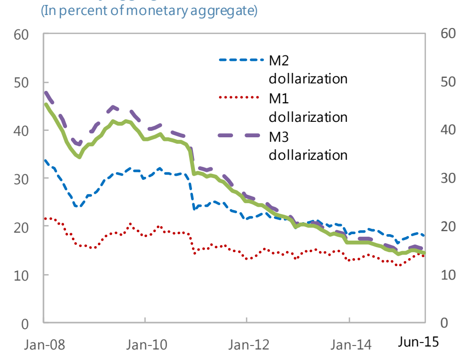
The foreign exchange market remains stable with low central bank intervention…

Central Bank Intervention in FX Market
(In millions of US dollars)



…and de-dollarization has continued.

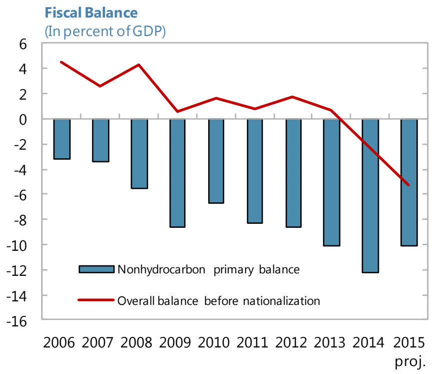
Monetary Aggregates Dollarization
(In percent of monetary aggregate)



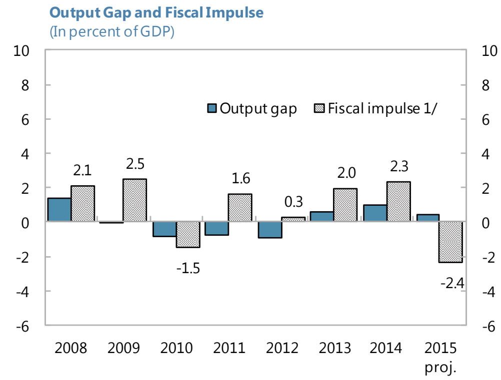
Sources: Central Bank of Bolivia and Fund staff calculations.

Figure 3. Bolivia: Fiscal Developments

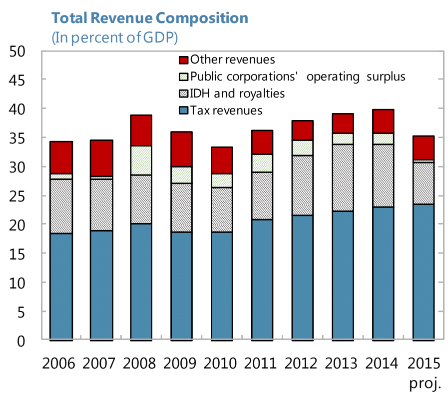
The overall fiscal deficit is projected to widen in 2015, after recording the first deficit in 2014 since 2005.



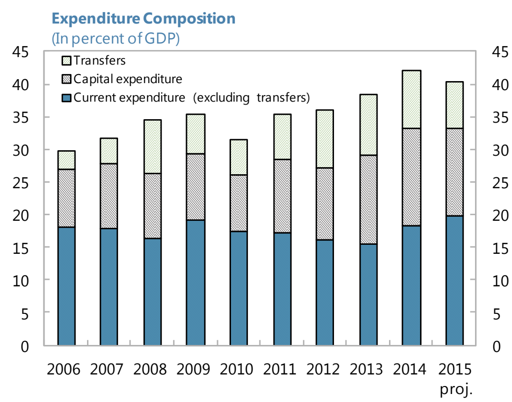
The fiscal impulse is projected to be negative, reflecting improvements in non-hydrocarbon primary balance



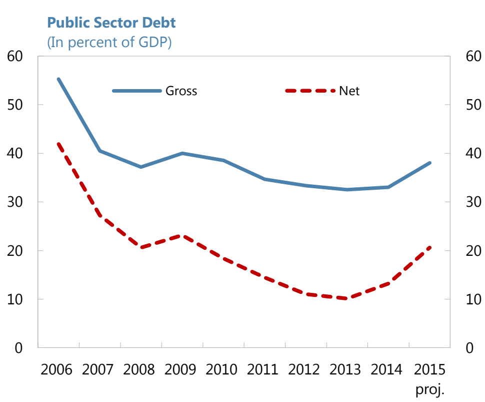
Hydrocarbons revenues are projected to shrink as oil prices decline…



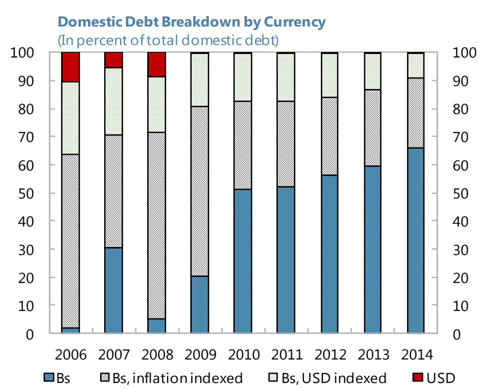
…with adjustments in capital expenditures partially offsetting the impact.



Public debt edged up in 2014, reflecting the first overall deficit since 2005.



The share of foreign currency debt continued to decline.

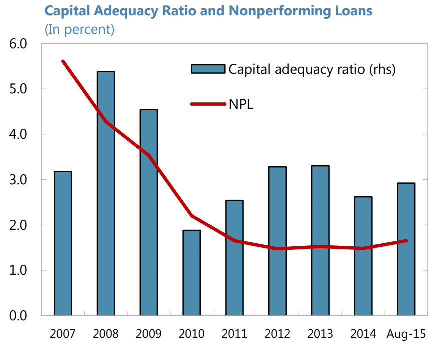


Sources: Ministry of Economy and Public Finances, Central Bank of Bolivia, and Fund staff calculations.

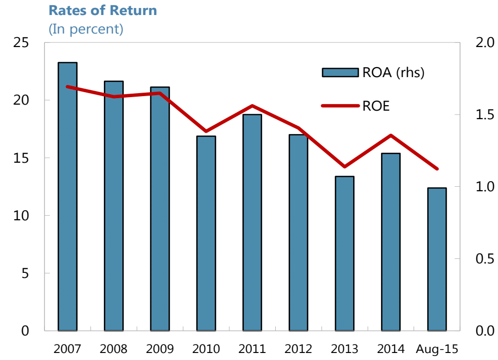
1/ The fiscal impulse is calculated as the change in the cyclically-adjusted non-hydrocarbons primary balance.

Figure 4. Bolivia: Financial Sector Developments

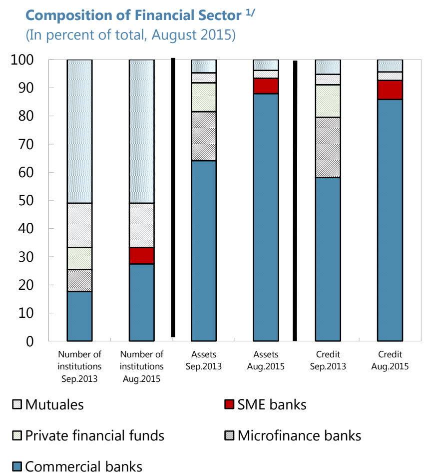
Capital adequacy remains above the regulatory requirements, and NPLs are low…



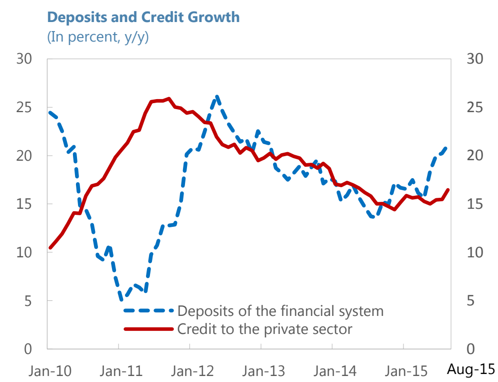
…while bank profitability is on a declining trend.



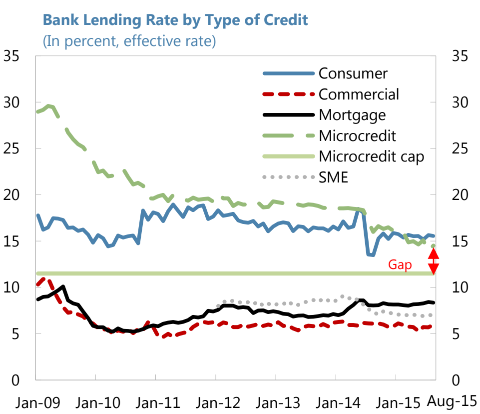
The introduction of the new Financial Services Law has led to some reorganization of financial sector…



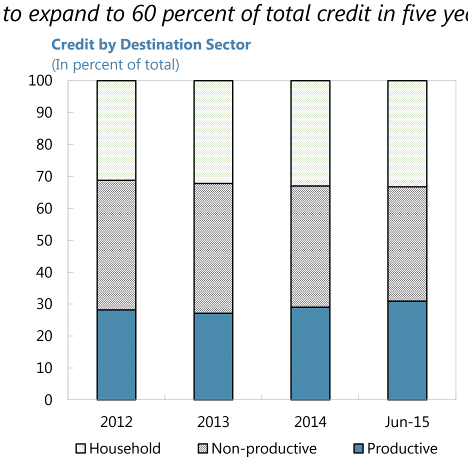
…and growth in private sector credit has decelerated



The microcredit lending rate is the most affected by the new law…



…and the share of credit to productive sector is mandated to expand to 60 percent of total credit in five years.



Sources: ASFI and Fund staff calculations.

[1] Licensed institutions only.

Table 2. Past Fund Policy Recommendations and Implementations

Recommendations	Status
Fiscal policy framework	
Avoid pro-cyclical fiscal stimulus and save budgetary resources	*Partially implemented.* The overall fiscal balance swung into deficit for the first time in nine years in 2014.
Improve the non-hydrocarbons balance	*Not implemented.*
Adopt a medium-term fiscal framework	*In progress.* The authorities are drafting a five-year development plan and are making progress with the preparation of medium-term fiscal projections and outlooks for key public enterprises.
Maintaining low and stable inflation	
Tighten monetary policy further if second-round inflationary effects prove persistent	*Implemented.* The inflationary pressures were succesfully contained in mid-2014 through monetary policy tightening and agreements with food producers.
Discontinue central bank lending to public enterprises	*Not implemented.* The central bank lending to public corporations has continued.
Gradually allow greater exchange rate flexibility	*Not implemented* . There has been a stable exchange rate vis-à-vis U.S. dollar since November 2011.
Safeguard financial stability	
Continue strengthening supervision	*Partially implemented.* Credit registry coverage was expanded and the depositor protection fund was created. Regulatory requirements were strengthened, including the inclusion of market risks to capital requirements, increase in the primary capital requirement (from 5 percent to 7 percent of risk-weighted assets and contingencies), and the guidance on operational and interest risks was issued. The Financial Stability Council has met for the first time in August 2015.
Employ less distortionary instruments to promote financial inclusion	*Not implemented.* Supreme decrees were issued to regulate interest rates and set credit quotas for the lending to the productive sector and social housing. Financial insitutions were given five years to comply, with intermediate annual targets to guide the progress.
Sustaining inclusive growth	
Improve the business climate	*Some progress made.* The Law on Investment Promotion was enacted in April 2014 and the Arbitration law in June 2015. Some of the laws, however, do not fully resolve regulatory uncertainty.
Enhance investment in infrastructure and human capital	*Partially implemented.* Significant increases in public infrastructure spending.

Source: Fund staff.

Table 3. Bolivia: Selected Economic and Financial Indicators

I. Social and Demographic Indicators

GDP per capita (U.S. dollars, 2014)	2,955	Poverty headcount ratio (percent of population, 2011)	45.0
Population (millions, 2014)	11.2	Gini index (2012)	46.6
Life expectancy at birth (years, 2011)	67	Adult literacy rate (percent, 2010)	91.2
Infant mortality rate (per thousand, 2010)	54.2	Net primary education enrollment rate (2010)	88.0

II. Economic Indicators

							Projections					
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Income and prices					(Annual percentage changes)							
Real GDP	3.4	4.1	5.2	5.1	6.8	5.5	4.1	3.5	3.5	3.5	3.5	3.5
Real GDP excluding hydrocarbons	4.7	3.5	5.0	4.4	6.2	5.4	5.2	3.6	3.6	3.7	3.6	3.6
CPI inflation (end-of-period)	0.3	7.2	6.9	4.5	6.5	5.2	4.2	5.0	5.0	5.0	5.0	5.0
					(In percent of GDP, unless otherwise indicated)							
Investment and savings												
Total investment	17.0	17.0	19.8	17.7	19.0	21.0	20.3	18.3	17.3	16.7	16.2	15.6
Public sector	9.5	9.5	10.5	10.5	11.3	12.4	11.1	9.2	8.5	8.3	8.1	7.8
Private sector (includes stockbuilding)	7.5	7.6	9.3	7.1	7.7	8.6	9.2	9.1	8.8	8.4	8.1	7.8
Gross domestic savings	19.8	23.9	25.5	27.1	26.0	22.4	15.0	12.8	12.9	13.0	13.0	12.9
Gross national savings	22.9	25.0	25.6	25.7	23.9	20.5	14.8	12.4	12.3	12.4	12.2	12.0
Public sector	9.9	11.1	11.4	12.3	12.0	10.1	5.8	3.4	3.1	3.2	3.5	3.5
Private sector	13.0	13.9	14.2	13.4	11.9	10.4	9.0	9.0	9.2	9.2	8.7	8.5
Saving/investment balances 1/	5.9	8.0	5.8	8.1	4.9	-0.6	-5.5	-6.0	-5.0	-4.3	-4.0	-3.6
Public sector	0.4	1.7	0.8	1.8	0.7	-2.3	-5.3	-5.8	-5.5	-5.1	-4.6	-4.3
Private sector	5.5	6.3	4.9	6.3	4.2	1.7	-0.2	-0.2	0.5	0.7	0.6	0.7
Combined public sector												
Revenues and grants	35.8	33.2	36.2	37.8	39.1	39.9	35.1	32.6	32.7	32.9	33.2	33.1
Of which: Hydrocarbon related revenue	11.3	10.2	11.4	13.0	13.5	12.7	7.7	5.5	5.8	5.9	6.0	6.1
Expenditure	35.8	31.5	35.4	36.0	38.4	43.3	40.4	38.4	38.1	37.9	37.8	37.4
Current	25.5	22.8	24.2	25.1	24.9	28.2	27.0	27.3	27.8	27.9	27.9	27.9
Capital 2/	10.3	8.7	11.2	11.0	13.5	15.0	13.4	11.1	10.4	10.0	9.8	9.5
Overall balance after nationalization costs	0.1	1.7	0.8	1.8	0.7	-3.4	-5.3	-5.8	-5.5	-5.1	-4.6	-4.3
Of which:												
Non-hydrocarbon balance, before nationalization costs	-10.3	-8.1	-9.6	-9.7	-11.1	-13.2	-11.1	-9.8	-9.7	-9.5	-9.3	-9.1
Total gross NFPS debt	40.0	38.5	34.7	33.3	32.5	33.0	38.0	42.0	44.1	45.8	46.8	47.6
NFPS deposits	12.6	15.1	14.4	16.5	16.5	16.5	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
External sector												
Current account 1/	4.3	3.9	0.3	7.2	3.5	0.2	-4.5	-5.0	-4.2	-3.6	-3.3	-2.9
Merchandise exports	28.4	32.4	34.6	41.3	37.9	37.0	27.2	24.0	23.6	23.2	22.7	22.0
Of which: natural gas	11.3	14.1	16.1	20.1	19.8	18.1	11.0	8.5	8.6	8.6	8.5	8.1
Merchandise imports	27.0	29.3	33.8	32.4	31.2	32.6	30.5	28.6	26.8	25.6	24.7	23.5
Capital and financial account	-2.4	0.8	8.6	-0.9	0.1	2.7	1.6	1.4	0.8	0.8	0.7	0.1
Of which: direct investment net	2.4	3.4	3.6	3.9	5.7	1.9	4.1	3.7	3.2	3.2	3.2	3.2
Overall balance of payments	1.9	4.7	8.9	6.3	3.6	2.9	-2.9	-3.6	-3.3	-2.8	-2.6	-2.8
Terms of trade index (percent change)	-24.6	-11.1	58.0	7.3	-1.5	-2.3	-15.7	-9.2	0.4	0.4	0.3	0.1
Net Central Bank foreign reserves 3/ 4/												
In millions of U.S. dollars	8,580	9,730	12,019	13,927	14,430	15,123	14,143	12,878	11,601	10,455	9,302	7,946
In percent of broad money	79.8	80.0	83.0	80.0	71.4	64.7	54.2	45.1	37.0	30.5	24.8	19.4
Exchange rates 5/												
Bolivianos/U.S. dollar (end-of-period)	7.0	6.9	6.9	6.9	6.9	6.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
REER, period average (percent change)	9.3	-4.9	1.9	5.2	5.6	7.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Money and credit					(Annual percentage changes, unless otherwise indicated)							
Credit to private sector (percent of GDP)	34.0	36.0	36.8	39.0	40.9	43.7	49.0	52.2	53.5	54.6	55.5	56.4
Broad money (percent change)	19.7	12.5	17.7	20.2	16.2	15.6	11.7	9.5	9.8	9.4	9.4	9.3
Interest rates (percent, end-of-period)												
Deposits (effective rate)	2.1	0.9	1.7	1.2	2.7	2.5	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Lending (effective rate)	9.1	10.4	10.8	10.6	11.4	8.0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
U.S. dollar and dollar-indexed deposits (in percent of total deposits)	52.6	43.8	34.5	26.3	21.0	17.6	16.4	15.2	14.0	12.8	11.6	10.4
U.S. dollar and dollar indexed credit (in percent of total credit)	49.5	38.6	30.7	21.3	15.8	10.2	10.2	10.2	10.2	10.2	10.2	10.2
Memorandum items:												
Nominal GDP (in billions of U.S. dollars)	17.5	19.8	24.1	27.3	30.9	33.2	33.5	35.2	38.2	41.4	44.9	48.6
Oil prices (in U.S. dollars per barrel)	61.8	79.0	104.0	105.0	104.1	96.2	51.6	50.4	55.4	59.8	62.2	63.0

Sources: Ministry of Economy and Public Finances, Central Bank of Bolivia, National Institute of Statistics, UDAPE, and Fund staff calculations.
1/ The discrepancy between the current account and the savings-investment balances reflects methodological differences. For the projection years, the discrepancy is assumed to remain constant in dollar value.
2/ Includes nationalization costs and net lending.
3/ Excludes reserves from the Latin American Reserve Fund (FLAR) and Offshore Liquidity Requirements (RAL).
4/ All foreign assets valued at market prices.
5/ Official (buy) exchange rate.

