

**IMMEDIATE
ATTENTION**

SM/11/85
Supplement 3

May 5, 2011

To: Members of the Executive Board

From: The Secretary

Subject: **Bolivia—Staff Report for the 2011 Article IV Consultation—Draft Public Information Notice**

Attached for consideration by the Executive Directors is the draft Public Information Notice (PIN) relating to the staff report for the 2011 Article IV consultation with Bolivia (SM/11/85, 4/29/11), which is being considered on a lapse of time basis. In the absence of a request for a Board discussion by **noon on Wednesday, May 11, 2011**, the Executive Board Assessment section of the PIN will be based on the staff appraisal, as attached.

At the time of circulation of this paper to the Board, the authorities of Bolivia have indicated that they need more time to consider whether they will consent to the Fund's publication of this paper. Publication will only proceed upon the receipt by the Fund of the member's explicit consent. Any requests for modifications for publication are expected to be received two days before the Board concludes its consideration.

Questions may be referred to Mr. Lopetegui (ext. 39688), Mr. Rosales (ext. 38688), and Ms. Sulla (ext. 38766) in WHD.

Unless the Documents Section (ext. 36760) is otherwise notified, the document will be transmitted, in accordance with the procedures approved by the Executive Board and with the appropriate deletions, to the WTO Secretariat forthwith; and to the European Commission, the European Investment Bank, and the Inter-American Development Bank, following its consideration by the Executive Board.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

Att: (1)

Other Distribution:
Department Heads



INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL
RELATIONS
DEPARTMENT

Public Information Notice (PIN) No. 11/xx
FOR IMMEDIATE RELEASE
May 13, 2011

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

IMF Executive Board Concludes 2011 Article IV Consultation with Bolivia

On [May 13, 2011], the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Bolivia, and considered and endorsed the staff appraisal without a meeting.¹

Background

Bolivia has posted a solid macroeconomic performance in recent years, on the back of strong terms of trade and prudent macroeconomic policies. Increased export volumes and prices led to a doubling of export receipts between 2005 and 2010, while real GDP growth rose from 3.1 percent in the first half of the past decade to 4.6 percent in the second half. The strength of the external and fiscal positions in recent years has allowed Bolivia to build a strong reserves cushion which has reduced macroeconomic vulnerability. While poverty and income inequality are still high, progress has been made on improving social inclusion and income distribution, as cash transfer programs have been successful in reducing extreme poverty, from about 30 percent in 2008 to 26 percent in 2009.

In 2010, real GDP grew by 4.2 percent on account of higher hydrocarbons production, with high terms of trade supporting domestic demand, and despite adverse weather shocks. The external current account surplus rose to 4.8 percent of GDP, and net international reserves currently stand at 50 percent of GDP and 80 percent of broad money. At the same time, inflation rose sharply, to 7.2 percent in December and 11 percent in March 2011, on the back of higher food commodity prices, some de-anchoring of expectations following an attempt at raising fuel prices

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

last December, and amid ample liquidity in the banking sector. The overall public sector surplus rose to 2.0 percent of GDP in 2010, from 0.3 percent in 2009.

With the pickup in inflation, interest rates have become sharply negative in real terms. In the context of higher credit growth, banks are profitable, well capitalized, and their nonperforming loan ratios are low. Progress on the de-dollarization of balance sheets has continued, with Boliviano-denominated credit and deposits standing at about 55 percent of the total.

Congress has approved a road map for fiscal decentralization and a reform of the pension system. The decentralization law sets the stage for a discussion of revenue assignments and spending responsibilities across different levels of government. The pension reform creates a semi-contributory regime with stepped up benefits for low-income households, funded with higher contributions from employers and employees. It also introduces a lower retirement age and nationalizes the administration of the pension funds.

Executive Board Assessment

In concluding the 2011 Article IV consultation with Bolivia, Executive Directors endorsed the staff's appraisal, as follows:

Despite adverse weather shocks, the Bolivian economy performed well in 2010. Real GDP growth rose, supported by favorable terms-of-trade and higher hydrocarbon production and exports. The external current account and public sector balances remained in surplus, and net international reserves climbed to new record highs, providing strong protection to face external shocks. The financial sector remains sound, with low nonperforming loans and adequate provisioning.

However, there has been a resurgence of inflation that will require policy adjustments to bring it back under control. While higher international food prices have been a key driver of inflation, easy monetary conditions have contributed to more generalized price increases. With the fiscal impulse envisaged for 2011, the central bank should exit faster from the very strong monetary stimulus provided over the past two years. A more rapid appreciation of the currency, which is estimated to be moderately undervalued, would also help reduce external inflationary pressures.

