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October 26, 2018

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From: The Secretary

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INTERNATIONAL MONETARY FUND

BOLIVIA

SELECTED ISSUES

October 26, 2018

Approved By
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APPENDICES

ENCOURAGING EXPORT DIVERSIFICATION IN BOLIVIA

Many developing countries have achieved higher sustained rates of growth driven by export diversification.[1] The trend in emerging and developing economies (EMDEs) around the world is toward export diversification.[2] The government of Bolivia has implemented a state-led industrialization strategy funded by hydrocarbon revenues that aimed to increase economic diversification, although exports have become less diversified since 2000. This note examines recent trends in Bolivia in a global and empirical context using the IMF Exports Diversification and Quality database and considers ways to create an environment that will encourage the expansion of economic activity into new sectors and toward export diversification. The success of small manufacturers is found to be a key factor, pointing to the importance of structural reforms that facilitate and support their development.

A. Introduction: Global Trends and Bolivia's Experience

1. The global trend is toward greater diversification of exports. Countries that have successfully moved up the income ladder have promoted, and experienced, export diversification. In the 1970-1980s, policies were often directed more at import substitution with extensive use of restrictive trade policies and tariffs to encourage domestic production. Recent empirical studies and policy research have found that structural reforms that facilitate private sector growth and an open trade regime have been more effective at promoting export diversification (Cherif *et al,* 2016, Samen 2010).

2. For most commodity exporters, however, export diversification has been elusive. With external and fiscal revenues heavily dependent on commodity exports, they are more vulnerable to external shocks. Policymakers have worked to redistribute commodity export revenues and reduce this vulnerability by broadening the export base and upgrading to higher value-added products. In general, however, their export base remains the least diversified among EMDEs.

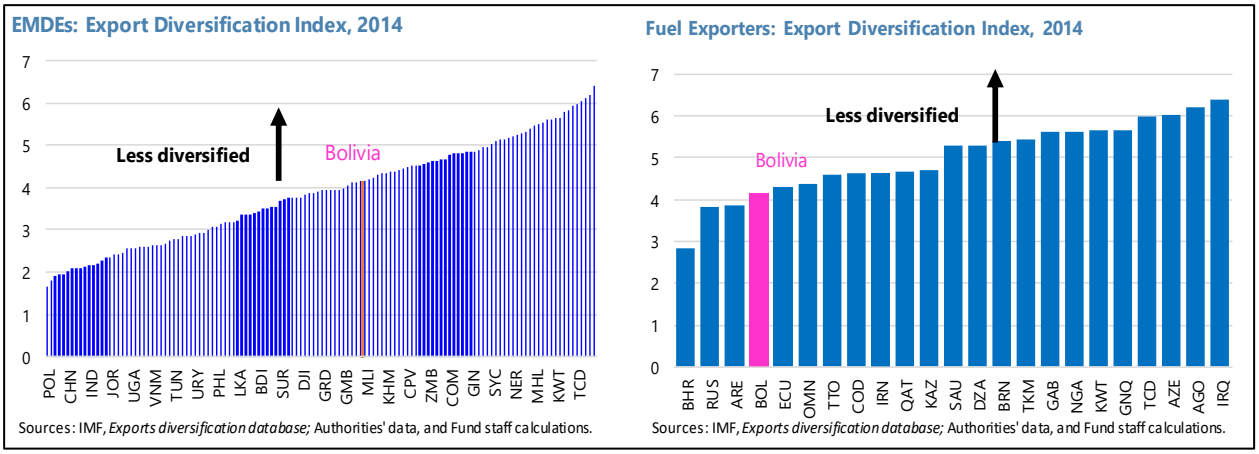
3. Bolivia is an interesting case. The economy is more diversified than most other hydrocarbon exporters and the level of export diversification is around the median among EMDEs. Bolivia achieved some progress in the 1990s, but export diversification declined after 2000 with the development of the hydrocarbon sector, while other EMDEs showed a trend in the opposite direction. This trend has continued in Bolivia since the drop in commodity prices in 2014.