Table 4. Bolivia: Operations of the Combined Public Sector[1/]

(In percent of GDP, unless otherwise indicated)

							Projections					
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Revenue	**35.8**	**33.2**	**36.2**	**37.8**	**39.1**	**39.9**	**35.1**	**32.6**	**32.7**	**32.9**	**33.2**	**33.1**
Taxes	26.9	26.3	28.9	31.8	33.7	33.7	30.6	28.4	28.3	28.3	28.4	28.4
IDH and royalties	8.3	7.7	8.3	10.3	11.5	10.8	7.3	5.5	5.7	5.9	5.9	5.9
Direct taxes	4.7	4.6	5.5	5.7	6.0	6.2	6.1	6.1	6.1	6.0	6.0	6.0
o/w: Corporate income tax	4.0	3.8	4.6	5.0	5.3	5.4	5.4	5.4	5.4	5.4	5.4	5.4
Indirect taxes	13.9	14.0	15.2	15.7	16.2	16.7	17.2	16.7	16.5	16.4	16.5	16.5
o/w: VAT	7.0	7.2	8.1	8.7	9.0	9.0	9.0	8.6	8.4	8.4	8.4	8.5
o/w: Excise tax on fuel	1.5	1.6	1.5	1.3	1.3	1.3	1.3	1.4	1.4	1.4	1.4	1.4
Grants	1.2	1.1	0.8	0.7	0.3	0.3	0.3	0.3	0.2	0.2	0.2	0.2
Other revenue	7.7	5.8	6.5	5.4	5.1	5.9	4.3	4.0	4.1	4.3	4.5	4.5
Nontax revenue	4.7	3.4	3.0	2.6	2.7	3.8	3.8	3.9	3.9	4.0	4.0	4.0
Public enterprises operating balance	3.0	2.5	3.2	2.6	2.0	1.9	0.4	0.0	0.1	0.0	0.1	0.2
Central bank operating balance	0.1	-0.1	0.2	0.1	0.3	0.2	0.0	0.0	0.1	0.3	0.4	0.4
Expenditure	**35.8**	**31.5**	**35.4**	**36.0**	**38.4**	**43.3**	**40.4**	**38.4**	**38.1**	**37.9**	**37.8**	**37.4**
Expense	**25.5**	**22.8**	**24.2**	**25.1**	**24.9**	**28.2**	**27.0**	**27.3**	**27.8**	**27.9**	**27.9**	**27.9**
Compensation of employees	10.2	9.5	9.3	9.0	9.1	10.4	11.2	10.7	10.7	10.7	10.7	10.7
Purchases of goods and services	2.6	2.2	3.0	2.1	2.3	2.8	3.3	3.3	3.3	3.3	3.3	3.3
Interest	1.6	1.4	1.2	1.0	1.0	1.0	1.0	1.1	1.2	1.3	1.3	1.3
Domestic	1.3	1.1	1.0	0.8	0.6	0.5	0.6	0.7	0.8	0.9	0.9	1.0
Foreign	0.4	0.3	0.2	0.2	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.3
Subsidies 2/	1.2	0.9	2.1	3.1	3.0	2.0	1.1	1.6	2.1	2.1	2.1	2.1
Social benefits 3/	8.4	7.8	7.9	8.8	8.9	9.5	8.9	9.0	9.0	9.0	9.0	9.0
Other expense	1.4	1.1	0.7	1.1	0.7	2.6	1.4	1.4	1.4	1.4	1.4	1.4
Other	0.9	1.1	0.7	1.1	0.7	1.5	1.4	1.4	1.4	1.4	1.4	1.4
Nationalization cost	0.3	0.0	0.0	0.0	0.0	1.1	0.0	0.0	0.0	0.0	0.0	0.0
Net acquisition of nonfinancial assets 4/	**10.3**	**8.7**	**11.2**	**11.0**	**13.5**	**15.0**	**13.4**	**11.1**	**10.4**	**10.0**	**9.8**	**9.5**
o/w: Public Enterprises	1.2	0.9	1.9	2.8	3.2	3.7	3.5	3.0	2.9	2.8	2.7	2.6
Gross operating balance	**10.3**	**10.4**	**12.0**	**12.7**	**14.2**	**11.7**	**8.1**	**5.3**	**4.9**	**5.0**	**5.2**	**5.2**
Net lending/borrowing (overall balance)	**0.0**	**1.7**	**0.8**	**1.8**	**0.7**	**-3.4**	**-5.3**	**-5.8**	**-5.5**	**-5.1**	**-4.6**	**-4.3**
Net financial transactions	**0.1**	**1.7**	**0.8**	**1.8**	**0.7**	**-3.4**	**-5.3**	**-5.8**	**-5.5**	**-5.1**	**-4.6**	**-4.3**
Net incurrence of liabilities	**-0.1**	**-1.7**	**-0.8**	**-1.8**	**-0.7**	**3.4**	**5.3**	**5.8**	**5.5**	**5.1**	**4.6**	**4.3**
External	1.0	1.0	1.8	2.3	2.5	1.3	1.5	1.6	1.5	1.5	1.5	1.4
Disbursements	3.1	4.1	4.7	5.5	4.0	2.3	3.0	3.0	2.9	2.8	2.7	2.6
Amortizations	-2.1	-3.0	-2.8	-3.2	-1.1	-0.9	-1.4	-1.4	-1.3	-1.2	-1.1	-1.2
Other external	0.0	0.0	-0.1	0.0	-0.5	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Domestic	-1.1	-2.7	-2.6	-4.1	-3.1	2.0	3.8	4.2	3.9	3.5	3.1	2.9
Banking system	-0.2	-5.3	-3.5	-3.4	-2.1	1.8	2.8	3.1	2.8	2.6	2.4	2.0
Central Bank	-0.4	-4.9	-2.7	-3.3	-2.4	1.8	2.2	2.5	2.3	2.1	1.9	1.8
Commercial banks	0.2	-0.4	-0.9	-0.1	0.2	0.0	0.6	0.6	0.5	0.5	0.4	0.2
Pension funds	0.0	0.0	0.0	-0.7	-0.8	-0.8	0.0	0.0	0.0	0.0	0.0	0.0
Other domestic	-1.1	2.6	0.9	-0.7	-1.0	0.2	1.0	1.2	1.1	0.9	0.7	0.9
Memorandum items:												
Primary balance	1.7	3.1	2.1	2.8	1.6	-2.4	-4.3	-4.7	-4.2	-3.8	-3.3	-3.0
Overall balance before nationalization	0.4	1.7	0.8	1.8	0.7	-2.3	-5.3	-5.8	-5.5	-5.1	-4.6	-4.3
o/w Non-hydrocarbon primary balance 5/	-8.6	-6.7	-8.3	-8.7	-10.1	-12.3	-10.1	-8.7	-8.5	-8.3	-8.0	-7.8
Overall balance as a share of non-hydrocarbon GDP	0.4	1.8	0.9	1.9	0.7	-2.5	-5.7	-6.1	-5.8	-5.3	-4.8	-4.5
Hydrocarbon related revenue 6/	11.3	10.2	11.4	13.0	13.5	12.7	7.7	5.5	5.8	5.9	6.0	6.1
Hydrocarbon balance 7/	10.1	9.8	10.4	11.4	11.7	11.0	5.9	4.0	4.3	4.5	4.7	4.8
Nonfinancial public sector gross public debt	40.0	38.5	34.7	33.3	32.5	33.0	38.0	42.0	44.1	45.8	46.8	47.6
o/w gross foreign public debt	15.6	15.4	14.8	15.7	17.0	17.3	18.6	19.3	19.3	19.4	19.4	19.3
Nonfinancial public sector gross public debt (in percent of non-hydrocarbon GDP)	42.6	41.1	37.5	36.9	36.3	36.5	40.6	44.3	46.6	48.3	49.3	50.0
Nominal GDP in billions of Bolivianos	121.7	137.9	166.2	187.2	211.9	228.0	230.1	241.7	262.1	284.2	308.0	333.6

Sources: Ministry of Economy and Public Finances and Fund staff calculations.

1/ The operation of mixed-ownership companies, primarily in the telecommunications, electricity and hydrocarbon sectors, are not included.

2/ Includes incentives for hydrocarbon exploration investments in the projection period.

3/ Includes pensions, cash transfers to households, and social investment programs (previously classified as capital expenditure).

4/ The authorities' programs of social investment, including school breakfast, recurrent costs on basic sanitation and social management, are reclassified to current spending.

5/ Primary balance before nationalization costs minus hydrocarbon related balance.

6/ Hydrocarbon related revenues are defined as direct hydrocarbon tax (IDH), royalties, and the operating balance of state oil/gas company (YPFB).

7/ Hydrocarbon related revenues minus YPFB capital expenditures.

Table 5. Bolivia: Summary of Balance of Payments
(In millions of U.S. dollars, unless otherwise indicated)

	2009	2010	2011	2012	2013	2014	Projections 2015	2016	2017	2018	2019	2020
Current account	**746**	**766**	**77**	**1,970**	**1,095**	**62**	**-1,517**	**-1,772**	**-1,587**	**-1,474**	**-1,477**	**-1,419**
Trade balance	415	812	431	2,676	2,360	1,783	-762	-1,259	-812	-581	-453	-251
Exports, f.o.b.	4,960	6,402	8,358	11,254	11,698	12,301	9,135	8,453	9,035	9,627	10,197	10,689
Exports, c.i.f.	5,486	7,052	9,215	11,991	12,372	13,028	9,860	9,179	9,760	10,353	10,922	11,415
Natural gas	1,968	2,798	3,885	5,479	6,113	6,012	3,682	3,003	3,289	3,579	3,822	3,962
Mining	1,846	2,396	3,429	3,744	3,077	3,929	3,577	3,470	3,544	3,618	3,694	3,781
Soy - related	488	496	628	977	1,211	1,083	846	915	1,048	1,196	1,369	1,568
Other	1,185	1,363	1,273	1,791	1,970	2,004	1,756	1,791	1,879	1,961	2,037	2,105
Imports, c.i.f.	-4,545	-5,590	-7,927	-8,578	-9,338	-10,518	-9,897	-9,712	-9,847	-10,209	-10,650	-10,941
Services (net)	-209	-263	-369	-342	-627	-1,099	-700	-374	-573	-621	-674	-729
Income (net)	-674	-864	-1,161	-1,629	-1,908	-1,707	-1,341	-1,447	-1,535	-1,631	-1,734	-1,845
Transfers (net)	1,213	1,081	1,175	1,266	1,270	1,084	1,286	1,308	1,334	1,359	1,384	1,408
Capital and financial account	**-421**	**157**	**2,083**	**-258**	**26**	**909**	**537**	**507**	**310**	**328**	**324**	**63**
Capital transfers	111	-7	6	6	6	5	0	0	0	0	0	0
Direct investment (net)	426	672	859	1,060	1,750	648	1,384	1,303	1,223	1,326	1,437	1,556
Gross investment	687	915	954	1,505	2,030	2,113	1,904	1,893	1,939	2,101	2,318	2,310
Disinvestment and investment abroad	-264	-293	-95	-445	-280	-1,465	-520	-590	-716	-775	-881	-754
Portfolio investment (net)	-154	90	186	-360	-429	-561	-448	-388	-463	-501	-564	-818
Public sector	160	263	537	651	-458	1,101	539	578	619	662	707	686
Disbursements	381	538	777	1,135	1,243	759	1,010	1,056	1,104	1,154	1,207	1,262
Amortization	-376	-528	-607	-829	-279	-193	-471	-478	-485	-492	-499	-576
Other (net)	156	253	367	346	-1,423	573	0	0	0	0	0	0
Private sector	-572	-101	-611	-815	-1,046	-1,303	-938	-986	-1,069	-1,160	-1,256	-1,361
Errors and omissions	-392	-759	1,107	-800	203	1,018	0	0	0	0	0	0
Overall balance	**325**	**923**	**2,160**	**1,712**	**1,122**	**971**	**-980**	**-1,265**	**-1,277**	**-1,146**	**-1,153**	**-1,355**
Financing	**-481**	**-923**	**-2,160**	**-1,712**	**-1,122**	**-971**	**980**	**1,265**	**1,277**	**1,146**	**1,153**	**1,355**
Memorandum items:												
Current account (in percent of GDP)	4.3	3.9	0.3	7.2	3.5	0.2	-4.5	-5.0	-4.2	-3.6	-3.3	-2.9
Current account (in percent of non-hydrocarbon GDP)	4.6	4.1	0.3	8.0	4.0	0.2	-4.8	-5.3	-4.4	-3.8	-3.5	-3.1
Non-energy current account (in percent of non-hydrocarbon GDP)	-3.4	-6.0	-10.6	-7.9	-12.5	-14.6	-12.5	-10.5	-9.6	-8.9	-8.5	-7.9
Merchandise exports (in percent of GDP)	28.4	32.4	34.6	41.3	37.9	37.0	27.2	24.0	23.6	23.2	22.7	22.0
Merchandise imports (in percent of GDP)	-26.0	-28.3	-32.8	-31.4	-30.2	-31.6	-29.5	-27.6	-25.8	-24.6	-23.7	-22.5
Net official reserves (end-of-period)	8,580	9,730	12,019	13,927	14,430	15,123	14,143	12,878	11,601	10,455	9,302	7,946
(in months of imports of goods and services)	19.5	17.6	15.7	16.8	15.6	14.1	14.4	13.7	11.8	10.2	8.7	7.1
Foreign direct investment (in percent of GDP)	2.4	3.4	3.6	3.9	5.7	1.9	4.1	3.7	3.2	3.2	3.2	3.2
GDP (in millions of U.S. dollars)	17,464	19,786	24,135	27,282	30,883	33,237	33,535	35,229	38,212	41,431	44,902	48,629
Capital account (in percent of GDP)	-2.4	0.8	8.6	-0.9	0.1	2.7	1.6	1.4	0.8	0.8	0.7	0.1
Errors and omissions (in percent of GDP)	-2.2	-3.8	4.6	-2.9	0.7	3.1	0.0	0.0	0.0	0.0	0.0	0.0
Export value growth (in percent)	-24.0	29.1	30.6	34.6	3.6	5.2	-25.5	-7.5	6.9	6.6	5.9	4.8
Export volume growth (in percent)	6.5	28.5	-26.0	25.8	7.5	10.5	-7.0	1.2	5.8	5.6	5.1	4.4
Export prices growth (in percent)	-28.6	0.4	76.4	7.0	-3.7	-4.8	-19.9	-8.6	1.0	0.9	0.8	0.5
Import value growth (in percent)	-10.6	23.0	41.8	8.2	8.9	13.1	-7.2	-1.9	1.4	3.7	4.4	3.6
Import volume growth (in percent)	-5.5	8.8	27.0	8.5	11.3	16.0	-2.3	-2.6	0.8	3.2	3.9	3.3
Import prices growth (in percent)	-5.3	13.0	11.6	-0.3	-2.2	-2.5	-5.0	0.7	0.6	0.5	0.4	0.4

Sources: Central Bank of Bolivia, National Institute of Statistics and Fund staff calculations.

Table 6. Bolivia: Central Bank Monetary Survey

	2009	2010	2011	2012	2013	2014	Projections 2015	2016
	(Flows in millions of Bolivianos, unless otherwise indicated)							
Net international reserves	5,981	7,720	14,923	13,090	3,453	4,752	-6,723	-8,677
(Flows in millions of U.S. dollars)	858	1,150	2,289	1,908	503	693	-980	-1,265
Net domestic assets	2,746	-4,918	-5,629	-7,141	1,541	2,781	7,411	10,124
Net credit to the nonfinancial public sector	-221	-6,923	-4,199	-5,989	-4,538	4,510	5,000	6,000
Net credit to financial intermediaries	4,140	2,758	-1,788	757	2,155	-641	432	734
Of which: Open market operations (increase -)	4,385	2,869	-1,590	747	-1,964	-680	2,488	500
Other items (net)	-1,173	-753	357	-1,909	3,924	-1,088	1,979	3,389
Net medium and long-term foreign assets	-1,452	228	-104	953	-177	236	-14	0
Base money	7,275	3,031	9,190	6,902	4,817	7,769	675	1,446
Currency in circulation	1,849	5,693	3,999	4,080	4,336	4,371	2,139	1,888
Bank reserves	5,426	-2,662	5,191	2,822	482	3,398	-1,465	-442
Legal Reserves	5,916	-2,749	4,669	2,533	-1,959	2,365	2,080	1,933
	(Stocks in millions of Bolivianos, unless otherwise indicated)							
Net international reserves	59,803	67,524	82,447	95,537	98,991	103,743	97,020	88,343
(Stocks in millions of U.S. dollars)	8,580	9,730	12,019	13,927	14,430	15,123	14,143	12,878
Net domestic assets	-30,511	-35,429	-41,058	-48,199	-46,658	-43,877	-36,466	-26,342
Net credit to the nonfinancial public sector	-12,434	-19,357	-23,556	-29,545	-34,083	-29,572	-24,572	-18,572
Net credit to financial intermediaries	-9,112	-6,354	-8,142	-7,384	-5,229	-5,870	-5,438	-4,703
Of which: Open market operations	-10,869	-8,000	-9,591	-8,844	-10,808	-11,488	-9,000	-8,500
Other items (net)	-8,965	-9,718	-9,361	-11,270	-7,346	-8,434	-6,456	-3,066
Net medium and long-term foreign assets	254	482	378	1,331	1,154	1,390	1,376	1,376
Base money	29,546	32,577	41,767	48,669	53,487	61,256	61,930	63,377
Currency in circulation	18,892	24,586	28,585	32,665	37,001	41,372	43,511	45,399
Bank reserves	10,653	7,991	13,182	16,004	16,486	19,884	18,420	17,978
Legal reserves	9,105	6,356	11,025	13,558	11,599	13,964	16,045	17,978
	(Annual percentage changes)							
Net international reserves	11.1	12.9	22.1	15.9	3.6	4.8	-6.5	-8.9
(Stocks in millions of U.S. dollars)	11.1	13.4	23.5	15.9	3.6	4.8	-6.5	-8.9
Net domestic assets	-8.3	16.1	15.9	17.4	-3.2	-6.0	-16.9	-27.8
Net credit to the nonfinancial public sector	1.8	55.7	21.7	25.4	15.4	-13.2	-16.9	-24.4
Net credit to financial intermediaries	-31.2	-30.3	28.1	-9.3	-29.2	12.3	-7.4	-13.5
Of which: Open market operations	-28.7	-26.4	19.9	-7.8	22.2	6.3	-21.7	-5.6
Other items (net)	15.1	8.4	-3.7	20.4	-34.8	14.8	-23.5	-52.5
Net medium and long-term foreign assets	-85.1	89.9	-21.5	252.0	-13.3	20.4	-1.0	0.0
Base money	32.7	10.3	28.2	16.5	9.9	14.5	1.1	2.3
Currency in circulation	10.8	30.1	16.3	14.3	13.3	11.8	5.2	4.3
Bank reserves	103.8	-25.0	65.0	21.4	3.0	20.6	-7.4	-2.4
Legal reserves	185.5	-30.2	73.5	23.0	-14.4	20.4	14.9	12.0

Sources: Central Bank of Bolivia and Fund staff calculations.

Table 7. Bolivia: Commercial Bank and Non-Bank Depository Institutions

							Projections	
	2009	2010	2011	2012	2013	2014	2015	2016
	(Flows in millions of Bolivianos, unless otherwise indicated)							
Foreign assets	3,994	-476	-1,923	1,477	1,914	3,720	5,389	5,263
(Stock in millions of U.S. dollars)	573	-62	-263	215	279	542	786	767
Net domestic assets	6,846	3,852	13,764	13,821	13,547	14,639	11,790	10,616
Net credit to the public sector	1,250	-564	-1,455	-143	510	-112	1,372	1,372
Credit to the private sector	3,400	8,258	11,423	11,832	13,784	13,038	12,973	13,388
Net position with the central bank	2,438	-3,211	6,899	4,642	2,088	4,372	-3,953	-942
Other items (net)	-241	-632	-3,103	-2,511	-2,835	-2,659	1,398	-3,203
Foreign liabilities	339	-896	-723	-193	85	116	-1,194	-1,194
Deposits	10,502	4,272	12,564	15,491	15,376	18,244	18,372	17,073
Local currency deposits	5,188	7,436	13,984	17,476	16,901	18,648	16,844	16,182
Foreign currency deposits	5,314	-3,164	-1,421	-1,985	-1,525	-404	1,529	891
	(Stocks in millions of Bolivianos, unless otherwise indicated)							
Foreign assets	10,583	10,107	8,184	9,660	11,574	15,295	20,684	25,947
(Stock in millions of U.S. dollars)	1,518	1,456	1,193	1,408	1,687	2,230	3,015	3,782
Net domestic assets	49,871	53,723	67,487	81,308	94,855	109,494	121,284	131,900
Net credit to the public sector	2,429	1,866	411	268	778	666	2,038	3,410
Credit to the private sector	41,409	49,668	61,090	72,922	86,706	99,744	112,717	126,105
Net position with the central bank	16,119	12,909	19,808	24,450	26,538	30,910	26,957	26,016
Other items (net)	-10,087	-10,719	-13,822	-16,333	-19,167	-21,826	-20,429	-23,632
Foreign liabilities	3,084	2,188	1,465	1,272	1,357	1,472	278	-915
Deposits	57,371	61,642	74,206	89,697	105,073	123,317	141,689	158,762
Local currency deposits	27,199	34,635	48,619	66,095	82,996	101,644	118,487	134,670
Foreign currency deposits	30,172	27,007	25,587	23,602	22,077	21,673	23,201	24,092
	(Annual percentage changes)							
Foreign assets	60.6	-4.5	-19.0	18.0	19.8	32.1	35.2	25.4
(Stock in millions of U.S. dollars)	60.6	-4.1	-18.1	18.0	19.8	32.1	35.2	25.4
Net domestic assets	15.9	7.7	25.6	20.5	16.7	15.4	10.8	8.8
Net credit to the public sector	105.9	-23.2	-78.0	-34.7	190.2	-14.4	205.9	67.3
Credit to the private sector	8.9	19.9	23.0	19.4	18.9	15.0	13.0	11.9
Net position with the central bank	17.8	-19.9	53.4	23.4	8.5	16.5	-12.8	-3.5
Other items (net)	2.4	6.3	28.9	18.2	17.4	13.9	-6.4	15.7
Foreign liabilities	12.4	-29.1	-33.0	-13.2	6.7	8.5	-81.1	-428.9
Deposits	22.4	7.4	20.4	20.9	17.1	17.4	14.9	12.0
Local currency deposits	23.6	27.3	40.4	35.9	25.6	22.5	16.6	13.7
Foreign currency deposits	21.4	-10.5	-5.3	-7.8	-6.5	-1.8	7.1	3.8
Memorandum items:								
Credit to private sector (in percent of GDP)	34.0	36.0	36.8	39.0	40.9	43.7	49	52
Deposits (in percent of GDP)	47.1	44.7	44.6	47.9	49.6	54.1	62	66
Broad money (in percent of GDP)	61.6	61.2	59.7	63.8	65.5	70.3	78	81
U.S. dollar and dollar-indexed deposits (in percent of total deposits)	52.6	43.8	34.5	26.3	21.0	17.6	16	15
U.S. dollar and dollar indexed credit (in percent of total credit)	49.5	38.6	30.7	21.3	15.8	10.2	10	10

Sources: Central Bank of Bolivia and Fund staff calculations.