The growth outlook for 2011 is favorable. Real GDP growth is expected to gather further momentum, reflecting the continued recovery of hydrocarbon production, higher public investment, and very favorable export prices. The external current account and the fiscal balance are expected to remain in surplus.

Given the strength of public financial cushions and the favorable outlook for gas prices, there is fiscal space to undertake additional public investment, provided that efforts continue to boost its effectiveness. Staff projects that, under current policies, public debt will be on a downward path over the next few years. As Bolivia's cushions are already strong, the authorities could take the opportunity to increase productive and social investment—while containing current

expenditure—to address development needs. This will require stepping up efforts to ensure the effectiveness of public spending and enhancing implementation capacity across all levels of government.

The authorities are encouraged to continue their reforms to the policy framework to improve policy responses to changing economic conditions. Multi-year budgeting will strengthen fiscal policy and improve investment planning. The establishment of a fiscal savings fund should proceed expeditiously, as it would facilitate anti-cyclical fiscal policy. At the same time, it would limit risky fiscal claims on the central bank, which is an important precondition for credible and effective monetary policy. As lower dollarization becomes more entrenched and domestic financial markets develop further, the authorities should move towards greater exchange rate flexibility.

The FSAP update has revealed important improvements in the financial sector, although further strengthening of macro-financial stability will require policy actions. The authorities need to manage a soft landing from historically-low interest rates while ensuring that appropriate levels of bank liquidity are maintained. Capital buffers need to be sustained through regulation focused on risks faced by banks rather than on developmental objectives. Further efforts are needed to align resources, capacity, and processes to the growing responsibilities of the financial sector supervisor, while ensuring its adequate independence. The central bank has effective mechanisms to provide liquidity and the bank the resolution framework is in line with best practices. However, the crisis management framework could be strengthened with a deposit insurance scheme to protect small depositors in the event of bank liquidation. AML/CFT regulations and practices should be strengthened to comply with international norms.

Sustaining high and stable medium-term growth will require improvements in the investment climate. Bolivia has yet to reverse the drop in private investment levels that began in the early 2000s. Key challenges include the adaptation of the legal framework for natural resources and private investment to the mandates of the Constitution in a way that ensures clear and stable rules of the game for the private sector.

Social policies have been effective and Bolivia has made inroads towards achieving MDGs. Going forward, while strengthening current programs and enhancing the delivery of health and education services, there is a need to improve the targeting of transfer programs. In particular, success in removing generalized fuel subsidies and allowing prices signals to stimulate agricultural production will depend upon the ability of the state to deliver adequate compensatory measures to the most vulnerable groups.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

Bolivia: Selected Economic Indicators

				Prel.	Proj.
	2007	2008	2009	2010	2011
(Annual percentage changes)					
Income and prices					
Real GDP	...	4.6	6.1	3.4	4.2
GDP deflator	...	7.4	10.4	-2.4	6.3
CPI inflation (period average)	...	8.7	14.0	3.3	2.5
CPI inflation (end-of-period)	...	11.7	11.8	0.3	7.2
(In percent of GDP)					
Combined public sector					
Revenues and grants	34.4	38.9	36.1	33.9	34.8
<i>Of which:</i>					
Hydrocarbons related revenue	9.4	13.4	13.1	10.9	11.4
Expenditure	31.8	34.6	35.5	31.9	34.1
Overall balance	1.7	2.8	0.3	2.0	0.7
Total gross public debt	40.9	37.5	40.5	39.9	36.2
External sector					
Current account	12.0	12.1	4.7	4.8	3.8
Merchandise exports	33.5	38.8	28.2	32.5	30.3
<i>Of which: Natural gas</i>	14.8	19.0	11.3	14.4	14.3
Merchandise imports	26.0	30.0	25.4	27.7	26.3
Gross international reserves					
In millions of U.S. dollars	5,319	7,722	8,580	9,730	10,440
In percent of broad money	75	85	81	80	74
(Changes in percent of broad money at the beginning of the period)					
Money and credit					
NFA of the banking system	35.4	34.6	10.2	8.2	7.4
NDA of the banking system	-3.7	-12.5	6.6	6.0	2.3
<i>Of which: Credit to the private sector (in percent of GDP)</i>	33.1	30.3	33.0	32.4	35.3
Broad money	31.7	22.2	16.8	14.2	9.7
Interest rates (percent, end-of-period)					
Deposits in local currency 61-90 days	3.7	5.7	0.4	0.5	...
Deposits in foreign currency 61-90 days	2.6	3.3	0.5	0.2	...

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