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IMF Concludes Article IV Consultation with Bolivia and Decides that Bolivia is Eligible for Debt Relief Under the HIPC Initiative

The IMF Executive Board on September 10, 1997 concluded the 1997 Article IV consultation[1] with Bolivia. It also decided that Bolivia would be eligible to receive debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative in September 1998. (The World Bank reached a similar decision on September 9, 1997).

Background

In 1996, Bolivia continued to implement a comprehensive stabilization and structural reform program begun in 1985 aimed at lowering inflation, promoting faster economic growth and reducing poverty. Output is estimated to have grown by 3.9 percent, while inflation was 8 percent by end year, as the price pressures that had emerged in 1995 eased substantially. Important progress was achieved in reforms of the public enterprises, health, education, and the pension system.

The combined public sector deficit was held to 1.9 percent of GDP in 1996 (only marginally higher than the 1995 deficit that was the lowest in the past 15 years). An increase in excise taxes on domestic petroleum products in January 1996, helped offset a decline in the operating surplus of public enterprises related to the capitalization of two enterprises in 1995, and official grants (many earmarked for external debt servicing) increased significantly. Under capitalization,

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

private investors acquire a 50 percent interest and management control of public enterprises in return for a commitment to undertake capital expenditure equivalent to the enterprise's net worth.

Structural reforms advanced in 1996 as three units of the state petroleum company (YPFB) were capitalized in December 1996. By end-1996, the capitalization program had generated commitments of US$1.7 billion of foreign direct investment over the period 1996-2002 (an average of about 2 percent of GDP a year). Also, the awarding of YPFB facilitated an agreement in December 1996 for the construction of a gas pipeline to Brazil between June 1997 and mid-1999 at an estimated cost of US$2 billion, with expenditures in Bolivia of US$450 million.

A comprehensive pension reform was adopted in November 1996 that privatized the old pay-as-you-go (PAYG) pension system and moved to a funded system, expanded the share of the workforce covered by the pension system and changed the structure of contributions and benefits to help ensure the viability of the private system.

As confidence in the domestic financial system improved, following the restructuring and recapitalization of troubled banks, the growth of broad money picked up from 9½ percent during 1995 to 25½ percent in 1996. Net international reserves increased by US$340 million, bringing gross reserves to US$1.1 billion the equivalent of seven months of imports and 94 percent of short-term liabilities of the central bank. Foreign direct investment (mostly in the capitalized enterprises) went up from about 2½ percent of GDP in 1995 to almost 6 percent of GDP in 1996, and gross domestic investment rose from 15½ percent of GDP in 1995 to 17 percent of GDP in 1996. The external current account deficit remained at about 5 percent of GDP, as nontraditional exports grew by 17 percent, and helped to offset strong import growth.

Also, the government continued to implement the education reform and started an integrated health care plan aimed to improve the coverage and quality of public services. The government introduced a new curriculum in 350 of the country's 1,800 school districts and distributed six million textbooks in Spanish and indigenous languages. In the area of health care, the government adopted a national program which provides a basic package of health services and free maternity and infant care, opened more local health centers in rural areas, and expanded its infant and child development program.

Looking ahead, the authorities aim to raise economic growth to 5½ percent by 1999, while lowering inflation gradually to 6 percent and preserving the international reserve cushion. The structural reforms of recent years are expected to promote increased savings, higher investment, and the development of a local capital market. Fiscal policy is designed to absorb the costs of recent structural reforms, most importantly the privatization of pensions. The current generation of structural reforms would be completed in 1997, and would be broadened to include steps to develop the local capital market and improve the efficiency of the labor market.

Within this medium-term strategy, the macroeconomic program for 1997 seeks to reduce inflation to 7 percent and to increase net international reserves by US$20 million. Output is projected to rise to 5 percent in 1997. The overall public sector deficit would rise to 3.3 percent of GDP in 1997 from less than 2 percent of GDP in 1995-96 (reflecting the short-term fiscal costs of structural reforms), while national savings would remain unchanged at 12 percent of GDP as the costs of the pension reforms are offset by pension contributions in the private sector.

Debt Relief Under the HIPC Initiative

The IMF decided that Bolivia was eligible for about US$448 million of debt relief under the HIPC Initiative (in net present value terms), which represents a reduction of about 13 percent in Bolivia's external public and publicly guaranteed debt. This decision was consistent with the preliminary deliberations of the Fund and the World Bank in April and with the views of the Inter-American Development Bank Board expressed in May, and was based on Bolivia's very strong policy track record since 1985 and the strength of its current economic program (see Press Release 97/41).