Table 8. Bolivia: Financial System Survey[1/]

	2009	2010	2011	2012	2013	2014	Projections 2015	2016
	(Flows in millions of Bolivianos, unless otherwise indicated)							
Net short-term foreign assets	9,975	7,244	13,000	14,567	5,367	8,472	-1,334	-3,414
(Flows in millions of U.S. dollars)	1,431	1,088	2,025	2,123	782	1,235	-194	-498
Net domestic assets	4,167	1,029	1,313	4,339	14,189	13,025	18,836	19,185
Net credit to the public sector	1,028	-7,487	-5,654	-6,132	-4,028	4,398	6,372	7,372
Credit to the private sector	3,400	8,258	11,423	11,832	13,784	13,038	12,973	13,388
Other items (net)	-261	258	-4,456	-1,362	4,433	-4,411	-509	-1,576
Net medium and long-term foreign liabilities (increase -)	1,791	-1,124	-619	-1,146	262	-120	-1,180	-1,194
Broad money	12,352	9,398	14,933	20,052	19,295	21,618	18,682	16,965
Liabilities in domestic currency	7,038	12,562	16,354	22,036	20,819	22,022	17,153	16,074
Foreign currency deposits	5,314	-3,164	-1,421	-1,985	-1,525	-404	1,529	891
	(Stocks in millions of Bolivianos, unless otherwise indicated)							
Net short-term foreign assets	70,387	77,631	90,631	105,198	110,565	119,037	117,704	114,290
(Stocks in millions of U.S. dollars)	10,099	11,186	13,212	15,335	16,117	17,352	17,158	16,660
Net domestic assets	7,428	8,458	9,771	14,110	28,299	41,324	60,160	79,344
Net credit to the public sector	-10,005	-17,492	-23,145	-29,277	-33,305	-28,906	-22,534	-15,162
Credit to the private sector	41,409	49,668	61,090	72,922	86,706	99,744	112,717	126,105
Other items (net)	-23,977	-23,718	-28,174	-29,536	-25,103	-29,514	-30,023	-31,599
Net medium and long-term foreign liabilities (increase -)	2,830	1,706	1,087	-59	203	82	-1,097	-2,291
Broad money	74,985	84,382	99,315	119,367	138,661	160,279	178,961	195,925
Liabilities in domestic currency	44,813	57,375	73,728	95,765	116,584	138,606	155,759	171,834
Foreign currency deposits	30,172	27,007	25,587	23,602	22,077	21,673	23,201	24,092
	(Changes in percent of broad money at the beginning of the period)							
Net short-term foreign assets	15.9	9.7	15.4	14.7	4.5	6.1	-0.8	-1.9
Net domestic assets	6.7	1.4	1.6	4.4	11.9	9.4	11.8	10.7
Net credit to the public sector	1.6	-10.0	-6.7	-6.2	-3.4	3.2	4.0	4.1
Credit to the private sector	5.4	11.0	13.5	11.9	11.5	9.4	8.1	7.5
Other items (net)	-0.4	0.3	-5.3	-1.4	3.7	-3.2	-0.3	-0.9
Net medium and long-term foreign liabilities	2.9	-1.5	-0.7	-1.2	0.2	-0.1	-0.7	-0.7
Broad money	19.7	12.5	17.7	20.2	16.2	15.6	11.7	9.5
Liabilities in domestic currency	11.2	16.8	19.4	22.2	17.4	15.9	10.7	9.0
Foreign currency deposits	8.5	-4.2	-1.7	-2.0	-1.3	-0.3	1.0	0.5

Sources: Central Bank of Bolivia, and Fund staff calculations.

1/ The financial system comprises the central bank, commercial banks and nonbanks, and the Banco de Desarrollo Productivo (BDP), which is a state-owned second-tier bank.

Table 9. Bolivia: Selected Vulnerability Indicators

	2009	2010	2011	2012	2013	2014
Reserve adequacy	(In millions of U.S. dollars, unless otherwise indicated)					
Net international reserves	8,580	9,730	12,019	13,927	14,430	15,123
NIR coverage, in percent of:						
Dollar deposits	198.2	250.0	322.2	404.8	448.4	478.7
Total deposits	104.2	109.5	111.1	106.5	94.2	84.1
Broad money	79.8	80.0	83.0	80.0	71.4	64.7
In months of imports of goods and services	19.5	17.6	15.7	16.8	15.6	14.1
Net foreign assets of the financial system	1,961	1,772	1,407	1,594	1,885	2,444
NFA coverage, in percent of:						
Dollar deposits	45.3	45.5	37.7	46.3	58.6	77.4
Total deposits	23.8	19.9	13.0	12.2	12.3	13.6
Broad money	18.2	14.6	9.7	9.2	9.3	10.5
Debt ratios	(In percent of GDP)					
Total gross NFPS debt	40.0	38.5	34.7	33.3	32.5	33.0
Domestic	24.4	23.1	19.9	17.6	15.5	15.8
External	15.6	15.4	14.8	15.7	17.0	17.3
Total net NFPS debt	23.1	18.4	14.4	11.0	10.1	13.2
Private external debt	5.3	5.0	3.8	2.9	2.6	2.6
Net International Investment Position	17.4	15.8	16.4	18.0	14.3	13.8
Commodity dependency						
Hydrocarbon revenue (in percent of total revenues) 1/	31.6	30.7	31.6	35.4	34.2	33.8
Non-hydrocarbon fiscal balance 2/	-10.3	-8.1	-9.6	-9.7	-11.1	-13.2
Gas exports (in percent of total exports)	39.7	43.7	46.5	48.7	52.3	48.9
Mining exports (in percent of total exports)	37.2	37.4	41.0	33.3	26.3	31.9
Banking sector indicators 3/						
Nonperforming loans (in percent of total loans)	3.5	2.2	1.7	1.5	1.5	1.5
Restructured loans (in percent of total loans)	6.4	3.6	2.2	1.5	1.4	1.2
Nonperforming and restructured loans (in percent of total loans)	9.9	5.8	3.9	3.0	2.9	
Capital adequacy ratio (in percent)	13.3	11.9	12.3	12.6	12.7	12.3
Profits after tax (in percent of equity)	20.6	17.3	19.5	17.6	14.2	16.9
Cash and short-term investments (in percent of total assets)	48.0	39.0	37.6	37.4	35.5	35.8
Composition of bank deposits						
Dollar deposits (in percent of total deposit)	52.6	43.8	34.5	26.3	21.0	17.6
Local currency deposits (in percent of total deposit)	47.4	56.2	65.5	73.7	79.0	82.4
Memorandum items:						
Fiscal balance (in percent of GDP)	0.1	1.7	0.8	1.8	0.7	-3.4
Total financial system deposits (US$ million)	6,724	8,267	8,986	10,817	13,075	15,317

Sources: Ministry of Economy and Public Finances, Central Bank of Bolivia, ASFI, and Fund staff calculations.
1/ Hydrocarbon related revenues are defined as direct hydrocarbon tax (IDH), royalties, and the operating balance of YPFB.
2/ Excludes hydrocarbon related revenues and YPFB capital expenditures.
3/ Latest available data.

Table 10. Bolivia: Millennium Development Goals

	First Observation	2006	2007	2008	2009	2010	2011	2012	2013	2014	Target 2015
Goal 1. Eradicate Extreme Poverty and Hunger											
Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day.											
Population below US$1 a day (in percent)	41.2 (1990)	37.7	37.7	29.9	26.1	...	...	...	...	17.8	**24.1**
Target 2: Halve, between 1990 and 2015, the proportion of people suffering hunger											
Prevalence of child malnutrition (percent of children under 5)	41.7 (1989)	...	...	27.2	...	...	...	18.5	...	...	**21.0**
Goal 2. Achieve Universal Primary Education											
Target 3. Ensure that, by 2015, children will be able to complete a full course of primary schooling.											
Net primary enrollment ratio (percent of relevant age group)	94.6 (1998)	95.2	94.2	...	90.7	88.0	82.2	...	...	...	**100.0**
Percentage of cohort reaching grade 8	55.4 (1992)	75.6	74.7	77.3	...	...	...	...	...	...	**100.0**
Goal 3. Promote Gender Equality and Empower Women											
Target 4. Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education by 2015.											
Gender disparities at completion of primary education (in percent)	-14 (1990)	-1.9	-0.5	-1.1	-0.5	0.5	0.0	...	...	...	**0.0**
Gender disparities at completion of secondary education (in percent)	3.2 (1992)	-1.5	-1.9	-1.4	...	...	-5.3	...	...	...	**0.0**
Goal 4. Reduce Child Mortality											
Target 5. Reduce by two-thirds, between 1990 and 2015, the under five mortality rate											
Infant mortality rate (per 1,000 live births)	122.1 (1990)	54.2	51.1	48.4	46.1	44.0	42.2	40.6	39.1	...	**40.0**
Immunization against measles (percent of children 12-23 months)	53 (1990)	88.0	86.0	92.0	93.0	88.0	96.0	96.0	95.0	...	**95.0**
Goal 5. Improve Maternal Health											
Target 6. Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.											
Maternal mortality ratio (modeled estimate, per 100,000 live births)	450 (1990)	...	...	...	...	230	...	...	200	...	**128**
Proportion of births attended by skilled health personnel (in percent)	43.2 (1989)	...	...	71.1	...	...	...	...	76.2	...	**70.0**
Goal 6. Combat HIV/AIDS, Malaria, and Other Diseases											
Target 7. Halt by 2015, and begin to reverse, the spread of HIV/AIDS											
HIV prevalence, total (percent ages 15-24)	1.8 (1990)	19.2	...	...	...	...	...	...	...	...	**13.0**
Target 8. Halt by 2015, and begin to reverse, the incidence of malaria and other major diseases											
Incidence of malaria (per 1,000 people)	7.5 (1990)	5.2	...	...	2.8	3.9	...	...	...	1.6	**2.0**
Incidence of tuberculosis cases cured (in percent of diagnosed)	66 (1994)	75.0	80.0	81.0	85.0	85.0	82.0	84.0	84.0	...	**95.0**
Target 10. Halve by 2015 proportion of people without access to safe drinking water											
Access to potable water (in percent of population)	57.5 (1992)	74.1	74.4	74.6	...	...	...	...	...	82.4	**78.5**
Access to improved sanitation facilities (in percent of population)	28 (1992)	47.5	47.7	48.4	...	...	...	...	...	56.8	**64.0**
Goal 8. Develop a global Partnership for Development											
Target 18. Make available new technologies, especially information and communications											
Mobile and fixed-line telephone subscribers (per 100 people)	2.9 (1991)	37.2	40.6	59.3	72.7	79.1	89.4	98.8	105.9	104.4	**...**
Internet users (per 100 people)	0.1 (1995)	6.2	10.5	12.5	16.8	22.4	30.0	35.3	36.9	39.0	**...**

Sources: UDAPE and World Bank Development Indicators.

Annex I. External Stability Assessment

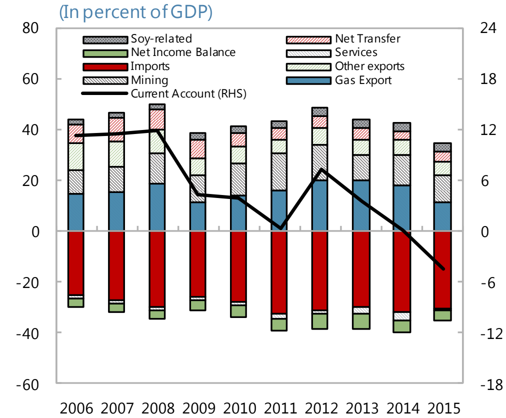
Having appreciated by over 40 percent since 2010, Bolivia's real exchange rate is assessed to be stronger than warranted by medium-term fundamentals and desirable policies as of 2015. The sharp decline in oil prices since late 2014, the dollar's appreciation, and neighboring countries' currency depreciation have weakened Bolivia's external position. The current account is expected to swing into a sizable deficit in 2015, which will only moderate gradually over the medium term. Reserves remain more than adequate by any metric but are expected to start declining. Bolivia ranks poorly in terms of competitiveness and measures of diversification and complexity. To the extent that lower gas export revenues and a more appreciated dollar will persist, Bolivia will need to regain competitiveness through facilitating relative wage and price adjustments and enhancing productivity.

Current Account

1. **The drop in oil prices is negatively impacting Bolivia's current account**. The current account is projected to post a 4.5 percent deficit in 2015 after dropping to balance in 2014 following a decade of surpluses. This is largely due to the drop in the value of natural gas exports to Brazil and Argentina, while imports remain significantly above levels seen earlier in the 2000s as the economic expansion continues. Income outflows from foreign investment in Bolivia have grown significantly during the economic expansion, while income from foreign reserves has weakened given low interest rates. Service imports, including those related to investment projects, have increased significantly over the last five years.

2. **The current account deficit appears larger than warranted by fundamentals and desirable policies.**[1] The EBA-lite methodology tailored to resource rich countries indicates a need for current account adjustment of about 2.6 percent of GDP if the large need for investment in infrastructure is considered for the case of a low-income country such as Bolivia. This translates into a real currency overvaluation of 15.6 percent. The main factors explaining the large current account gap when comparing with previous estimates are the deterioration of the current account and fiscal balances

Current Account
(In percent of GDP)



Source: Central Bank of Bolivia.

[1] Following Bems and Carvalho (2009), we include only oil and gas exporting countries in the sample, given the differences inherent in commodity exporters. The EBA-Lite CA model is estimated as a function of changes of fiscal balance, changes in reserves, capital account openness, the private credit to GDP ratio, net foreign assets, relative output per worker, the oil and gas trade balance, the dependency ratio, the GDP growth forecast, a measure of the institutional and political environment, the aid and remittances to GDP ratio, and the output gap. Further details can be found at http://www.imf.org/external/np/res/eba/data.htm.

as a result of the substantive deterioration of the terms of trade.

3. Looking ahead, the current account deficit is expected to gradually decline, although downside risks related to hydrocarbons prospects loom large. The current account deficit is expected to fall to near 3 percent of GDP by 2020, based on a modest recovery in oil prices, a small increase in the volume of gas exports to Brazil and Argentina, and a modest adjustment of domestic demand and government spending. However, further declines in export commodity prices remain a key vulnerability given the significant dependence of commodity exports (gas, mining, and soybeans account for 85 percent of total exports). Investment in exploration of hydrocarbon reserves is critical in the long term, as known reserves are expected to deplete before 2030 at current extraction rates.

Exchange Rate, Relative Prices, and Competitiveness

4. The CPI based real effective exchange rate has been appreciating since 2010 and is now stronger than warranted by medium-term fundamentals and desirable policies. Given the de facto stabilized regime against the U.S. dollar combined with dollar appreciation, the real effective exchange rate (REER) has appreciated by more than 40 percent since 2010. The appreciation has been especially sharp recently since the 2nd half of 2014 given the significant depreciations of the Brazilian real and the Argentine peso against the dollar (21 percent overall, 43 percent against the real, and 13 percent against the peso, respectively during July 2014–September 2015). Brazil and Argentina are Bolivia's most important trading partners. Overall, the EBA-lite IREER model points to about 25 percent overvaluation of the exchange rate in 2015, but is judged to be less robust than the CA approach given huge residuals. These residuals are likely related to significant structural changes in the Bolivian economy in recent years that are not well captured by the models used.

Bolivia: Exchange Rate Assessment, Model Results

	Current account norm 2/	Current account balance 2/	Gap 2/	Elasticity	REER 3/
EBA-lite methodology 1/					
CA	-1.9	-4.5	-2.6	-16.8	15.6
REER					25.0
	Current account balance 2/				
	Norm	Underlying		Elasticity	REER 3/
CGER-like methodologies 4/					
Macroeconomic balance	-1.3	-2.9		-16.8	5.0
External sustainability	0.6	-2.9		-16.8	19.9
Equilibrium real exchange rate 5/					36.3

Source: IMF staff calculations.

1/ Assessment based on information for 2015 and based on a modified EBA Lite CA regression with only oil/gas exporting countries.

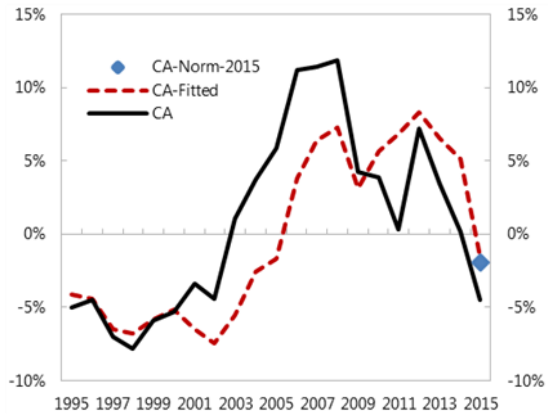
2/ Percent of GDP.

3/ Positive number indicates overvaluation.

4/ Estimated REER gap includes adjustment for multilateral consistency.

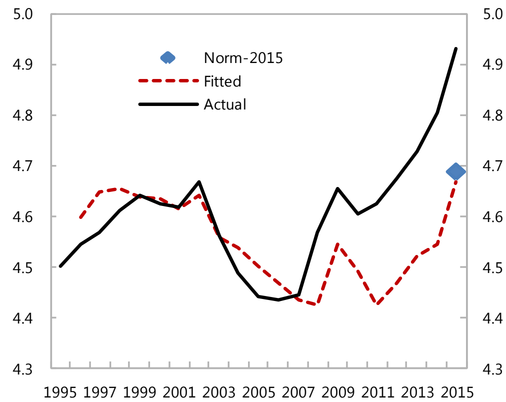
5/ Based on REER as of April 2015

Current Account: EBA-Lite Results, 1995-2015



Source: IMF staff calculations.

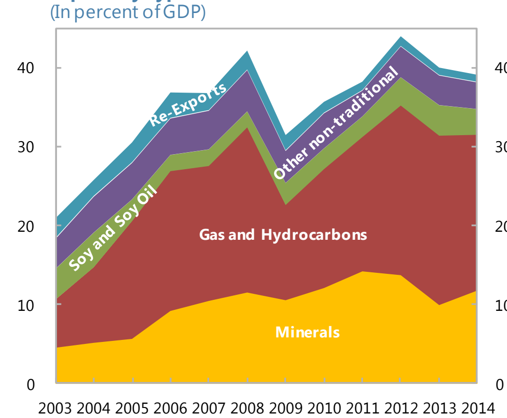
REER: EBA-Lite Results, 1995-2015



Source: IMF staff calculations.

5. Export diversification has shown some progress in recent years but remains modest. Bolivia's two main traditional export sectors (gas and minerals) have remained competitive principally because of favorable prices, their extractive nature, and the fact that hydrocarbon exports to Brazil and Argentina cannot be easily substituted because of technological reasons. Non-traditional exports increased in value but shrank as share of total exports, implying a larger dependence of the economy on exports of commodities. While the country's weak infrastructure complicates the transport of exported goods, the public sector has been promoting and succeeding with exports of specific non-traditional products, especially chestnut and quinoa. However, private domestic and foreign investments in new sectors are scarce. Notably, the non-traditional and re-export sectors did not increase their share in the economy during the last 12 years.

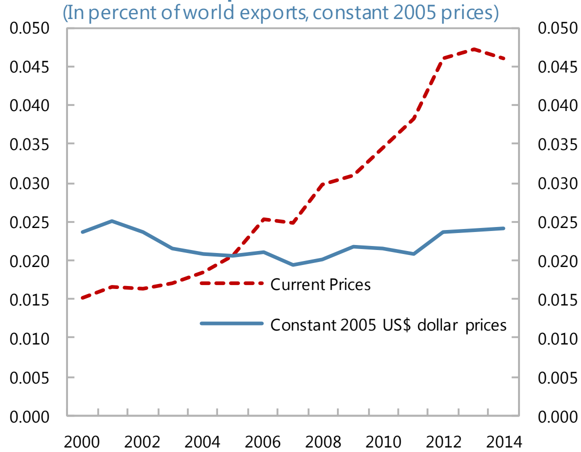
Exports by Type of Product
(In percent of GDP)



Source: Central Bank of Bolivia.

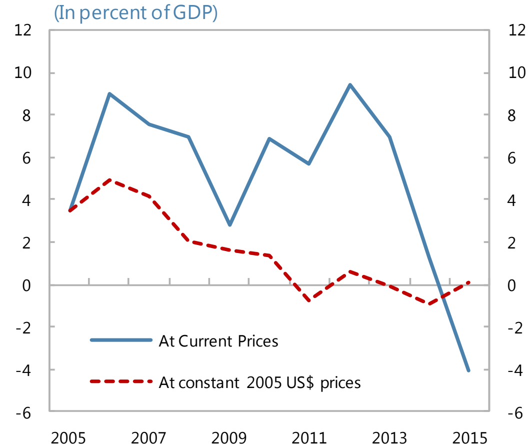
6. Bolivia's share of global exports has risen over the past decade but largely due to increasing gas export prices. The share has increased from about 0.02 percent in 2000 to about 0.05 percent in 2014. This marked upward trend has been driven by favorable price dynamics in Bolivia's main traditional export products (minerals and gas), and in its main non-traditional export product (soy). That said, Bolivia has just maintained its share of global export markets at constant 2005 U.S. dollar prices. A closer analysis of Bolivia's trade balance confirms that the trade surpluses after 2011 would have been much smaller or even deficits when valued at constant 2005 U.S. dollar prices.

Share of World Exports, 2000-14
(In percent of world exports, constant 2005 prices)



Source: IMF, World Economic Outlook; and IMF staff calculations.

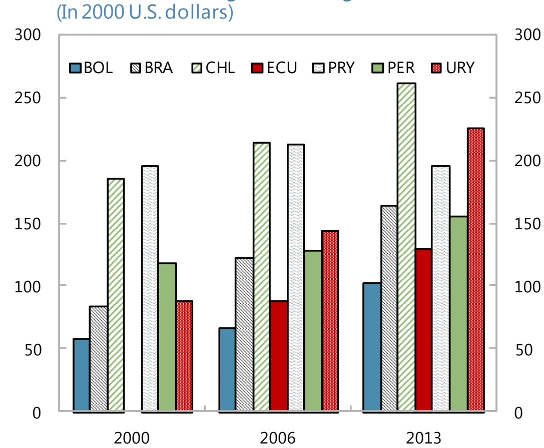
Trade Balance, 2005-14
(In percent of GDP)



Source: IMF, World Economic Outlook; and IMF staff calculations.

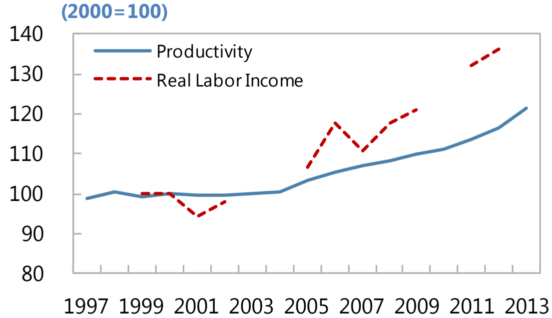
7. **Minimum and average wage growth has been fast, outpacing productivity growth**. Bolivia's minimum wage is still the lowest in the region as measured in real U.S. dollars (US$57 in 2000 and US$127 in 2015), however it grew nearly 80 percent during 2000–2013, just surpassed in Brazil (about 100 percent) and in Uruguay (over 150 percent) over the same period. While this had important positive effects on poverty, it has also increased labor costs of non-commodity exports and led to wage growth outpacing productivity growth over the last decade. This has adversely affected the competitiveness of the country. The distribution of wage growth seems to favor low-skill workers; indeed, annualized real wage growth for high-skill workers was negative during 2000–2012 (-2 percent).