4. The authorities in Bolivia recognize the importance of economic diversification. Their Patriotic Agenda 2025 and 2016-2020 Economic and Social Development Plan (PDES) lay out an

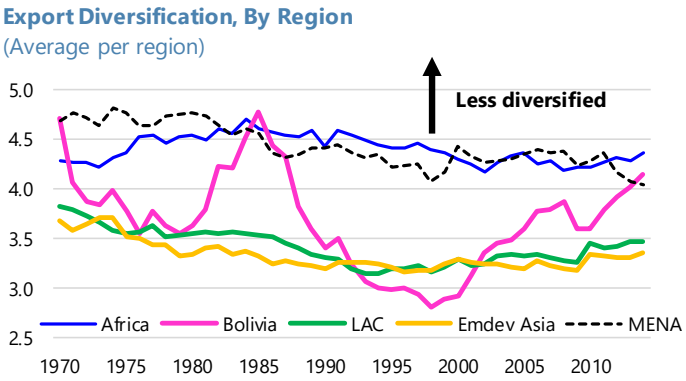
[1] Prepared by Marie Kim, with comments from Nicole Laframboise and Fuad Hasanov.

[2] This study uses 'Theil' Indices of export diversification following definitions and methods used in Cadot *et al* (2011) and export diversification and 'quality' data from the IMF "Export Diversification and Quality Database" that ensures consistency in cross-country analysis. See (https://www.imf.org/external/np/res/dfidimf/diversification.htm).

an economic model and approach to support this objective.[3] Among the principal goals that were to be met by 2020, Bolivia aimed to introduce new sectors and products, including by promoting the development of small producers and community/cooperative sectors.[4] The main action though has been in state-led, capital-intensive industrialization, including to develop derivative products from the hydrocarbon sector, such as urea. They are currently developing renewable energy sources and increasing hydroelectric potential to export hydro-electric power. Other efforts to introduce higher value-added goods, such as lithium-based batteries, are underway. In other productive sectors where smaller producers would be more likely to operate, like agro-processing or textiles, the strategy has included promoting import substitution.



5. Despite efforts to diversify the economy, export diversification has declined in recent years. The purpose of this study is to examine and understand trends to better inform macro-structural policy advice. Section B surveys the literature on the role of export diversification in economic development; section C explains the history and structure of Bolivia's economy; section D analyzes the factors that could reverse the de-diversification trend in Bolivia; and section E draws conclusions and proposes four ingredients to get Bolivia back on the pro-export diversification track.



Sources: IMF, *Exports diversification database;* Authorities' data, and Fund staff calculations.

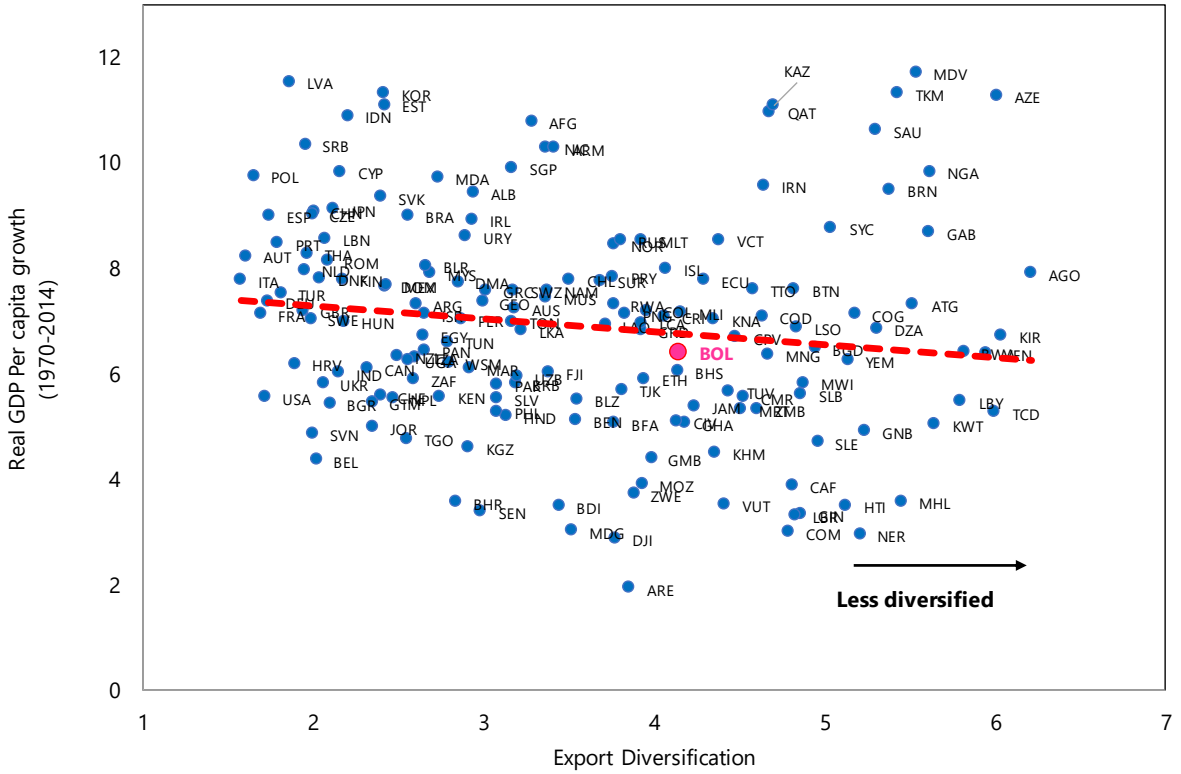
[3] The *PDES* is currently being reviewed and the revised plan is expected by December 2018.