Executive Board Assessment

Executive Directors agreed with the thrust of the staff appraisal. They commended the authorities for maintaining strong macroeconomic policies and sustaining the momentum of structural reforms in 1996 and 1997, noting that Bolivia had one of the best implementation records in structural reform among ESAF countries. Those policies had contributed to lowering inflation, improving prospects for private investment, and to making further progress toward external viability. Directors noted, however, that real GDP growth had remained at about 4 percent—insufficient for substantial progress in reducing poverty—and that domestic saving, though rising, was still low. Therefore, further efforts were needed to consolidate the macroeconomic stabilization and deepen structural reforms, especially to tackle poverty and improve social conditions.

Noting that the program for 1997 aimed at a modest reduction in inflation to 7 percent during the year, Directors commented that a further decline in inflation would improve the environment for private sector-led growth, and urged the authorities to keep inflation on a downward path in the next few years.

Directors commented that the economic strategy for 1997–99 was centered on the pension reform and other structural changes, including increased spending on the social sectors, together with a fiscal plan to absorb the short-term costs of these reforms, with a view to promoting further growth in national saving and developing the local capital market. While a more rapid fiscal adjustment might have been preferable, Directors agreed that the fiscal plan included in the program was likely to enable Bolivia to secure the long-term benefits of these reforms, but they cautioned against any delay in the pace of fiscal adjustment.

Directors urged the authorities to keep government borrowing from the pension funds as low as possible to limit the growth in the government's domestic debt, and to help ensure that a large proportion of the savings of the pension funds was channeled to private investment. They stressed the importance of a careful monitoring of public expenditures, particularly by local governments, to avoid any slippages in fiscal policy. They encouraged the authorities to stand ready to take fiscal measures if signals, such as higher-than-expected import growth, began to suggest an excessive expansion in domestic demand.

Directors felt that credit restraint remained an important element of the program. They noted that the current exchange rate policy had served Bolivia well, but some Directors were concerned that the levels of external current account deficit projected for 1997 and 1998, while reflecting a surge in foreign direct investment, did involve some risk. In that context, they emphasized the importance of keeping fiscal, monetary, and particularly exchange rate policies under close review.

Directors welcomed the government's commitment to completing the structural reforms that would transform the role of the state in the economy, and encouraged the authorities to continue privatizing public enterprise assets, to intensify customs reform, strengthen the legislative and regulatory framework to promote the local capital market, and to seek improved flexibility in the labor market. Directors emphasized the importance of the planned intensification of the government's social and anti-poverty programs, particularly in the context of Bolivia's participation in the HIPC Initiative. Directors noted the considerable progress in resolving financial sector difficulties in 1996, and supported the authorities' plan to strengthen the financial system further. In their view, it was important to maintain vigilant bank supervision, and to implement fully and on schedule the planned measures to tighten prudential requirements and strengthen banks' capital.

Press Information Notices (PINs) are a new series of IMF press notices (see Press Release 97/21). PINs are issued, at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies.

Bolivia: Selected Economic Indicators

	1993	1994	1995	1996
		In percent		
Domestic Economy				
Change in real GDP	4.1	4.6	3.9	4.0
Deflator	7.5	7.8	12.9	12.7
Change in consumer prices (end of period)	9.3	8.5	12.6	8.0
		In millions of U.S. dollars 1/		
External Economy 2/				
Exports; f.o.b.	710	998	1,075	1,132
Imports; f.o.b.	1,154	1,276	1,376	1,578
Current account balance	-419	-219	-336	-385
Capital account balance	341	209	257	727
Direct investment	122	90	177	426
Gross official reserves	495	658	737	1,138
In months of imports	4.7	5.7	5.6	7.8
Current account balance (in percent of GDP)	-7.3	-3.6	-5.0	-5.1
External debt (in percent of GDP)	74.3	77.9	71.7	61.9
Debt service ratio 3/	48.6	35.3	42.2	25.4
Change in real effective exchange rate (in percent) 4/	-0.7	-9.8	3.5	2.4
		In percent of GDP 1/		
Financial Variables				
Overall public sector balance	-6.0	-3.0	-1.8	-1.9
Change in broad money (M3)(in percent)	36.4	21.6	9.5	25.8
Interest rate (in percent) 5/	10.2	9.6	11.3	9.0

Sources: Bolivian authorities; and IMF staff estimates.
1/ Unless otherwise noted.
2/ Balance of payments data for 1994-96 are not strictly comparable with those for previous years because of changes in the way imports and other components are estimated.
3/ After debt relief. In percent of exports of goods and non-factor services.
4/ (+) = appreciation.
5/ Foreign currency bank deposits.