Real Minimum Wages in the Region
(In 2000 U.S. dollars)



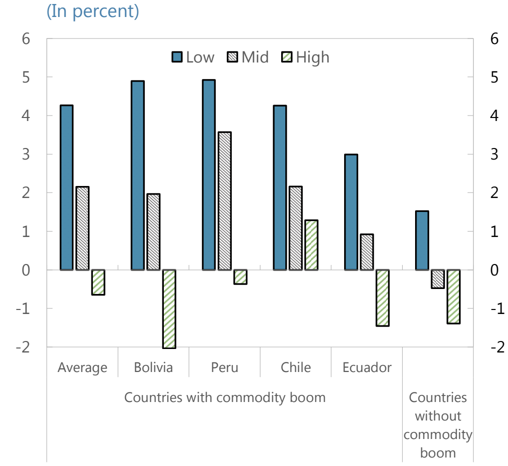
Sources: ECLAC, ILO and IMF staff calculations.

Bolivia: Labor Productivity and Real Labor Income 1/
(2000=100)



1/ Labor productivity refers to real GDP per employed person.
Source: WDI and SEDLAC, World Bank and IMF staff calculations.

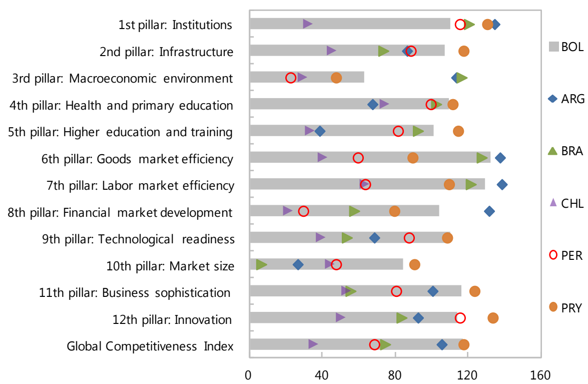
Annualized Real Wage Growth by Education Level
(In percent)



Source: SEDLAC (CEDLAS and the World Bank).

8. Other structural indicators of competitiveness point to a weak position with respect to other countries in the region. The only category where Bolivia is in the top half of the Global Competitiveness indicators is Macroeconomic Environment. The major constraints for competitiveness seem to be Goods Markets Efficiency and Labor Market Efficiency, where Bolivia ranks in the positions 132 and 129 out of 140 countries, respectively. Addressing longstanding weaknesses in logistic performance would also help boost trade and competitiveness. In the 2014 Logistics Performance Index of the World Bank, Bolivia ranked 121 out of 160 countries; well below neighboring countries. Transport infrastructure; ease of arranging shipments; logistics services quality; tracking and tracing; and timeliness all scored below regional peers.

Competitiveness Indicators 1/



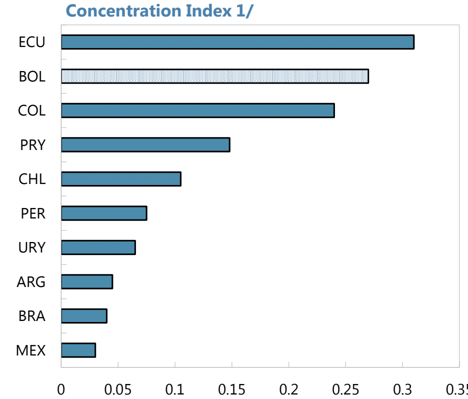
Source: World Economic Forum, Global Competitiveness Report.
1/ Ranking among 140 countries.

Logistics Performance Index and Components

Source: World Bank.

9. Recent research by the IMF indicates that Bolivia ranks poorly in terms of economic diversification and complexity. More specifically, the range of produced goods is narrow, and their level of sophistication remains low, two factors that have been found important for long-term growth. Bolivia ranks low also relative to its regional neighbors in terms of product concentration. Infrastructure, education, and market openness are keys to inducing greater sophistication.

Herfindahl-Hirschman Product Concentration Index 1/

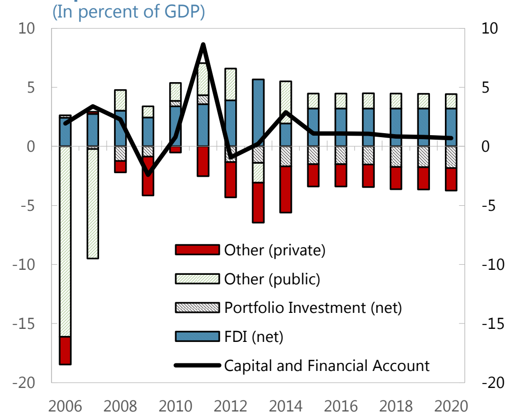


SourceWorld Integrated Trade Solution (WTIS).
1/ Measures dispersion of trade value acroos export products. More trade value concentration in exports has index closer to 1.

Capital Flows, Reserves, and the International Investment Position

10. The capital account registered a small surplus in 2014 and is expected to remain in surplus in the medium term. Bolivia attracted sizable foreign direct investment and official financing in 2014. Portfolio outflows have been driven by commercial bank's required liquid asset (RAL) abroad. Other capital outflows (private) have also significantly increased in 2013 and 2014. Looking ahead, the capital account is projected to register small surpluses given a continuation of these trends.

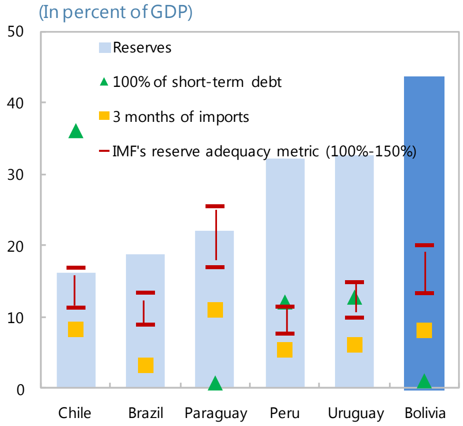
Capital Flows, 2006-2020
(In percent of GDP)



Source: IMF staff calculations based on national authorities' data.

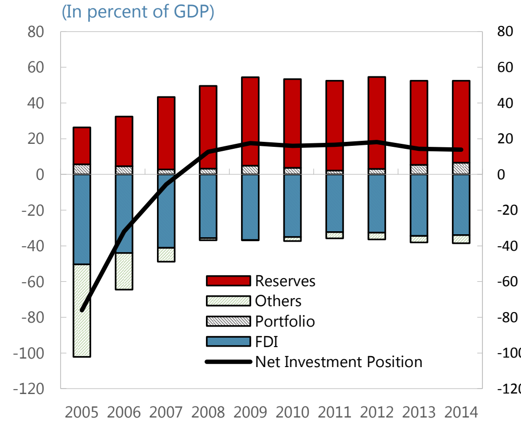
11. International Reserves remain well above various metrics of reserve adequacy, providing ample buffers, although they are expected to decline in the medium term. Reserve coverage is equivalent to 14 months of imports and is substantially above the adequacy threshold suggested by short-term debt or broad money. Substantial accumulated assets represent both savings of the exhaustible resource revenues and protection against vulnerabilities from oil price volatility. Looking ahead, staff expects reserves to decline to around US$6¾ billion by 2020 given current account deficits and decreased net capital flows. This should still be reasonably adequate level, although in terms of broad money it will fall to 20 percent. The net international investment position has remained positive since 2008, standing at 13.7 of GDP at end-2014, with external assets are dominated by international reserves.

Adequacy of International Reserves, 2014
(In percent of GDP)



Source: IMF staff calculations based on national authorities' data.

International Investment Position
(In percent of GDP)



Source: Haver Analytics, Inc..

Annex II. Financial Stability Assessment for Bolivia

1. **Financial Soundness Indicators suggest vulnerabilities have increased to "medium" in the first half of 2015, driven by an increasing credit-to-GDP ratio**. However, banks' balance sheets remain healthy with low balance sheet structural risks and strong buffers. The deposit-to-loan ratio remains high, while foreign exchange exposure is limited given low deposit and credit dollarization. The leverage ratio and profitability remain at acceptable levels, and non-performing loans are low. Looking ahead, the financial services law may lead to new risks building up, and vigilance regarding asset quality and the speed of credit growth needs to be maintained.

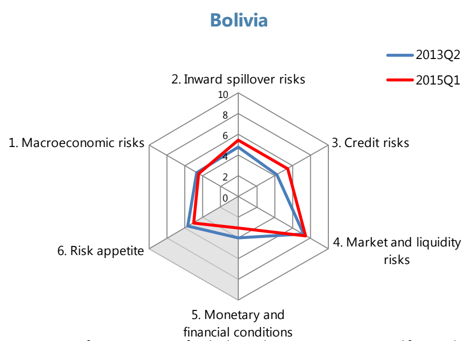
Financial Soundness Indicators Vulnerability Heatmap

Bolivia	2012Q4	2013Q1	2013Q2	2013Q3	2013Q4	2014Q1	2014Q2	2014Q3	2014Q4	2015Q1	2015Q2
Overall Financial Sector Rating	L	L	L	L	L	L	L	L	L	M	M
Credit cycle	L	L	L	L	L	L	L	L	L	M	M
Change in credit / GDP ratio (pp, annual)	2.2	1.9	2.0	1.6	2.0	2.0	2.0	1.8	2.8	3.6	3.7
Growth of credit / GDP (%, annual)	6.0	5.1	5.3	4.1	5.1	5.3	5.0	4.5	6.8	8.8	8.9
Credit-to-GDP gap (st. dev)	-0.8	-1.3	-0.6	-1.0	-0.8	-1.4	-0.6	-0.8	0.3	0.2	1.4
Balance Sheet Soundness	L	L	L	L	L	L	L	L	L	L	L
Balance Sheet Structural Risk	L	L	L	L	L	L	L	L	L	L	L
Deposit-to-loan ratio	124.6	122.5	117.4	116.2	121.3	119.6	115.4	117.7	122.8	118.7	119.2
FX liabilities % (of total liabilities)	28.0	28.1	27.1	25.3	22.9	23.6	23.1	20.1	18.6	19.6	19.1
FX loans % (of total loans)	19.6	17.8	15.4	13.8	12.0	10.1	9.4	7.2	6.3	5.8	4.9
Balance Sheet Buffers	L	L	L	L	L	L	L	L	L	L	L
Leverage	L	L	L	L	L	L	L	L	L	L	L
Leverage ratio (%)	8.6	8.4	8.5	8.5	8.2	8.1	8.2	8.2	8.2	7.7	7.7
Profitability	L	L	L	L	L	L	L	L	L	L	L
ROA	1.4	0.8	0.9	1.0	1.1	1.1	1.2	1.2	1.2	1.1	1.0
ROE	17.6	10.8	11.4	12.5	14.2	15.1	15.7	16.0	15.7	14.8	13.8
Asset quality	L	L	L	L	L	L	L	L	L	L	L
NPL ratio	1.5	1.6	1.6	1.6	1.5	1.6	1.5	1.6	1.5	1.7	1.6
NPL ratio change (%, annual)	-9.1	-7.6	-5.4	-5.2	1.3	3.1	-5.0	-1.2	-1.3	4.3	4.0

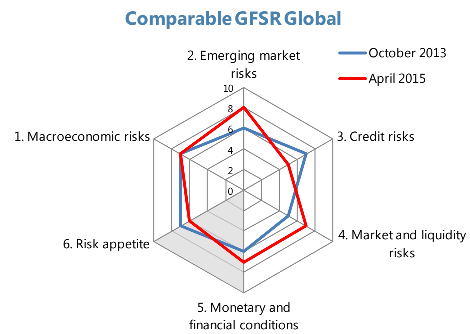
Vulnerability codes:
- High
- Moderate
- Low

Sources: Fund staff estimates based on authorities data.

2. Bolivia's financial stability map does not show a significant increase in risks when compared with the period before the introduction of the financial services law in 2013. Inward spillover risks have increased marginally, reflecting the external vulnerability related to the commodity price decline and a high concentration of exports. Credit risks have also increased, mainly because of a slight increase in non-performing loans and a decrease in banks' profitability. The level of overall macro-economic risks for Bolivia is lower than the level of global risks reported in the April 2015 Global Financial Stability Report.



Note: Away from center signifies higher risks, easier monetary and financial conditions, or higher risk appetite.



Note: Away from center signifies higher risks, easier monetary and financial conditions, or higher risk appetite.

Annex III. Debt Sustainability Analysis[1]

Bolivia shows low risk of debt distress for total and external public debt under the current baseline scenario. Under the baseline scenario, debt ratios remain below the respective risk thresholds even under extreme shocks. However, debt sustainability depends on the authorities' fiscal consolidation efforts in response to lower hydrocarbon revenues. Moreover, there are downside risks related to uncertainty surrounding hydrocarbons production and discovery of natural gas reserves. An alternative scenario, which assumes no augmentation of current proven natural gas reserves and a shorter resource horizon up to the mid-2020s, indicates higher risk of debt distress, with total public sector debt breaching the debt distress threshold by 2025.

BACKGROUND

1. The decline in Bolivia's gross public debt stalled in 2014, and the ratio is projected to continue rising as the drop in international oil prices reduces hydrocarbon revenues significantly. Bolivia has successfully reduced its public debt as a share of GDP from 95.7 percent in 2003 to 32.5 percent in 2013, supported by MDRI debt relief, consecutive fiscal surpluses, and strong economic growth. The trend reversed in 2014 as Bolivia recorded the first fiscal deficit in nine years, with the debt increasing slightly to 33.0 percent of GDP. The increase is projected to continue while the authorities undergo gradual fiscal adjustments, and total public debt is estimated to stabilize at around 48 percent of GDP by 2020. External debt has declined significantly to 17.3 percent in 2014 from 65.0 percent in 2003, and the share of foreign currency debt in domestic debt declined to 10.8 percent from 82.5 percent over the same period. The commodity price boom and a limited capacity to execute capital expenditure have lead to a sizable accumulation of public sector deposits at the central bank, providing some buffers.

BASELINE SCENARIO

2. The main assumptions of the baseline scenario for the period of 2015–2035 are:

- ***Annual real GDP growth***: 4.1 percent in 2015 and 3.5 percent thereafter through 2020 (staff's estimate of potential growth). Output growth is assumed to continue to decelerate to a little above 3 percent by 2035, reflecting slowing population growth and more moderate capital accumulation.

- ***Inflation (CPI, period average):*** 4.3 percent in 2015, 4.9 percent in 2016, and 5 percent in 2017–2035.

[1] While remittances are an important source of foreign exchange, their contribution is not high enough to require their inclusion in the DSA.

- ***External sector:*** in line with the staff's medium-term projections through 2020, and based on stable import and export ratios to GDP over the long term. Net FDI is assumed to remain stable at around 3 percent of GDP.

- ***Fiscal assumptions and financing strategy:*** in line with the staff's medium-term projection through 2020. For 2021–35, a primary deficit of around 2 percent of GDP is assumed on average, on the basis of a stable path of international oil prices and gradual adjustments in non-hydrocarbons fiscal balances in response to persistently low oil prices. External financing is assumed to account for about 25 percent of financing needs, with CAF expected to remain the largest external lender.

- ***Average concessionality of public external debt:*** around 20 percent in the long term, based on projected disbursements of official loans and concessional financing conditions.

3. Under the baseline scenario, Bolivia's public and external debt are expected to remain stable throughout the projection period. Bolivia is classified as medium performer in terms of its policy and institutional capacity, measured by the three year average of the World Bank's Country Policy and Institutional Assessment (CPIA) scores. The gross non-financial sector public debt is projected to increase to 46.2 percent of GDP in PV terms by 2020 and to a peak of 48.4 percent in 2028, before declining to 45.5 percent in 2035, remaining below the threshold of 56 percent. Total external debt (including private) is projected to peak at 18.9 percent of GDP in PV terms in 2021, and then decline to 13.8 percent by 2035. All the debt burden indicators for Bolivia are below the specific indicative thresholds for medium performers.

4. Standard stress tests on the baseline scenario suggest that Bolivia's low public and external indebtedness is resilient to the majority of shocks. Under the most extreme stress test to external debt—a onetime 30 percent nominal depreciation relative to the baseline in 2016—the ratio of the PV of debt to GDP deteriorates by around 6¾ percentage points on impact, and the gap remains in large part in the medium to long term. All the external debt indicators remain well below the threshold in the extreme stress scenarios. For public debt, the PV of debt to GDP breaches the threshold under the scenario in which the primary balance is assumed to remain in a deficit of 4.2 percent from 2015 onwards. The stress tests, however, indicate that debt ratios remain below indicative thresholds even for the extreme shock of an increase in other debt-creating flows in 2016 equivalent to 10 percent of GDP.

ALTERNATIVE SCENARIO

5. Bolivia's risk of debt distress is low under the baseline scenario but there are downside risks related to uncertainty surrounding hydrocarbons production. Based on the analysis under the baseline and the most extreme stress test, staff believes that Bolivia's risk of debt distress is low, and its debt is expected to be sustainable over the medium and long term. Nevertheless, it should be noted that debt sustainability will depend on the authorities' fiscal consolidation efforts in response to lower hydrocarbon revenues, and investment for exploration and successful discovery of natural gas reserves.

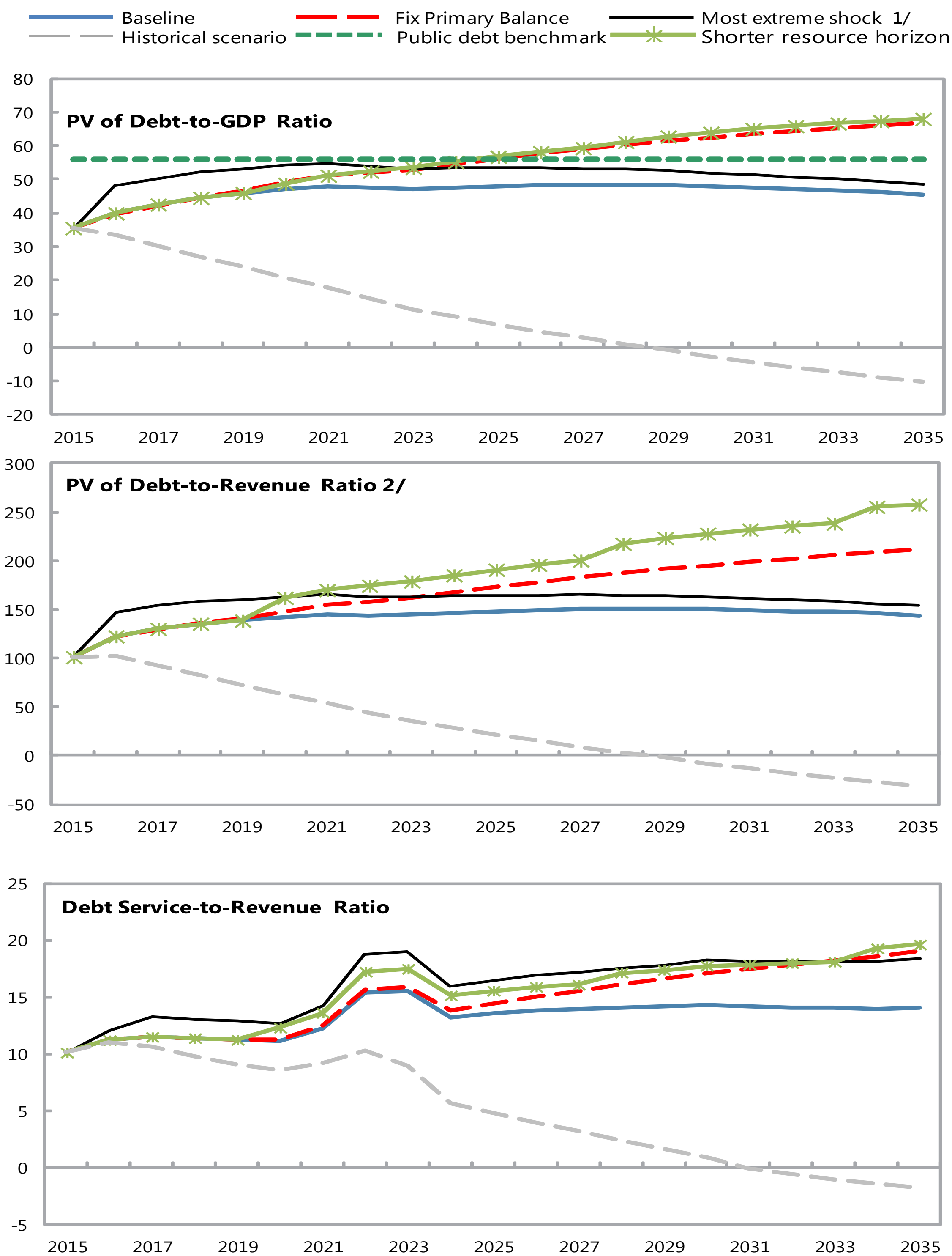
6. To assess the impact of the exhaustion of natural gas reserves, the following assumptions are made under an alternative scenario with a shorter resource horizon:

- **Natural gas resource horizon**: Given the uncertainty and length of time natural gas exploration takes, an alternative scenario assesses the debt sustainability implications of a shorter resource horizon only based on current proven reserves. Current reserves are expected to last only through 2025, based on staff's medium-term production assumptions under the baseline scenario. The alternative scenario, therefore, assumes that the long-term export contract with Brazil will not be renewed after 2019 and the production volume will drop in 2020, resulting in a continued production for Argentina (until the end of current contract in 2027) and domestic use until 2033. The authorities have increased efforts to explore natural gas reserves, including through drafting decrees setting investment regimes for the hydrocarbons sector, and this scenario could be viewed as the upper bound for the debt sustainability risks.

- ***Fiscal assumptions:*** With the assumed loss of hydrocarbons related revenues, the primary deficit of the non-financial public sector is assumed to average around 5¾ percent of GDP in 2020–35.

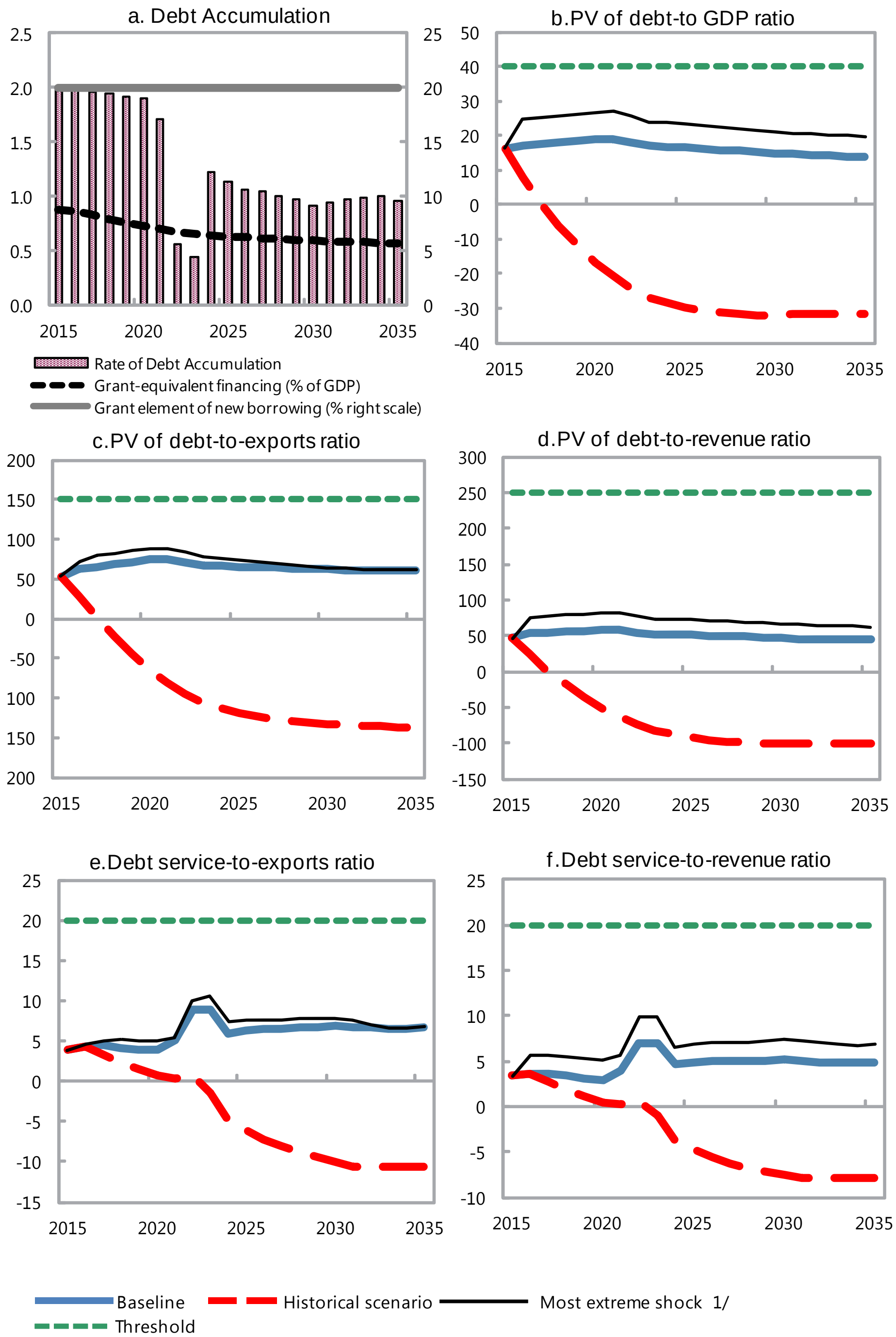
7. Under the shorter resource horizon scenario, the debt trajectory starts to worsen from mid-2020s, reflecting the assumed exhaustion of current proven gas reserves. The PV of the public debt-to-GDP ratio is projected to breach the threshold in 2025 and continue to rise, reflecting primary deficits. The public debt-to-GDP ratio, in nominal terms, could reach around 85 percent of GDP by 2035.

Figure 1. Bolivia: Indicators of Public Debt Under Alternative Scenarios, 2015–2035[1/]



Sources: Country authorities; and staff estimates and projections.
1/ The most extreme stress test is the test that yields the highest ratio on or before 2025.
2/ Revenues are defined inclusive of grants.

Figure 2. Bolivia: Indicators of Public and Publicly Guaranteed External Debt under Alternative Scenarios, 2015–2035[1/]



Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio on or before 2025. In figure b. it corresponds to a One-time depreciation shock; in c. to a Non-debt flows shock; in d. to a One-time depreciation shock; in e. to a Non-debt flows shock and in figure f. to a One-time depreciation shock

Table 1a. Bolivia: Public Sector Debt Sustainability Framework, Baseline Scenario, 2012–2035

(In percent of GDP, unless otherwise indicated)

	Actual					Estimate	Projections								
	2012	2013	2014	Average 5/	Standard Deviation 5/	2015	2016	2017	2018	2019	2020	2015-20 Average	2025	2035	2021-35 Average
Public sector debt 1/	33.3	32.5	33.0			38.0	42.0	44.1	45.8	46.8	47.6		48.5	45.7	
of which: foreign-currency denominated	18.5	19.1	19.0			20.7	21.8	22.0	22.2	22.4	22.3		20.3	17.5	
Change in public sector debt	-1.3	-0.8	0.5			5.0	4.0	2.2	1.6	1.1	0.7		0.1	-0.7	
Identified debt-creating flows	-5.6	-4.5	0.0			5.0	4.0	2.2	1.6	1.1	0.7		0.1	-0.7	
Primary deficit	-2.9	-1.6	2.4	-2.7	2.6	4.2	4.6	4.2	3.8	3.3	3.0	3.9	2.4	1.3	2.1
Revenue and grants	37.8	39.1	39.9			35.1	32.6	32.7	32.9	33.2	33.1		32.4	31.5	
of which: grants	0.7	0.3	0.3			0.3	0.3	0.2	0.2	0.2	0.2		0.2	0.1	
Primary (noninterest) expenditure	34.9	37.5	42.3			39.4	37.2	36.9	36.7	36.4	36.1		34.9	32.9	
Automatic debt dynamics	-2.8	-2.9	-1.3			0.8	-0.7	-2.1	-2.2	-2.2	-2.3		-2.3	-2.0	
Contribution from interest rate/growth differential	-1.9	-2.2	-1.2			0.0	-0.7	-1.5	-1.6	-1.7	-1.7		-1.7	-1.5	
of which: contribution from average real interest rate	-0.2	0.0	0.5			1.3	0.6	-0.1	-0.1	-0.2	-0.1		-0.1	-0.1	
of which: contribution from real GDP growth	-1.7	-2.1	-1.7			-1.3	-1.3	-1.4	-1.5	-1.5	-1.6		-1.6	-1.4	
Contribution from real exchange rate depreciation	-0.9	-0.7	-0.1			0.8	0.0	-0.6	-0.5	-0.5	-0.5		...	...	
Other identified debt-creating flows	0.0	0.0	-1.1			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Privatization receipts (negative)	0.0	0.0	-1.1			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Debt relief (HIPC and other)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Residual, including asset changes	4.3	3.7	0.5			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Other Sustainability Indicators															
PV of public sector debt	...	...	30.1			35.5	39.9	42.5	44.6	46.0	47.1		48.0	45.5	
of which: foreign-currency denominated	...	...	16.0			18.3	19.7	20.4	21.0	21.5	21.9		19.8	17.2	
of which: external	...	...	14.3			16.2	17.3	17.7	18.1	18.5	18.8		16.4	13.8	
PV of contingent liabilities (not included in public sector debt)	...	...	...			...	...	...	...	...	...		...	...	
Gross financing need 2/	1.9	3.1	6.5			7.8	8.3	8.0	7.6	7.0	6.7		6.8	5.8	
PV of public sector debt-to-revenue and grants ratio (in percent)	...	...	75.4			101.2	122.6	130.1	135.5	138.7	142.3		148.0	144.1	
PV of public sector debt-to-revenue ratio (in percent)	...	...	75.9			102.0	123.6	131.1	136.5	139.6	143.2		148.8	144.7	
of which: external 3/	...	...	36.2			46.4	53.4	54.7	55.6	56.2	57.3		50.8	43.9	
Debt service-to-revenue and grants ratio (in percent) 4/	11.8	11.4	10.2			10.1	11.2	11.5	11.4	11.2	11.2		13.6	14.0	
Debt service-to-revenue ratio (in percent) 4/	12.0	11.5	10.3			10.2	11.3	11.6	11.5	11.3	11.2		13.6	14.1	
Primary deficit that stabilizes the debt-to-GDP ratio	-1.5	-0.8	1.9			-0.8	0.7	2.1	2.2	2.2	2.3		2.3	2.0	
Key macroeconomic and fiscal assumptions															
Real GDP growth (in percent)	5.1	6.8	5.5	5.0	1.0	4.1	3.5	3.5	3.5	3.5	3.5	3.6	3.5	3.1	3.3
Average nominal interest rate on forex debt (in percent)	2.7	2.8	2.8	3.5	1.0	2.7	2.6	2.5	2.4	2.4	2.3	2.5	3.1	3.2	3.2
Average real interest rate on domestic debt (in percent)	-2.3	-1.8	1.8	-1.2	4.8	7.1	2.3	-0.9	-0.9	-0.8	-0.8	1.0	-1.1	-1.1	-1.1
Real exchange rate depreciation (in percent, + indicates depreciation	-5.0	-4.3	-0.6	-6.3	5.5	4.2	...	...	...	...	...	...	...	...	...
Inflation rate (GDP deflator, in percent)	7.1	6.0	2.0	7.3	5.1	-3.1	1.5	4.8	4.8	4.7	4.6	2.9	5.0	5.0	5.0
Growth of real primary spending (deflated by GDP deflator, in percer	8.3	14.5	19.1	4.2	7.2	-3.1	-2.1	2.6	2.8	2.9	2.5	0.9	2.9	2.5	2.7
Grant element of new external borrowing (in percent)	...	...	...	...	...	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	...

Sources: Country authorities; and staff estimates and projections.

1/Non financial public sector gross debt.

2/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period.

3/ Revenues excluding grants.

4/ Debt service is defined as the sum of interest and amortization of medium and long-term debt.

5/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 1b. Bolivia: Sensitivity Analysis for Key Indicators of Public Debt, 2015–2035

	Projections							
	2015	2016	2017	2018	2019	2020	2025	2035
PV of Debt-to-GDP Ratio								
Baseline	36	40	43	45	46	47	48	45
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	36	33	30	27	24	21	7	-10
A2. Primary balance is unchanged from 2015	36	40	42	45	47	49	56	67
A3. Permanently lower GDP growth 1/	36	40	43	45	47	48	52	56
A4. Alternative Scenario : Shorter resource horizon	36	40	43	45	46	49	57	68
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2016-20	36	40	42	43	45	46	45	42
B2. Primary balance is at historical average minus one standard deviations in 2016-201	36	36	35	38	39	41	43	43
B3. Combination of B1-B2 using one half standard deviation shocks	36	35	33	34	36	37	37	35
B4. One-time 30 percent real depreciation in 2016	36	48	50	52	53	54	53	50
B5. 10 percent of GDP increase in other debt-creating flows in 2016	36	48	50	52	53	54	53	48
PV of Debt-to-Revenue Ratio 2/								
Baseline	101	123	130	136	139	142	148	144
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	101	103	92	82	72	63	21	-32
A2. Primary balance is unchanged from 2015	101	122	129	136	141	148	173	212
A3. Permanently lower GDP growth 1/	101	123	131	137	141	146	159	179
A4. Alternative Scenario : Shorter resource horizon	101	123	130	136	139	162	191	258
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2016-20	101	122	128	132	135	138	140	132
B2. Primary balance is at historical average minus one standard deviations in 2016-201	101	111	108	115	119	123	133	135
B3. Combination of B1-B2 using one half standard deviation shocks	101	107	100	105	108	111	115	110
B4. One-time 30 percent real depreciation in 2016	101	147	153	157	159	163	164	158
B5. 10 percent of GDP increase in other debt-creating flows in 2016	101	147	154	158	160	163	164	154
Debt Service-to-Revenue Ratio 2/								
Baseline	10	11	11	11	11	11	14	14
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	10	11	11	10	9	9	5	-2
A2. Primary balance is unchanged from 2015	10	11	11	11	11	11	14	19
A3. Permanently lower GDP growth 1/	10	11	12	11	11	11	14	17
A4. Alternative Scenario : Shorter resource horizon	10	11	11	11	11	12	16	20
B. Bound tests								
B1. Real GDP growth is at historical average minus one standard deviations in 2016-20	10	11	11	11	11	11	13	13
B2. Primary balance is at historical average minus one standard deviations in 2016-201	10	11	11	11	11	11	12	13
B3. Combination of B1-B2 using one half standard deviation shocks	10	11	11	10	10	10	10	11
B4. One-time 30 percent real depreciation in 2016	10	12	13	13	13	13	16	18
B5. 10 percent of GDP increase in other debt-creating flows in 2016	10	11	12	12	12	12	16	15

Sources: Country authorities; and staff estimates and projections.

1/ Assumes that real GDP growth is at baseline minus one standard deviation divided by the square root of the length of the projection period.

2/ Revenues are defined inclusive of grants.

Table 2a. Bolivia: External Debt Sustainability Framework, Baseline Scenario, 2012–2035[1/]

	Actual			Historical [6/]	Standard [6/]	Projections									
				Average	Deviation							2015-2020			2021-2035
	2012	2013	2014			2015	2016	2017	2018	2019	2020	Average	2025	2035	Average
External debt (nominal) 1/	**18.6**	**19.7**	**19.9**			**21.3**	**21.9**	**22.0**	**22.0**	**22.0**	**21.9**		**19.5**	**16.7**	
of which: public and publicly guaranteed (PPG)	15.7	17.0	17.3			18.6	19.3	19.3	19.4	19.4	19.3		16.9	14.1	
Change in external debt	0.0	1.0	0.2			1.4	0.7	0.0	0.0	0.0	-0.1		-0.5	-0.2	
Identified net debt-creating flows	-13.3	-11.3	-3.4			-0.4	0.6	0.2	-0.4	-0.6	-1.0		-2.6	-2.8	
Non-interest current account deficit	**-7.6**	**-3.8**	**-0.6**	**-6.7**	**4.6**	**4.0**	**4.6**	**3.7**	**3.1**	**2.9**	**2.5**		**0.8**	**0.5**	0.7
Deficit in balance of goods and services	-8.6	-5.5	-2.0			4.4	4.6	3.6	2.9	2.5	2.0		1.4	1.4	
Exports	44.9	41.3	40.6			30.7	27.5	27.1	26.7	26.2	25.5		25.0	23.0	
Imports	36.4	35.8	38.7			35.1	32.1	30.8	29.6	28.7	27.5		26.4	24.4	
Net current transfers (negative = inflow)	-4.6	-4.1	-3.3	-6.0	1.9	-3.8	-3.7	-3.5	-3.3	-3.1	-2.9		-2.3	-1.5	-2.0
of which: official	-0.8	-0.6	-0.1			-0.3	-0.3	-0.2	-0.2	-0.2	-0.2		-0.1	-0.1	
Other current account flows (negative = net inflow)	5.6	5.8	4.7			3.5	3.6	3.6	3.5	3.4	3.4		1.7	0.6	
Net FDI (negative = inflow)	**-3.9**	**-5.7**	**-1.9**	**-2.6**	**2.2**	**-4.1**	**-3.7**	**-3.2**	**-3.2**	**-3.2**	**-3.2**		**-3.2**	**-3.2**	-3.2
Endogenous debt dynamics 2/	**-1.8**	**-1.8**	**-0.9**			**-0.3**	**-0.2**	**-0.3**	**-0.3**	**-0.3**	**-0.3**		**-0.1**	**0.0**	
Contribution from nominal interest rate	0.3	0.4	0.5			0.5	0.5	0.5	0.4	0.4	0.4		0.5	0.4	
Contribution from real GDP growth	-0.8	-1.1	-1.0			-0.8	-0.7	-0.7	-0.7	-0.7	-0.7		-0.6	-0.5	
Contribution from price and exchange rate changes	-1.3	-1.1	-0.4			...	...	...	...	...	...		...	...	
Residual (3-4) 3/	**13.3**	**12.3**	**3.6**			**1.8**	**0.0**	**-0.2**	**0.4**	**0.6**	**0.9**		**2.1**	**2.6**	
of which: exceptional financing	0.0	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
PV of external debt 4/	...	...	17.0			18.8	19.9	20.4	20.8	21.2	21.5		19.0	16.4	
In percent of exports	...	...	41.7			61.2	72.4	75.1	77.8	80.7	84.3		76.0	71.5	
PV of PPG external debt	**...**	**...**	**14.3**			**16.2**	**17.3**	**17.7**	**18.1**	**18.5**	**18.8**		**16.4**	**13.8**	
In percent of exports	**...**	**...**	**35.2**			**52.6**	**62.8**	**65.3**	**67.9**	**70.6**	**74.0**		**65.4**	**60.0**	
In percent of government revenues	**...**	**...**	**36.2**			**46.4**	**53.4**	**54.7**	**55.6**	**56.2**	**57.3**		**50.8**	**43.9**	
Debt service-to-exports ratio (in percent)	**6.4**	**6.0**	**6.1**			**6.2**	**6.9**	**7.0**	**6.8**	**6.7**	**6.6**		**9.0**	**9.8**	
PPG debt service-to-exports ratio (in percent)	**4.3**	**5.1**	**4.4**			**3.9**	**4.3**	**4.4**	**4.2**	**4.0**	**3.8**		**6.2**	**6.7**	
PPG debt service-to-revenue ratio (in percent)	**5.2**	**5.4**	**4.5**			**3.4**	**3.7**	**3.7**	**3.4**	**3.2**	**3.0**		**4.8**	**4.9**	
Total gross financing need (Billions of U.S. dollars)	-2.0	-1.8	0.2			0.9	1.2	1.2	1.0	1.0	0.8		0.4	0.4	
Non-interest current account deficit that stabilizes debt ratio	-7.6	-4.9	-0.8			2.7	3.9	3.7	3.1	2.8	2.6		1.3	0.7	
Key macroeconomic assumptions															
Real GDP growth (in percent)	5.1	6.8	5.5	5.0	1.0	4.1	3.5	3.5	3.5	3.5	3.5	3.6	3.5	3.1	3.3
GDP deflator in US dollar terms (change in percent)	7.5	6.0	2.0	9.0	6.2	-3.1	1.5	4.8	4.8	4.7	4.6	2.9	5.0	5.0	5.0
Effective interest rate (percent) 5/	2.1	2.4	2.6	2.7	0.6	2.5	2.4	2.3	2.2	2.1	2.0	2.2	2.8	2.8	2.9
Growth of exports of G&S (US dollar terms, in percent)	32.7	4.1	5.8	19.6	19.1	-23.7	-6.0	7.1	6.8	6.2	5.3	-0.7	7.7	7.3	7.8
Growth of imports of G&S (US dollar terms, in percent)	8.2	11.5	16.2	19.2	13.7	-8.5	-3.8	3.9	4.4	5.0	3.7	0.8	7.8	7.4	7.6
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0
Government revenues (excluding grants, in percent of GDP)	37.1	38.8	39.6			34.8	32.3	32.4	32.6	32.9	32.9		32.3	31.4	32.0
Aid flows (in Billions of US dollars) 7/	0.3	0.2	0.2			0.1	0.1	0.1	0.1	0.1	0.1		0.1	0.2	
of which: Grants	0.2	0.1	0.1			0.1	0.1	0.1	0.1	0.1	0.1		0.1	0.2	
of which: Concessional loans	0.1	0.1	0.1			0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Grant-equivalent financing (in percent of GDP) 8/	...	...	...			0.9	0.9	0.8	0.8	0.8	0.7		0.6	0.6	0.6
Grant-equivalent financing (in percent of external financing) 8/	...	...	...			26.8	26.5	26.4	26.3	26.2	26.1		25.6	24.4	25.2
Memorandum items:															
Nominal GDP (Billions of US dollars)	27.3	30.9	33.2			33.5	35.2	38.2	41.4	44.9	48.6		73.7	165.4	
Nominal dollar GDP growth	13.0	13.2	7.6			0.9	5.0	8.5	8.4	8.4	8.3	6.6	8.7	8.2	8.5
PV of PPG external debt (in Billions of US dollars)			4.8			5.4	6.1	6.8	7.5	8.3	9.2		12.1	22.8	
(PVt-PVt-1)/GDPt-1 (in percent)						2.0	2.0	2.0	1.9	1.9	1.9	1.9	1.1	1.0	1.0
Gross workers' remittances (Billions of US dollars)	1.0	1.1	1.1			1.2	1.2	1.2	1.3	1.3	1.3		1.6	2.3	
PV of PPG external debt (in percent of GDP + remittances)	...	...	13.9			15.6	16.7	17.2	17.6	18.0	18.4		16.0	13.6	
PV of PPG external debt (in percent of exports + remittances)	...	...	32.7			47.1	55.8	58.4	60.9	63.7	66.9		60.3	56.5	
Debt service of PPG external debt (in percent of exports + remittanc	...	...	4.0			3.5	3.9	3.9	3.7	3.6	3.5		5.7	6.3	

Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as [r - g - ρ(1+g)]/(1+g+ρ+gρ) times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and ρ = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that PV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

7/ Defined as grants, concessional loans, and debt relief.

8/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

Table 2b. Bolivia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed Debt, 2015–2035

(In percent)

	Projections							
	2015	2016	2017	2018	2019	2020	**2025**	2035
PV of debt-to GDP ratio								
Baseline	16	17	18	18	19	19	**16**	14
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	16	8	0	-6	-12	-17	**-30**	-32
A2. New public sector loans on less favorable terms in 2015-2035 2	16	18	19	20	20	21	**20**	20
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	16	17	18	18	18	19	**16**	14
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	16	16	16	17	17	17	**16**	14
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	16	17	18	18	19	19	**17**	14
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	16	20	22	22	22	23	**18**	14
B5. Combination of B1-B4 using one-half standard deviation shocks	16	13	9	10	10	11	**12**	13
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	16	25	25	26	26	27	**23**	20
PV of debt-to-exports ratio								
Baseline	53	63	65	68	71	74	**65**	60
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	53	28	1	-23	-45	-65	**-119**	-138
A2. New public sector loans on less favorable terms in 2015-2035 2	53	65	69	73	78	83	**80**	85
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	53	63	65	68	71	74	**65**	60
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	53	54	60	62	65	68	**62**	60
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	53	63	65	68	71	74	**65**	60
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	53	72	80	83	85	88	**73**	61
B5. Combination of B1-B4 using one-half standard deviation shocks	53	43	30	33	35	38	**41**	49
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	53	63	65	68	71	74	**65**	60
PV of debt-to-revenue ratio								
Baseline	46	53	55	56	56	57	**51**	44
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	46	24	1	-19	-36	-51	**-92**	-101
A2. New public sector loans on less favorable terms in 2015-2035 2	46	55	58	60	62	64	**62**	62
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	46	53	54	55	56	57	**50**	44
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	46	49	50	51	52	53	**49**	44
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	46	53	55	56	57	58	**51**	44
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	46	61	67	68	68	68	**57**	44
B5. Combination of B1-B4 using one-half standard deviation shocks	46	41	28	30	32	33	**36**	40
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	46	76	78	79	80	81	**72**	62

Table 2b. Bolivia: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed Debt, 2015–2035 (concluded)

(In percent)

Debt service-to-exports ratio

Baseline	4	4	4	4	4	4	**6**	7
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	4	4	3	2	1	1	**-6**	-11
A2. New public sector loans on less favorable terms in 2015-2035 2	4	5	5	5	5	5	**7**	9
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	4	5	5	5	5	5	**6**	7
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	4	4	5	5	4	4	**6**	7
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	4	5	5	5	5	5	**6**	7
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	4	5	5	5	5	5	**8**	7
B5. Combination of B1-B4 using one-half standard deviation shocks	4	4	4	3	3	3	**3**	5
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	4	5	5	5	5	5	**6**	7

Debt service-to-revenue ratio

Baseline	3	4	4	3	3	3	**5**	5
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2015-2035 1/	3	4	3	2	1	0	**-5**	-8
A2. New public sector loans on less favorable terms in 2015-2035 2	3	4	4	4	4	4	**6**	7
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2016-2017	3	4	4	4	4	4	**5**	5
B2. Export value growth at historical average minus one standard deviation in 2016-2017 3/	3	4	4	4	4	3	**4**	5
B3. US dollar GDP deflator at historical average minus one standard deviation in 2016-2017	3	4	4	4	4	4	**5**	5
B4. Net non-debt creating flows at historical average minus one standard deviation in 2016-2017 4/	3	4	4	4	4	4	**6**	5
B5. Combination of B1-B4 using one-half standard deviation shocks	3	4	3	3	3	3	**3**	4
B6. One-time 30 percent nominal depreciation relative to the baseline in 2016 5/	3	6	6	5	5	5	**7**	7
Memorandum item:								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	19	19	19	19	19	19	**19**	19

Sources: Country authorities; and staff estimates and projections.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline., while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Annex IV. Background Analytical Work

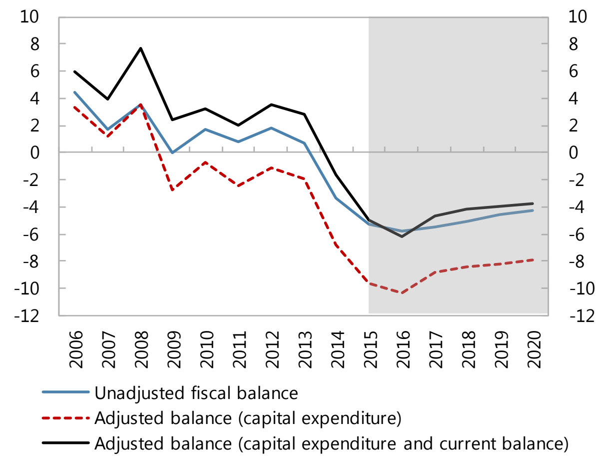
I. Fiscal Balances and the Public Sector Balance Sheet[1]

A. Adjusted Fiscal Balances

1. Investment by public enterprises is expected to increase further in the coming years, as natural gas-related exploration starts to pick up. Despite the greater role played by state-owned enterprises, roughly ¼ of total state investment is excluded from the fiscal accounts. This investment is made by 25 subsidiaries of the SOEs YPFB (hydrocarbons), ENDE (electricity) and by ENTEL (nationalized telecom company). These companies could pose increasing contingent fiscal risks and a closer look at their financial states is merited.

2. Adjusted overall balances are slightly higher than the unadjusted fiscal balances reported by the authorities. The balance worsens by 2.1 percent of GDP on average for 2006–14 with the inclusion of capital expenditure by the relevant subsidiaries. On the other hand, estimated current balances based on the available information improve the overall balance by 4.2 percent of GDP. The adjusted balance is projected to be similar to the unadjusted one during 2015–2016.

Overall Balances
(In percent of GDP)



Fiscal overall balances and adjusted balances
(in percent of GDP)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Fiscal overall balance	4.5	1.7	3.6	0.0	1.7	0.8	1.8	0.7	-3.4
Capital expenditure by companies with state participation (net of YPFB HQ)	1.2	0.6	0.0	2.7	2.4	3.2	2.9	2.6	3.4
o/w: YPFB subsidiaries	0.9	0.9	1.2	1.9	1.8	2.1	2.0	1.8	1.9
Estimated current balances of companies with state participation	2.7	2.8	4.1	5.1	4.0	4.4	4.7	4.7	5.2
o/w: YPFB subsidiaries	2.6	2.7	3.6	3.8	2.6	3.0	3.3	3.1	3.3
Adjusted overall balance	6.0	4.0	7.7	2.4	3.2	2.0	3.5	2.8	-1.6

Sources: Ministry of Economy and Public Finance, Ministry of Planning, YPFB, ENTEL and staff estimates and calculations.

[1] Prepared by S. Ogawa. See accompanying Selected Issues Paper.

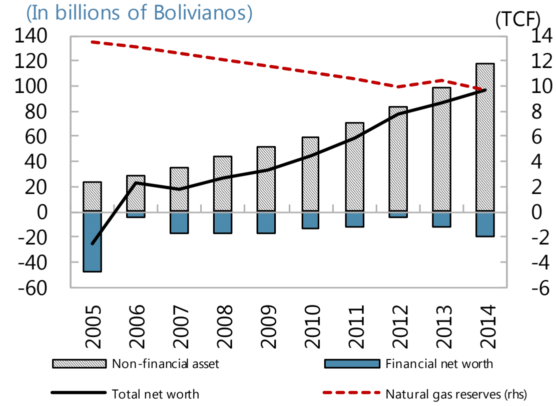
B. Public Sector Balance Sheet

3. Aggregate public sector net worth masks complex intra-governmental transactions. Overall, public sector financial and physical net worth has increased dramatically since 2007. Increasing public investment on the back of strong hydrocarbon fiscal revenues contributed to the accumulation of physical assets, while resulting in accumulation of international reserves at the central bank and deposits for sub national governments. But this has been at the cost of depletion of the physical asset (hydrocarbons reserves). SOEs' net worth is close to zero, as the accumulation of assets from natural resource revenues is matched by the increase in direct lending from the central bank (around 8.4 percent of GDP as of mid-2015, with the current lending limit up to 18 percent of GDP). Central government net worth has remained consistently in deficit over the years. Sub national governments net worth has increased steadily, benefitting from natural gas revenue sharing, but declined in 2014 as the capacity to execute capital expenditure projects improved.

4. Public sector net worth could start to gradually decline given the more challenging external environment, something that merits close attention. SOEs net worth could turn negative should the current pace of central bank lending for investment projects continue. Given the Treasury guarantee for central bank lending to SOEs, this could lead to a fiscal contingent risk should SOEs' operations deteriorate further. Sub national governments, especially those with limited alternative sources to hydrocarbons revenues, could start accumulating debt. Central bank net worth should remain positive, but the composition of assets and liabilities could change significantly with loans to SOEs increasingly replace international reserves on the asset side.

Public Sector Net Worth & Natural Gas Reserves

(In billions of Bolivianos)



Public Sector Net Worth

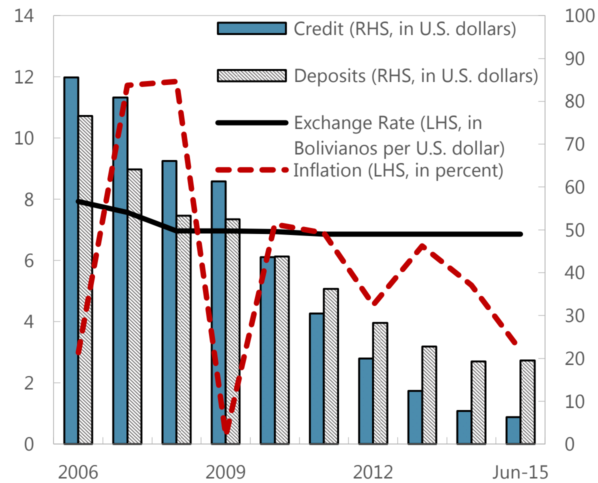
	2006	2007	2008	2009	2010	2011	2012	2013	2014
	(in billions of Bolivianos, unless otherwise stated)								
Physical assets	**28.4**	**35.3**	**43.6**	**50.8**	**58.7**	**70.4**	**83.1**	**98.7**	**117.1**
Financial net worth	**-4.9**	**-16.9**	**-16.8**	**-17.4**	**-13.6**	**-12.2**	**-5.2**	**-12.4**	**-20.5**
Financial assets	49.1	66.7	88.5	96.3	112.7	139.9	170.6	193.2	201.7
Cash and equivalent	21.3	25.0	30.3	33.1	49.0	69.9	92.3	93.8	93.1
Securities and shares	25.5	39.2	54.3	59.2	59.1	62.4	66.0	78.5	83.9
Loans	2.3	2.5	3.9	3.9	4.5	7.5	12.2	20.7	24.6
Others	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.2	0.2
Financial liabilities	54.0	83.6	105.4	113.7	126.3	152.2	175.8	205.7	222.3
Cash and equivalent	14.8	17.5	24.7	31.5	36.4	48.5	61.5	70.3	70.1
Currency in circulation	8.8	14.1	17.0	18.9	24.6	28.6	32.7	37.0	41.4
Securities and shares	26.7	33.7	43.2	40.2	39.7	42.3	39.5	43.8	49.3
Loans	3.1	17.7	19.9	21.1	23.4	30.6	39.8	52.1	59.2
Others	0.8	0.6	0.5	2.0	2.2	2.3	2.3	2.4	2.3
Public sector net worth	**23.5**	**18.4**	**26.7**	**33.4**	**45.1**	**58.1**	**77.8**	**86.3**	**96.6**
(in percent of GDP)	25.6	17.8	22.2	27.4	32.7	35.0	41.6	40.7	42.4

Sources: IMF Monetary and Financial Statistics, and staff calculations.

II. Entrenching a Durable De-Dollarization in Bolivia[2]

5. Financial dollarization has declined significantly since 2006 in the context of macroeconomic stability and given prudential measures. The share of deposits denominated in U.S. dollars declined from nearly 85 percent at end-2005 to about 20 percent by mid-2015, while share of credit denominated in U.S. dollars declined to 6.3 percent. During this period, the exchange rate has remained relatively stable (with a de-facto stabilized exchange rate against dollar since 2011) and inflation declined to well within single digit levels. Since early-2009, Bolivian banks have been required to make an additional provision of up to 1.5 percent for foreign currency denominated loans. And a tax of 0.15 percent has been imposed on foreign currency financial transactions for accounts larger than US$2,000 since 2006. There has also been a steady increase in reserve requirements on foreign currency deposits from 21.5 percent in 2008 to nearly 52 percent in 2015, compared to 12 percent for deposits in Bolivianos.

De-dollarization



Source: IMF staff calculations based on national authorities' data.

6. Given its success so far, Bolivia could refocus its policies from further reducing dollarization toward maintaining a durable de-dollarization. Apart from maintaining macroeconomic and political stability, this will require: (i) increasing economic diversification, (ii) further strengthening institutional quality and credibility, (iii) deepening capital markets, and (iv) allowing greater exchange rate flexibility.

7. An orderly transition to greater exchange rate flexibility should not necessarily reverse the de-dollarization trend significantly. This is a legitimate concern of the authorities. There is evidence, however, to suggest that making de-dollarization durable at low levels of dollarization—as in the case of Bolivia—requires gradual moves toward two-way exchange rate flexibility. This is in addition to credible macroeconomic policies and prudential frameworks that internalize the risks of balance sheet dollarization (Kokenyne et al., 2010).

[2] Prepared by D. Heng. See accompanying Selected Issues Paper.

Extent of Preparedness for Transitioning to Greater Flexibility: Before the Full Float 1/

	Orderly Exits			Exits Under Pressure			Degree of preparedness
	Chile (1984–99)[1]	Israel (1985–2005)[1]	Poland (1990–2000)[1]	Brazil (1999)[1]	Czech Rep. (1996–97)[1]	Uruguay (2002)[1]	Bolivia (2014)
Elements for a Floating Regime							
I. FX Market Development							
Spots Markets	✓	✓	✓	✓	✓	✓	✓
Derivative Markets/Hedging Instruments	✓	✓	✓	✓ (futures)	✓[2]	X	X
Complementary Markets							
Interbank Money Market	✓	✓	✓	✓	✓	X	✓
Securities Market	✓	✓	✓	✓	✓	✓	✓
II. FX Risk Management Capacity	✓	✓	✓	X	✓	X	✓
III. Alternative Monetary Policy Framework	✓	✓	✓	X	X	X	X
Monetary Policy Implementation Capacity	✓	✓	✓	✓	✓	X	✓
IV. Intervention Strategy for a Floating Regim	With the float	✓	With the float	With the float	✓	With the float	Discretionary intervention
Overall Preparedness	Well prepared	Well prepared	Well prepared	Reasonably well prepared	Reasonably well prepared	Not well prepared	Reasonably well prepared
Memo: Capital Account Liberalization							
Short-term Capital Inflows Liberalized	✓	✓	✓	✓	✓	✓	✓
Capital Ouflows Liberalized	✓	✓	✓	✓	✓	✓	✓
Derivative Transactions Liberalized	✓	✓	✓	✓	✓	✓	✓

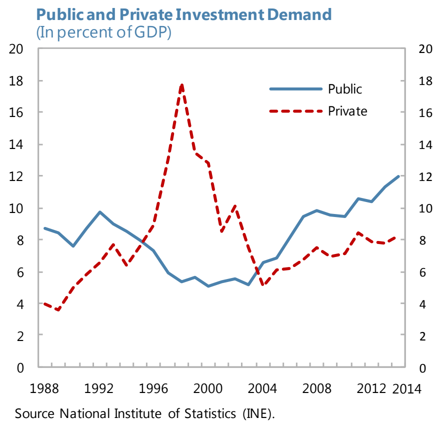
Source: Lennart Erickson, Anna Ivanova and Jorge Restrepo (2015) and staff analysis

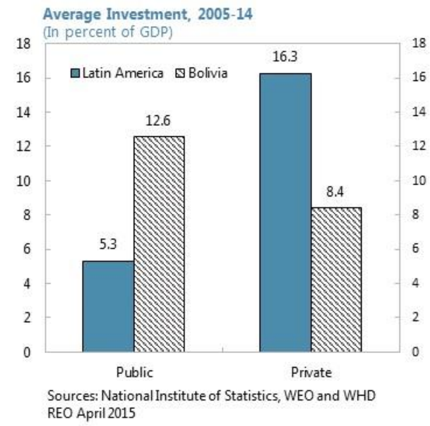
8. Bolivia appears to be well placed to make a transition to greater exchange rate flexibility. Country cases in which the transition was relatively smooth suggests that it takes time (e.g., Israel 1985–2005, Chile 1984–99, and Poland 1990–2000). However, Bolivia meets many of the preconditions needed for a successful transition (table), only lacking derivatives markets to help manage exchange rate risk and an alternative monetary policy framework.

III. Strengthening Private Investment[3]

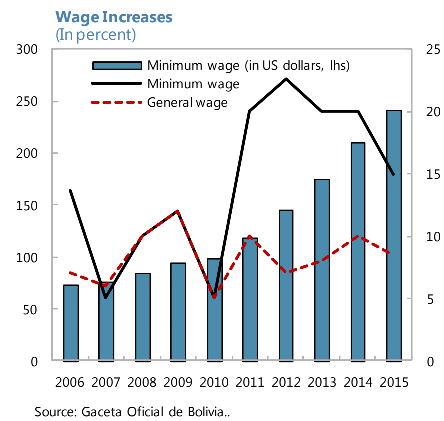
9. Bolivia's impressive growth performance partly reflects a public investment boom, while private investment has remained lackluster. In the past five years alone, investment contributed about 2 percent to growth each year, compared to 1 percent in the region. In particular, public investment has increased significantly since 2005, driven by large investments in the transport, hydrocarbons, and construction sectors. Private investment, however, lags behind regional averages.

[3] Prepared by F. Bornhorst and S. Cardenas. See accompanying Selected Issues Paper.





10. Bolivia needs to address key impediments to realize the important complementarities between the public and the private sector. These include:



- *Transportation infrastructure*. Bolivia ranks 121 out of 160 countries in the World Bank's 2014 *Logistics Performance Index*. The substantial internal distances, combined with a difficult terrain (mountains, valleys and plateaus) pose important challenges to reaching domestic and foreign markets. And less than 10 percent of its roads are paved compared to a regional average of 22 percent.

- *Wage costs.* These have risen significantly, with the minimum wage increasing nearly 4-fold and private sector wages growing by 8 percent on average over the last 10 years (while inflation averaged 6 percent). Other mandatory wage costs (including but not limited to the double-Christmas bonus if growth exceeds 4.5 percent) have further increased costs.

- *Labor regulations and informality.* A dated labor legislation and lack of judicial efficiency have reduced formal job creation and led to a boom in one-person companies, which operate at the margin of formality. And surveys link informality to reduced incentives for formal private investment, especially in the face of smuggling and other illegal activities.

- *Price controls and regulatory uncertainty.* The government's policy to protect consumers and curb inflation by intervening in markets and controlling prices for a variety of goods (up to ¼ of the CPI basket: mainly food, but also inputs such as cement) increases uncertainty over revenues and weighs negatively on investment decisions. In addition, firms have noticed a significant increase in the regulatory burden, including frequent supervisory and tax audits.

- *Export uncertainty*. The new Constitution determines that goods may only be exported once domestic demand has been satisfied. In the case of soy-beans, for example, where international prices are significantly higher than the (regulated) domestic prices, uncertainty over the availability of export permits reduces the incentives for farmers to invest in increasing production capacity.

- *Legal uncertainty*. The process of adapting the legal framework to the new 2009 New Constitution remains incomplete, which creates legal uncertainties that are particularly relevant for large, foreign investors. While some important laws have been approved recently many lack regulating decrees or omit important aspects (e.g., the mining law does not specify the tax regime).

BOLIVIA

November 5, 2015

STAFF REPORT FOR THE 2015 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

The Western Hemisphere Department (In Consultation with Other Departments)

CONTENTS

FUND RELATIONS

(As of September 30, 2015)

Membership Status: Joined December 27, 1945; accepted its obligations under Article VIII, sections 2, 3, and 4 on June 5, 1967. The exchange system is free of restrictions on current international payments and transfers.

General resources Account

	SDR Million	% Quota
Quota	171.50	100.00
Fund holdings of currency (Exchange Rate)	162.64	94.83
Reserve Tranche Position	8.87	5.17

SDR Department

	SDR Million	% Quota
Net cumulative allocation	164.13	100.00
Holdings	166.70	101.56

Outstanding Purchases and Loans: None

Latest Financial Arrangements

(In SDR Millions)

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	Apr 02, 2003	Mar 31, 2006	145.78	111.50
ECF [1/]	Sep 18, 1998	Jun 07, 2002	100.96	63.86
ECF [1/]	Dec 19, 1994	Sep 09, 1998	100.96	100.96

[1/] Formerly PRGF.

Projected Payments to the Fund[2/]

(SDR Million; Based on existing use of resources and present holdings of SDRs)

	2015	2016	2017	2018	2019
Principal					
Charges/Interest		0.00	0.00	0.00	0.00
Total		**0.00**	**0.00**	**0.00**	**0.00**

[2/] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Safeguards Assessment: Under the Fund's safeguards assessment policy, the Central Bank of Bolivia (CBB) was subject to an assessment with respect to the April 2, 2003 Stand-by Arrangement (SBA). A safeguards assessment was completed on June 27, 2003, and while no systemic risks with the CBB's safeguards were identified, uncertainties were expressed about the de facto lack of operational independence and program monetary data. An update assessment was completed on September 27, 2004 in conjunction with an augmentation of the SBA. This assessment confirmed that measures had been implemented to address all previously identified vulnerabilities, except for those requiring a change in the central bank law. Currently, CBB is not subject to the policy.

Exchange Arrangement: The Bolivian currency is the Boliviano and the de jure exchange rate regime is crawling peg to the U.S. dollar. Within the scope of the official crawling peg exchange rate regime, in an external environment characterized by market exchange rate volatility and decreasing external inflation, the sliding rate was set to zero to anchor the public expectations. Consequently, the boliviano stabilized against the U.S. dollar since November 2011. Accordingly, the de facto exchange rate arrangement has been retroactively reclassified to a stabilized arrangement from a crawling peg, effective November 2, 2011. The exchange regime is free of restrictions and multiple currency practices.

Article IV Consultation. The last Article IV consultation was completed by the Executive Board on January 27, 2014 (Country Report No. 14/36). Bolivia is on a standard 12-month consultation cycle.

Implementation of HIPC Initiative

	Original Framework	Enhanced Framework	Total
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	
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**
Implementation of MDRI Assistance			
Total debt relief (SDR Million)[3/]			160.93
Financed by: MDRI Trust			154.82
Remaining HIPC resources			6.11
Debt relief by facility (SDR Million)			

Debt Relief by Facility (SDR Million)

	Eligible Debt		
Delivery Date	GRA	PRGF	Total
January 2006	83.08	N/A	83.08
January 2006	6.70	71.15	77.85

[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 cannot 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.

[3/] The Multilateral Debt Relief Initiative (MDRI) provides 100 percent debt relief to eligible member countries that are qualified for the assistance. Grant assistance from the MDRI Trust and HIPC resources provide debt relief to cover the full stock of debt owed to the Fund as of end-2004 that remains outstanding at the time the member qualifies for such debt relief.

Implementation of Post-Catastrophe Debt Relief (PCDR): Not Applicable

Technical Assistance, 2010–15

Department	Purpose	Date
FAD	Treasury management and sub national debt control	May 10
FAD	Development of a medium-term macro fiscal framework	May 10
FAD	Institutional strengthening of tax and customs administration	Jun. 10
FAD	Integration of tax and customs administrations	Jan. 11
STA	National accounts	Feb. 11
MCM	Road map for the Issuance of Sovereign Bonds	Nov. 11
LEG	AML/CFT regulatory and institutional framework	Jan. 12
STA	Government Finance Statistics	Feb. 12
LEG	AML/CFT regulatory and institutional framework	Jul. 12
FAD	Integration of tax and customs administrations	Aug. 12
FAD	Tax policy (mining code reform)	Dec. 12
LEG	AML/CFT regulatory and institutional framework	Apr. 13
FAD	ROSC Evaluation of fiscal transparency	Apr. 13
MCM	Medium-term debt strategy	Apr. 13
FAD	Institutional strengthening of tax and customs administration	Jul. 13
FAD	Tax policy (international taxation, personal income tax and tax expenditure)	Jul. 13
STA	SDDS assessment	Oct. 13
STA	National accounts	Oct. 13
FAD	VAT gap and tax expenditure	Feb. 14
FAD	Auditing and evaluation of TA for the national tax service)	Feb. 14
FAD	Special schemes for small taxpayers and personal income tax	Oct. 14
FAD	Strategies for transfer pricing and control of medium and small taxpayers	Oct. 14
FAD	Medium-term fiscal framework	Oct. 14
STA	Government finance statistics	Dec. 14
FAD	Customs administration (risk management)	Jul. 15
STA	External sector statistics	Sep. 15

RELATIONS WITH THE WORLD BANK AND BANK-FUND COLLABORATION UNDER THE JMAP

A. Relations with the World Bank

The upcoming Country Partnership Framework (CPF) for the fiscal period 2016–2020 will provide the umbrella for World Bank Group (WBG) support to Bolivia. The CPF will be discussed by the Board of Executive Directors in December 2015. The program under the CPF is aimed at maximizing the impact of WBG interventions on poverty reduction and the promotion of shared prosperity, the WBG Twin Goals. Three selectivity filters were used to frame the program: (a) broad consistency with the priority constraints identified in the WBG Systematic Country Diagnostic (SCD); (b) alignment with the Government's development plans and demands; and (c) the WBG comparative advantage in sustaining Bolivia's progress in moving toward the Twin Goals. Despite the filters, the WBG engagement in Bolivia will remain flexible with respect to the evolution of the country's growth trajectory and new demands that may arise from the authorities.

The WBG program under the CPF is comprised of two pillars and five objectives that will provide general direction to the WBG's engagement. The CPF has the following two pillars: (1) promote broad-based and inclusive growth; and (2) support environmental and fiscal sustainability, and resilience to climate change and economic shocks. Within each pillar, the following inter-linked objectives will guide the WBG's engagement: (i) reduce transport costs and increase connectivity of isolated and vulnerable communities to the national road network; (ii) increase access to selected quality basic services for the poorest rural and urban communities; (iii) improve opportunities for income generation, market access and sustainable intensification (Pillar 1); (iv) strengthen capacity to manage climate change and reduce vulnerability to natural disasters; and (v) strengthen institutional capacity to improve public resource management and the business environment (Pillar 2). The formulation of the pillars and objectives aims at both reflecting the current portfolio but also allowing space for nascent government demands.

The WBG program during the CPF period will see the transition to International Bank for Reconstruction and Development (IBRD)-only country. The existing trend of a steady state number of projects (about 11–13) is expected to continue. In addition, the policy dialogue is expected to increase in response to financing demands from Government, underpinned by a solid unfolding policy agenda in the areas of climate change and possibly investment climate and fiscal management. During FY2015, the WBG delivered the first Development Policy Financing (DPF) for Bolivia on Disaster Risk Management that included also the first IBRD loan for the country in recent years.. The Program will encompass an indicative allocation from the International Development Association (IDA) for FY2015–2017 of Special Drawing Rights (SDR) 148.0 million (US$208 million equivalent) and a transition to IBRD-only financing by the end of the current IDA17 cycle at the end of FY2017.

The WBG's engagement is defined for the first year of the CPF, but less so for subsequent years to allow for flexibility in responding to emerging priorities. The World Bank's portfolio of operations for FY2016 is based on the sustained dialogue with the Bolivian authorities. New lending operations in FY2016 include an additional financing for a rural community-driven development project, two operations in the transport sector, and a potential DPF on climate change. For FY2017 and beyond, the pipeline is open, with the exception of possible additional financings in some successful projects, to allow the WBG to meet emerging needs in Bolivia and reflect the findings of a Performance and Learning Review (PLR) that is planned for early FY2018. The PLR will offer a critical stocktaking exercise and allow the WBG to adjust course as necessary.

The CPF takes into account the existing portfolio as much of the impact on the CPF objectives will be derived from these legacy portfolio. This will also ensure a degree of continuity between the previous FY2012–2015 Country Partnership Strategy (CPS) and the current CPF. The current portfolio is focused on disaster risk management and climate change, rural development and agriculture, transport, strengthening of statistical capacity, energy, urban development and employment. The World Bank's portfolio comprises 11 lending operations totaling US$752 million, of which US$353 million remain undisbursed (Table 1). Looking forward, the priorities will be to: (i) consolidate the portfolio in traditional areas, and expand it to capture emerging demands from Government, including greater attention to human capital; and (ii) address the main challenges in implementation, especially those related to institutional capacity and governance and fiduciary standards. New operations in FY2016 worth US$605 million.

Table 1. World Bank Investment Portfolio in Bolivia (as of October 2015)

Project	Commitment (US$ million)	Disbursed (US$ million)	Undisbursed* (US$ million)	Closing Date
Access and Renewable Energy	50.0	0.00	45.45	December 2021
Pilot Program for Climate Resilience (PPCR) Phase 2 – Integrated Basin Management	45.5	0.10	45.40	June 2020
Agricultural Innovation and Services	39.0	22.7	12.87	February 2017
Community Investment in Rural Areas	100.0	28.51	68.23	November 2019
Rural Alliances Project II	50.0	17.64	29.12	November 2017
Expanding Access to Reduce Health Inequalities (APL3)	11.17	9.71	0.61	December 2015
Strengthening Statistical Capacity & Information for Evidence-Based Planning	73.3	49.26	20.29	December 2017
Improving Employability and Labor Income of Youth	20.0	0.0	18.20	December 2020
Urban Infrastructure Project	54.0	36.41	17.83	December 2016
Disaster Risk Management DPF	200.0	197.18	0.0	July 2016
National Roads & Airport Infrastructure	109.5	1.86	95.89	December 2016
Total	**752.47**	**363.35**	**353.89**	

*Undisbursed balances differ from the difference between committed and disbursed amounts due to variations in the exchange rates between SDRs and U.S. dollars.

The International Finance Corporation (IFC) will continue supporting opportunities for private sector development under the CPF. As part of IFC's commitment to reengage in Bolivia, it has recently approved the first long-term financing operation in the Bolivia's banking sector in over a decade. This credit facility will exclusively finance local Small and Medium Enterprises (SMEs). In addition, two other operations were approved in the agribusiness and hospitality sectors. As for Advisory Services (AS), the IFC is implementing projects in strategic sectors to maximize employment, simplify business creation and income generation in low-income populations, as well as minimize impacts on the environment. In addition, dialogue with partners in new sectors is underway. As for the Multilateral Investment Guarantee Agency (MIGA), in the absence of any immediate pipeline projects in the country, it remains open to supporting foreign direct investments via its political risk insurance products.

In addition, the World Bank will continue providing Advisory Services and Analytics (ASA). In the next years ASAs will focus on those areas where the World Bank can provide value added, respond to Government needs and in alignment with the knowledge gaps identified in the SCD. Table 2 presents the list of ongoing Non-Lending Technical Assistance. The program is kept open to respond to emerging requirements.

Table 2. Ongoing ASA FY2016

	Product
Multidimensional Poverty Phase IV	TA
Investment Promotion Event	TA
Peru and Bolivia HIV/AIDS Analysis	TA
Strengthening Human Talent for Science and Technology	TA
Revision of Water and Sanitation Pre-investment Norms	TA
Multiannual Budgeting and Planning	TA
Urban Development	TA

Trust funds (TF) continue to be used to support policy dialogue and to pilot innovative ideas. The current TF portfolio (Table 3) includes four grants in areas such as quality of statistical systems, early childhood care and development, community-driven development in remote areas and institutional strengthening.

Table 3. World Bank Trust Fund Portfolio in Bolivia (as of October 2015)

Project	**Amount (US$ million)**
Ensuring Quality in the National Statistical System (TFSCB)	0.24
Early Childhood Care And Development in the Most Vulnerable Districts Of La Paz And El Alto (JSDF)	2.78
Integrated Community-Driven Territorial Development for Remote Communities in the Amazon (JSDF)	2.21
Strengthening of Planning, Investment, Fiduciary and Procurement Capacities	0.52
TOTAL	**5.75**

B. IMF Relations with the World Bank under JMAP

The following priorities were identified for the coordinated work-plan on Bolivia:

- **Strengthening of the fiscal framework**, multi-annual budgeting and the link with the planning process remains a challenge. The public sector has to strengthen capacity in public sector management, procurement and public investment, including at the subnational level.

- **Improving the business climate to bolster investment.** Bolivia's private investment rate remains significantly below the levels observed in the past decade and well below the regional average.

- **Reducing poverty.** Significant challenges remain in poverty reduction and inequality. Also, access to basic services, particularly in rural areas, remains a challenge. Social services, including access to quality basic education, health, water and sanitation and employability of low income youth and social protection network is in the agenda.

It was agreed that the teams continue with the following division of labor:

- **Multi-annual budget and planning framework.** The Bank is supporting the Ministry of Development Planning in setting up the basis for multiannual planning and the link with the budget process. The Bank is also supporting the strengthening of capacities for public investment, including at the sub-national level.

- **Debt management.** The Bank continues open to a Government requirement to develop an action plan based on the last DeMPA report.

- **Poverty and social protection.** The Bank has been providing technical assistance on poverty measurement, including monetary poverty and multidimensional well-being indicators. This complements the support provided to generate high quality statistical information through a STATCAP project. These tools would help both diagnosis and targeting of population that fails to reach minimum standards of multidimensional welfare, and on building capacity on the measurement of poverty including on gender issues. Also, the Bank will continue assisting the Government in the areas of youth employment, health and early child development.

- **Private sector development**. The IFC is providing credit lines to financial institutions to lend to SMEs. The Bank will continue advancing the preparation of a DPL focused on investment climate enhancement.

RELATIONS WITH THE INTER-AMERICAN DEVELOPMENT BANK

As of September 30, 2015, the Inter-American Development Bank (IDB) had approved loans to Bolivia amounting to US$6.05 billion, with disbursements totaling US$4.63 billion. Bolivia's outstanding debt to the IDB was approximately US$1,666.7 million with undisbursed approved funds for US$1,067.25 million. During the year net cash flows to the country were positive for a seventh year in a row, a trend expected to continue in the base scenario to 2016. At the end of 2007, the IDB unilaterally joined the IMF-WB MDRI initiative, by writing off a total of US$741.1 million in principal payments and US$307.3 million of future interest payments, generating an estimated annual fiscal space of more than US$18.0 million on average.

After the last round of debt relief, the IDB has implemented new criteria of allocation of concessional lending which is consistent with the application of the Debt Sustainability Framework. The IDB lending to Bolivia follows the operational guidelines for concessional funds under the Fund of Special Operations (FSO) performance-based allocation system. Parallel lending operations, modality that blends ordinary and concessional funding, will be the preferred lending instrument up to 2020.

The IDB and Bolivia have a country strategy covering the period 2011–2015. Under the country strategy, the IDB has decided to increase financial flows to Bolivia. While in 2011, the approval of new loans was US$252 million, it will reach US$475.1 million in 2015 and US$633.4 million in 2016.

Under the Bank's country strategy with Bolivia, the government and the IDB have agreed on making sustainable growth and poverty-inequality reduction as main objectives of their strategic engagement. In pursuit of this objective, the Bank aligned its actions with those on Bolivia's National Development Plan. The country strategy targets its interventions in the following sectors: (i) Transport; (ii) Water and sanitation; (iii) Energy; (iv) Early Childhood Development (ECD); (v) Health; (vi) Education; and (vii) Institutional and Sustainability Strengthening. As overarching sectors, the IDB focuses on climate change and indigenous population/diversity issues. A new Country Strategy is currently being developed.

As of September 30, 2015 the portfolio of executing sovereign guaranteed operations in Bolivia consists of 31 operations, totaling US$1.77 billion, of which 37.2 percent has already been disbursed. The current executing portfolio supports mostly transport, water and sanitation and energy infrastructure interventions. The non-sovereign guaranteed executing portfolio consists of 16 loans ascending to US$40.9 million.

STATISTICAL ISSUES

(As of October 15, 2015)

A. Assessment of Data Adequacy for Surveillance

General: Data provision has some shortcomings, but is broadly adequate for surveillance. Staff welcomes the progress made by the authorities to further strengthen the quality and timeliness of statistics, which includes updating the base of the national accounts, implementing the agricultural and economic census, a plan to reinstate the employment survey, and working towards full subscription of the Special Data Dissemination Standard (SDDS).

National Accounts: The National Institute of Statistics (INE) is working on updating of the base year of the national accounts (from 1990 to 2007) which includes the implementation of the System of National Accounts 1993 (SNA 1993) and some of the most relevant recommendations of the SNA 2008. INE's plans to release preliminary results (year 2007–2012) and definitive series in 2014 have been delayed.

Labor market: The quality of the household and employment surveys has declined in the last few years, due mainly to financial constraints. The quarterly employment survey was discontinued in 2003, leading to a lack of quarterly information on unemployment, employment and wages. Yearly information on wages is still compiled by INE.

Prices statistics: Industrial producer price indices (PPI) and external trade unit values are compiled by INE, but are in need of revision as regards concepts and definitions consistent with SNA 1993, as well as treatment of seasonal products, missing items, quality changes, and introduction of new products. A PPI TA is planned for November 2015.

Government finance statistics: Annual data on the operations of the consolidated central government do not cover all operations of decentralized agencies and operations channeled through special funds. The ongoing implementation of a comprehensive financial management system, with funding from the IADB/WB, will help ensure proper monitoring of public sector financial operations including subnational fiscal operations, debt and social spending. It will also be important to improve on the reporting of the operations and debt of public enterprises.

Balance of payments: Sources of information for both balance of payments and international investment position (IIP) are considered sound, but the classification of units by institutional sector and the classification of external assets and liabilities by functional categories and instruments need to be enhanced. Some institutions that shall be considered Other Deposit-Taking Corporations and a fund that should be considered part of the General Government sector and held sizable amounts of external assets and are currently included under the Other Sectors; the assets of several sizable funds are classified under Portfolio Investment or Other Investment regardless of the real nature of the assets; valuation changes of relevant Bolivian external assets are not identified and they are included in transactions. Securities issued internationally by the Bolivian government held by resident investors are identified in the data sources but they are treated as external liabilities in the external sector statistics (ESS). Investigations with reporters in order to delimitate services (mainly construction or other business services) and direct investment are needed, and the method to estimate the amounts of goods for processing services related to the exports by Bolivia shall be updated. Consistency within ESS needs also to be enhanced. During a September 2015 TA mission on ESS, an implementation plan for the compilation of ESS on a BMP6 basis was agreed. SDDS requirements regarding ESS are currently met.

B. Data Standards and Quality

Bolivia has participated in the General Data Dissemination System (GDDS) since November 2002. Data ROSC published on August 13, 2007.

Bolivia: Indicators Required for Surveillance

(As of October 15, 2015)

	Date of Latest Observation	Date Received	Frequency of Data[1]	Frequency of Reporting[1]	Frequency of Publication[1]	Memo Items: Data Quality–Methodological Soundness[10]	Memo Items: Data Quality–Accuracy and Reliability[11]
Exchange Rates	Daily	Daily	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[2]	Daily	Daily	D	D	D		
Reserve/Base Money	Sep. 2015	Oct. 2015	M	M	M	O, LO, LO, O	O, O, O, O, O
Broad Money	Sep. 2015	Oct. 2015	M	M	M		
Central Bank Balance Sheet	Sep. 2015	Oct. 2015	M	M	M		
Consolidated Balance Sheet of the Banking System	Sep. 2015	Oct. 2015	M	M	M		
Interest Rates[3]	Sep. 2015	Oct. 2015	W	W	W		
Consumer Price Index	Sep. 2015	Oct. 2015	M	M	M	LO, O, LO, O	O, LO, LNO, O, LO
Revenue, Expenditure, Balance and Composition of Financing[4] – General Government[5]	Aug. 2015	Oct. 2015	M	M	M	LO, LO, LNO, LO	LO, O, O, O, LO
Revenue, Expenditure, Balance and Composition of Financing[4]– Central Government[6]	Aug. 2015	Oct. 2015	M	M	M		
Stock of Central Government and Central Government-Guaranteed Debt[7]	Aug. 2015	Oct. 2015	M	M	M		
External Current Account Balance	Q1 2015	Sep. 2015	Q	Q	Q	O, LO, LO, LO	LO, O, LO, O, LO
Exports and Imports of Goods and Services[8]	Q1 2015	Sep. 2015	Q	Q	Q		
GDP/GNP	Q1 2015	Aug. 2015	Q	Q	Q	LO, LO, LO, O	LNO, LO, LNO, O, LO
Gross External Debt	Sep. 2015	Oct. 2015	M	M	M		
International Investment Position[9]	Q1 2015	Sep. 2015	Q	Q	Q		

[1] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); Irregular (I); Not Available (NA).

[2] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[3] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[4] Foreign, domestic bank, and domestic nonbank financing.

[5] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[6] Bolivia does not compile central government fiscal data.

[7] Guaranteed non-financial public sector debt. Including currency and maturity composition.

[8] Monthly frequencies for goods only.

[9] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[10] Reflects the assessment provided in the data ROSC (published on August 13, 2007, and based on the findings of the mission that took place during January 24–February 7, 2007) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O); largely observed (LO); largely not observed (LNO); not observed (NO); and not available (NA).

[11] Same as footnote 10, except referring to international standards concerning (respectively) source data, assessment of source data, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

Statement by Mr. Chodos and Mr. De la Barra on Bolivia
November 20, 2015

Background

Despite a regional context of economic slowdown, Bolivia's economic growth was outstanding in 2014 (5.5 percent) and will be similar in 2015 (estimated 5 percent) registering the highest growth rate in South America, driven mainly by the dynamism of internal demand. The ample public investment of the Bolivian authorities in recent years will allow the continuation of such trend from 2016 onwards. During 2015 all economic activities have contributed this performance with the exception of crude oil and natural gas. Bolivia's exceptional macroeconomic performance was corroborated by major credit risk rating agencies in their positive evaluations, which translated into a continuous increase of the country risk rate in recent years. As a matter of fact, Fitch Ratings upgraded Bolivia's long-term foreign and local currency Issuer Default Ratings (IDRs) in 2015 based on Bolivia's improvement in fiscal revenue, domestic investment and regulatory framework, as well as its robust external buffers and ample fiscal policy space that render its economy better-placed to absorb adverse shocks and adopt counter-cyclical policies.

The staff report presents a pessimistic view of the Bolivian economic outlook and it does not take into account the country's medium-term economic objectives and policies, including contingency plans to face shocks. Moreover, the authorities regret that staff has not given the necessary attention to the authorities' claims regarding the effect that IMF surveillance reports may have on expectations, especially regarding growth, the exchange rate, financial inclusion, financial strength and economic stability. The Bolivian authorities have repeatedly expressed that economic agents are very sensitive in Bolivia, as they do not internalize projections appropriately, due to the manipulation and mishandling of information by media and political opposition.

Growth Outlook and Potential Growth

The staff once again puts unnecessary emphasis on Bolivia's commodity dependence and the challenges that the new commodity cycle would mean for the country. The staff's statements are not accompanied by technical and empirical support that demonstrates how the change in commodity price cycle significantly affects Bolivia's economic growth. The authorities reiterate the importance to strike the right balance between the importance of commodity prices and the country's overall economic performance. The staff must acknowledge that domestic demand is the main engine of growth in Bolivia. Furthermore, the government's economic policy is fundamental for a better performance of the economy, not only for the current juncture but also for the long-term development strategy. The authorities reiterate that the Bolivian economy is not decelerating given its resiliency, which will keep the strong growth tendency.

Growth momentum for 2015 does not have the "cost" of twin deficits as indicated by the staff since all components of domestic demand are staying positive. The Bolivian authorities are projecting a growth rate of about 5 percent for 2015. Given that until June 2015 a cumulative growth of 4.7 percent was already recorded, the growth rate of 4.1 percent for 2015—projected by the staff—would imply only growing 3.5 percent the rest of the year, which is highly unlikely given the envisaged acceleration of public investment in the second half of 2015, the starting up of the liquid hydrocarbon separation plant, better performance of the financial sector due to the expansionary monetary policy, a solid performance of the agricultural sector registered as of June 2015, and expansion in electricity and construction sectors.

In 2014 the staff had estimated Bolivia's potential output to be around 5 percent. The estimate now has been changed to 3.5 percent which is not justified and appears unreasonable from a technical or theoretical point of view, taking into account the continuous increase in domestic private consumption, investment (public and private, that both recorded peaks in recent years), capital, and employment in the economy. The Bolivian government has estimated (through a wide range of methodologies) that the potential output for Bolivia remains at 5 percent.

Also, the staff underestimates the GDP growth by 2.2 percentage points on average for 2015-2020, because new projects, such as electricity generation or hydrocarbons industrialization, among others, are not considered. These projects not only diversify the economy, but increase its complexity and reduce the vulnerability to external shocks.

On the other hand, a 4.7 percent growth as of June 2015—reported by the General Index for Economic Activity (IGAE)—would already be exceeding the re-estimated potential GDP and the country would start experiencing inflationary pressures, which is not the case as inflation is under control.

While the fall in terms of trade could, in theory, affect public investment, it is important to note that Bolivia is in a strong position to face a fall in exports revenue, since the country has enjoyed several years with twin surplus, which provides greater space compared to even advanced economies. In addition, controlled inflation and the Central Bank of Bolivia (CBB)'s liability level due to monetary regulation operations give ample space for a more expansionary monetary stance to complement fiscal policy in stimulating the dynamism of economic activity.

It is important to note that according to the World Economic Outlook (WEO), countries that have a less pro-cyclical fiscal policy and have high levels of credit, such as Bolivia, are less likely to face large variations in their growth. Moreover, the WEO states that countries with heavy investments in sectors favored by the boom are more vulnerable to shocks. Nevertheless, this is not the case for Bolivia, given that between 2006 and 2014, hydrocarbons and mining investment represented only 13.8 percent of public investment. Therefore, it is contradictory for IMF staff to reduce Bolivia's potential growth.

The staff forecasts assume that Bolivia has a short horizon for its proven gas reserves omitting the exploration plans that will be carried out by the national oil company (YPFB). We must say that the gas reserves are increasing and there are enough assurances that the contract with Brazil will be renewed and expanded. Exploration by YPFB has produced important outcomes, such as the discovery of a new well (Margarita 7) that allows incorporating a new reservoir of gas (increasing 0.8 trillion cubic feet in gas reserves). An additional reservoir of crude oil in Santa Cruz has also been found, which provides 28 million barrels of oil (MMBbl) and nearly triples the reserves of crude oil in the country, from 16 to 44 MMBbl. Furthermore, Bolivia is already able to sell gas to other countries. Higher diversification of the Bolivian economy is expected once the new development plan (under preparation) starts being implemented.

The exploration schedules include investments amounting to US$ 4,308 million between 2015 and 2019, of which 22 percent will be made by foreign companies (Repsol and Petrobras). Also recently, Total and British Gas (foreign corporations) committed to invest around US$1,500 million in exploration until 2019. The government is highly committed to oil and gas exploration. As a matter of fact, it has decided to carry out exploration even in unconventional areas and, for that matter, licensing procedures are being streamlined and the Supreme Decree 2366 has been approved (May 2015) allowing exploration in protected areas.

Private Investment and Foreign Direct Investment

The staff's superficial knowledge about the country is evidenced once again when it comes to analyze investment on the private sector. The IMF staff repeatedly discusses Bolivia's low levels of private investment compared to Latin America, without mentioning that private investors have scarce capital and low risk appetite. However, the staff has to acknowledge that in the last decade private investment has presented a growing trend. In fact, private investment as a percentage of GDP has continuously increased from 5.4 percent in 2004 to 8.6 percent in 2014.

During the 20 years of neoliberal period, Bolivia never had a strong private sector despite the favorable environment offered to private investors. The staff should not insist on asking for a larger share of private investment because this sector lacks capacity and entrepreneurial vision. Neither wage policy nor the exchange rate level are the cause of low private investment, but the low productivity.

The regulatory framework has been improved in order to increase private investment. The Investment Protection Law and the Conciliation and Arbitration Law recently approved represent a significant step forward for legal security for national and foreign investment.

These laws are a result of consensus with the private sector and international cooperations, and also provide investment incentives.

The Bolivian government is highly committed to facilitate private investment, both domestic and foreign, and last month organized in New York the Investing in Bolivia Summit, which attracted the interest of more than 200 investors. Consequently, the Ministry of Development Planning will create an exclusive office for dealing with Foreign Direct Investment (FDI) flows. In the same vein, President Morales on his recent visit to Germany, Italy, Ireland, and France strengthened business and economic ties with these countries. Another expression of such commitment is the Development Promotion of National Industry bill submitted by the Ministry of Productive Development and Plural Economy to the National Assembly.

The IMF staff does not consider that political, social, and economic stability in Bolivia play an important role in assuring an appropriate investment climate. Maintaining a stable exchange rate has allowed more certitude for families and firms positively supporting investment climate and maintain the strength and stability of the financial system.

FDI flows have continuously entered the country reflecting investors' high level of certainty and confidence in the national economy. In fact, during recent years Bolivia was one of three countries in the region with the highest cumulative index of FDI (along with Brazil and Paraguay). In addition, Bolivia shows low levels of volatility in these flows, which eventually translate into attenuated economic cycles.

Fiscal Policy

Public finance continued to evolve sufficiently in 2014; in fact, the tax burden (excluding hydrocarbon tax - IDH), increased from 21.7 percent in 2013 to 22.3 percent in 2014. According to the Economic Commission for Latin America (ECLAC), Bolivia has the largest tax-to-GDP ratio increase over the past 23 years in the whole of Latin America. Expenses were greater than revenues due to the record level of public investment, mainly executed by sub-national entities (governorates and municipalities). There were also unforeseen expenditures because of the rehabilitation of the economy of the Amazon region—impacted by natural disasters—and payments made to nationalized companies. Consequently, the overall balance recorded a healthy deficit of 3.4 percent of GDP in 2014.

The fiscal deficit in 2015 is set to be around 4.1 percent of GDP, below the level projected by the staff report (5.3 percent). This projection is highly distorting given the precedent discipline that Bolivia has applied in managing public finances. The fiscal deficit in 2015 will be in line with the Financial Fiscal Program agreed between the CBB and the Ministry of Economy and Public Finance (MEPF) since there will be no extraordinary expenses. Also, it is expected that spending on goods and services will decrease because of—among others—lower hydrocarbons subsidies, a lower tin price for Vinto Metallurgical Company and lower wheat imports. Transfers linked to oil prices will also decline. On the income side, the tax revenue increase will partly compensate for the fall on oil prices. Even though the authorities are engaged in pursuing an ambitious investment program for 2016, macroeconomic stability is paramount for the country and the authorities do not intend to put it in danger.

The staff emphasizes the importance of reducing the non-hydrocarbon fiscal deficit. However, this should not be a policy target. The reason is that the calculation methodology is not standard; hence the results cannot be contrasted with the authorities' own estimations.

The pessimistic medium-term fiscal deficit forecasts do not include higher revenues from the productive diversification envisaged in the government´s development plan—especially from energy and mining projects.

Bolivia's external debt stock is one of the lowest in the region and the world, and is below the thresholds established by international organizations. The assumptions to assess Bolivia's debt sustainability are distorting, such as low growth forecasts and zero probability of finding new gas reserves, which obviously imply higher debt-to-GDP ratios. Consequently, the debt levels forecasted by the IMF staff, which reach up to 85 percent of GDP, are not realistic.

Although Bolivia does not have a medium-term fiscal framework according to the IMF methodology, the development plan in preparation includes long-term fiscal projections that give consistency to macroeconomic and development policies. The technical assistance report "Progress in the implementation of the Fiscal framework of medium-term" (February 2015) acknowledges that the MEFP has been making efforts to implement a medium-term fiscal framework, and it has prompted reforms to strengthen such process. Directives of the 2015 Budget establish that public institutions have to elaborate annual and multi-annual budgets, spanning five years.

Exchange Rate and Monetary Policy

There are several alternative methodologies that indicate that the Bolivian currency is not overvalued. Indeed, econometric models estimated by the CBB reflect that the behavior of the real exchange rate has been consistent with movements of economic fundamentals. Furthermore, during recent years there were no persistent misalignments of the real exchange rate from its equilibrium level.

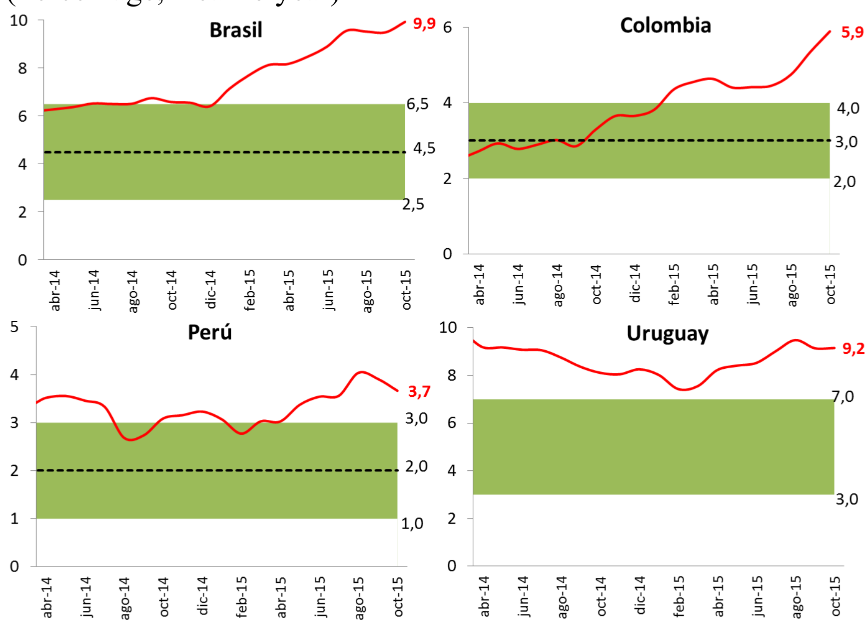
It is worth mentioning that any methodology for assessing equilibrium exchange rates involves conceptual simplifications and could generate different quantitative estimations, which highlight the high degree of sensibility to different assumptions, for example the period of analysis.

The staff's conclusion regarding a high overvaluation of the domestic currency in the specific case of Bolivia could cause an overreaction within the country and unintentionally lead to an attack to the domestic currency. The Bolivian authorities provided ample explanation to staff on the exchange rate policy, its objectives and internal consistency with the objectives of the overall economic policy. They have also repeatedly remarked that any assertion—like the one included in the staff report regarding overvaluation—could dangerously exacerbate expectations of agents, which may cause financial disintermediation, dollarization and a loss of net international reserves (NIR).

The policy of exchange rate stability allowed the proper management of both external price shocks and exchange rates adjustments in neighboring countries; the exchange rate is consistent with the decline in international prices and it has not affected external competitiveness, since persistent real exchange rate misalignments were not generated.

It must also be stressed that a depreciation of the Bolivian currency may generate inflationary pressures, such as those observed in the region. In fact, during 2015 several countries with an inflation-targeting regime and flexible exchange rates experienced higher inflation (persistently above target bands) driven by the pass-through effect from the depreciation to inflation (Figure 1) worsened by a higher exchange rate volatility.

Figure 1
Annual inflation in selected countries
(Percentage, Year to year)



Source: Bloomberg

An extremely relevant fact of the Bolivian economy, is that a sudden devaluation without preparation for the public may be contractive, generating a decline in domestic economic activity. As discussed in the literature, there are several mechanisms through which devaluation may affect output. First of all, its effects on the real exchange rate may be rapidly offset by an increasing inflation. Furthermore, devaluation may generate a redistribution of income from groups with a high marginal propensity to consume, to those with a high marginal propensity to save, resulting in a decline in aggregate demand and output. Moreover, in the short run the productive structure is very rigid and, therefore, real devaluation does not necessarily produce an increase in tradable output. Technical analysis demonstrates that the Marshall Lerner condition (excluding hydrocarbons) has not been met, given the low sensitivity of exports and imports combined to exchange rate variations. This implies that the competitiveness of Bolivian exports is related to other variables, for example, the competitiveness of the private sector, so that depreciation alone would fail to stimulate them.

Moreover, ECLAC data shows that the average real wage in Bolivia is the lowest in South America and that it has remained stable in recent years, which improves competitiveness with respect to neighboring countries. More importantly, public investment was strongly aimed at improving energy infrastructure, transport and communications in the country, which reduced costs for the private sector and, at the same time, contributed to enhancing competitiveness. Furthermore, it must be pointed out that the nominal exchange rate is no longer considered as one of the determinants of external competitiveness (the World Economic Forum no longer takes into account the exchange rate at the time of evaluating competitiveness of economies).

The recommendation for a more flexible exchange rate policy is a traditional and worn off one and staff should be aware that it cannot always be applied to all countries because economic conditions and development stages are different among countries, and idiosyncratic vulnerabilities are in place.

Regarding the NIR, they have decreased mainly due to extraordinary operations and changes in foreign currency and gold valuations. The observed loss during the first months of the year does not represent a risk to macroeconomic stability since the authorities have envisaged it within the 2015 financial program projections. In this regard, projecting a NIR fall of more than 65 percent of GDP by 2020 appears speculative.

The current account deficit recorded recently is in accordance with what is happening in the region, although it must be noted that the deficit observed in Bolivia is among the smallest, given that the trade balance was not affected significantly. The current account deficit would be lower than the 4.5 percent projected by the staff, as a result of remittances and a moderate fall in non-traditional exports. Furthermore, CBB studies conclude that the current account will converge to its equilibrium level faster than in other countries of the region. In addition, imports have registered a low decline: as of the third quarter of 2015 it is less than in similar period in 2014.

The last financial crisis highlighted the need for monetary policy through almost zero interest rates; therefore, central banks had to apply non-conventional monetary policies reflecting a lack of efficacy of the traditional monetary policy, which is not the case in Bolivia. On the contrary, during recent years several policy instruments have been introduced that have strengthened the monetary policy transmission channels and improved its effectiveness. In addition, Bolivia's current monetary policy was analyzed by the staff, concluding that it was effective and useful.

As for inflation, it is projected that the 2015 end-of-period inflation would be below the 5.5 percent target, and even less than in the previous year (5.2 percent). Such lower inflation would provide enough space to continue implementing monetary impulses to contribute to the dynamism of the real sector. In addition, the Bolivian government is ready to adopt short-term policy measures to control inflation.

By mandate of the Constitution, the CBB`s main objective is to maintain the internal purchasing power of the currency, to contribute to economic and social development; therefore, loans to strategic national public companies (EPNE) are part of this mandate. It is worth mentioning that these loans follow the guidelines of the annual Financial Program signed by the CBB and MEPF, in which growth and inflation targets are set (consistent with a prudent macroeconomic management). In addition, these credits are monitored and controlled by the Superior and Strategic Council for Public Enterprises. Policy coordination between the CBB and the Executive Branch has demonstrated a high effectiveness in achieving macroeconomic objectives in terms of inflation and economic growth.

The Financial System

The staff argues that the Financial Services Law (FSL) is altering the composition of credit flows and posing risks to financial stability. Such statement has neither technical nor empirical support (no risk indicator worsened because of the law) and therefore is subjective and mere speculation.

The law has not relaxed the rules on the process of credit evaluation. The government's financial policy focuses on increasing productive credit and social housing as part of the goals of the Bolivian Economic Model to support economic development and improve living conditions with more affordable housing for the people.

The financial system in Bolivia is not a cause for concern because it shows positive and strong indicators. The credit-to-GDP ratio is one of the lowest in the region and there is space to grow without posing risks. Non-performing loans (NPL) represent 1.7 percent as of September 2015. To reign on risks and detect vulnerabilities in the financial system the Financial Stability Council was created to take care of and monitor macro-prudential issues.

In addition, in 2015 the financial system remains very liquid, and new loans continue to flow while their quality has not been affected. Up to September 2015, the financial system's loan portfolio is US$1,654 million higher than in December 2014, registering a new record. Banks will achieve the 60 percent productive loans quota without causing excessive credit growth. Credit quotas have so far proved effective in redirecting credit towards productive loans which enhance the output capacity of the economy, while NPLs remained the lowest in the region. Banks remain profitable and the decreasing number of microfinance borrowers did not reflect reduced financial inclusion, but a reclassification within the financial sector, economic growth and strategic alliances between banks and micro financial institutions. There appears to be no support to say that financial disintermediation may occur because of greater loan size.

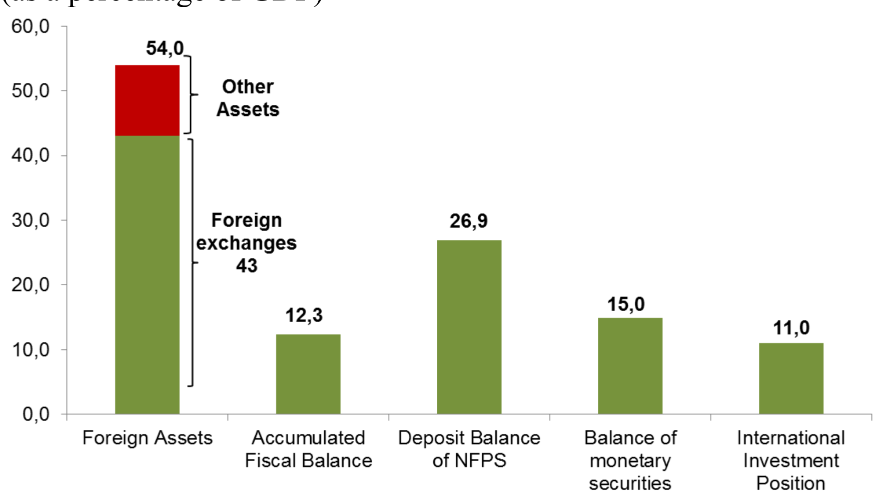
FSL include additional provisions and the possibility to increase the capital requirements. These prudential measures have resulted in a less vulnerable financial system to adverse scenarios.

The staff, without merit, emphasizes risks that microfinance institutions will face because of the FSL. On the contrary, all financial institutions (including the formal microfinance institutions outside ASFI regulation) continue to grow steadily and their profitability continues to be positive. Interest rate caps for loans have not negatively affected microfinance institutions.

Bolivian microfinance institutions are recognized and are seen as an example throughout the world. These institutions know how to deal with non-traditional guarantees and have proven able to adapt to changing conditions. Different studies in the region remark on the quantity and the quality of services provided. Resources that were lent to borrowers traditionally excluded by banks have had exceptional growth with a very low NPL ratio. All studies reach the same conclusion: the success of Bolivia's microfinance. For example, the CGAP Microfinance Gateway mentions Bolivia as the second country with the best conditions for the development of microfinance worldwide, because it has the lowest interest rates for customers and the lowest levels of NPLs. Another study by the IDB's Multilateral Investment Fund published in 2015, mentions Bolivia as the country with the highest level of microcredit penetration. Microcredit portfolio in terms of GDP amounted to 12 percent.

Mentioning a "perfect storm" for Bolivia is pure speculation, not based on any empirical model. Bolivia has had buffers for many years (Figure 2). Countries like Bolivia were using the fiscal space to build such buffers and applying growth-enhancing and social policies aimed to tackle poverty and inequality; however, if external conditions deteriorate Bolivia will be forced to use its accumulated buffers but growth-policy cannot be abandoned at a cost of reverting poverty to prior levels. The CBB's credibility cannot be lost for none of the reasons that the staff mentions. The staff's statements, as such, can cause damage to expectations of domestic and foreign economic agents and, therefore, the Bolivian economy.

Figure 2
Accumulated Buffers 2005-Sep 2015
(as a percentage of GDP)



The staff claims that financial entities would have difficulties reaching the credit quotas established by the FSL based on calculations of portfolio growth. However, as previously mentioned, the financial system has high liquidity ratios and enough capital to sustain credit growth. In addition, staff does not consider social housing credits for their estimates in quota calculation, which represents, up until September 2015, around 20 percent of the productive portfolio. Partial credit guarantees recommended by the staff, are not an innovation since they have already been applied since 2011.

The staff's assertion that financial inclusion may improve with market-based mechanisms has no technical support. Moreover, in the neoliberal period, when banking supervision was low, more than 12 large financial entities (such as Banco Sur, Cochabamba, BIDESA, Progreso, BBA, Potosi, Minero, and Agricola) failed between 1985 and 2000. Moreover, financial intermediation during this period was smaller than 2006 onwards. In the past, loans were mostly directed to consumption and services. At the same time, dollarization reached 97 percent in loans and 93 percent in deposits, which resulted in a very vulnerable financial system in which the CBB's role as lender of last resort was very limited and expensive.

Policy Recommendations

The Bolivian government does not agree with the IMF´s policy recommendations. Between 1986 and 2005 the six agreements with conditionality signed with the IMF did not solve Bolivia´s economic problems, expressed in twin deficits, important foreign reserve losses, high levels of foreign debt and a large financial dependence. On the contrary, since 2006, Bolivia has implemented its economic policies with sovereignty and will not follow any IMF policy recipe.