[4] Pillar 6 of the Patriotic Agenda 2025: *Soberanía Productiva con Diversificación y Desarrollo Integral sin la Dictadura Capitalista*. Ministry of Development Planning (2016), *Plan de Desarrollo Económico y Social: En el Marco del Desarrollo Integral para Vivir Bien 2016-2020*, La Paz.

B. Export Diversity—A Not-So-Simple Concept

6. Export diversification is associated with higher real GDP per capita (IMF, 2014)**.** Quantifying the impact of export diversification on growth is complicated by the numerous feedback loops between the two indicators. After controlling for possible endogeneities, Fund staff (2014) concluded that export diversification is a potential growth determinant (McMillan and Rodrik, 2011, and Lin, 2012).[5] Developing economies often rely on a narrow range of traditional primary goods, where technical inputs are limited and the productivity benefits from technology transfer spill over less to other sectors and potential growth. A few examples of successful diversification this way include the East Asian Tigers in the 1970-1980s and several ex-Soviet Union countries in the 1990s, where agriculture-based exports were transformed into more diverse, higher 'quality' manufactured exports (IMF 2014).

Growth and Export Diversification

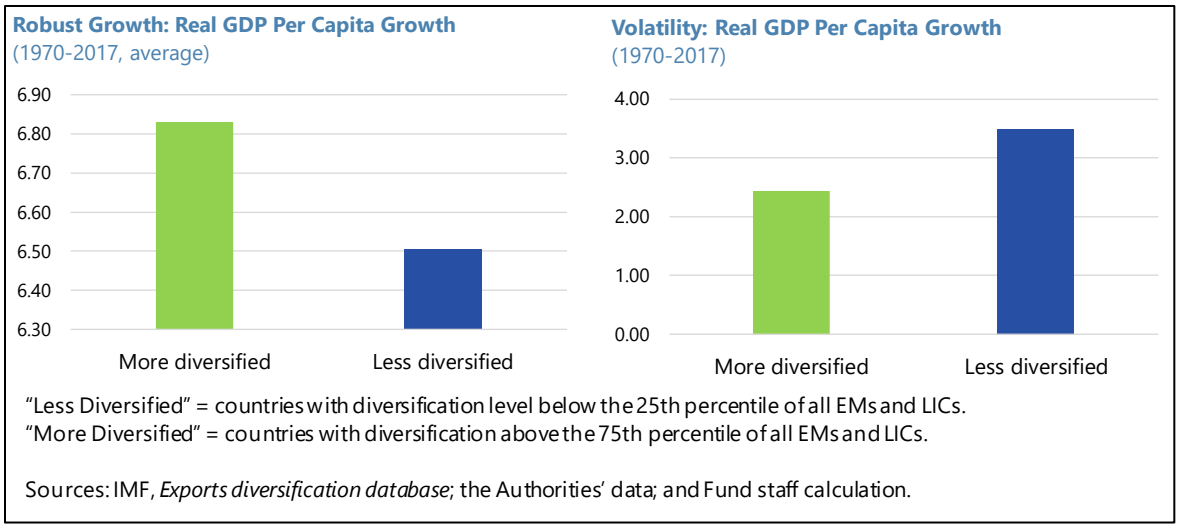


Sources: IMF Export diversification database; andFund staff calculations.

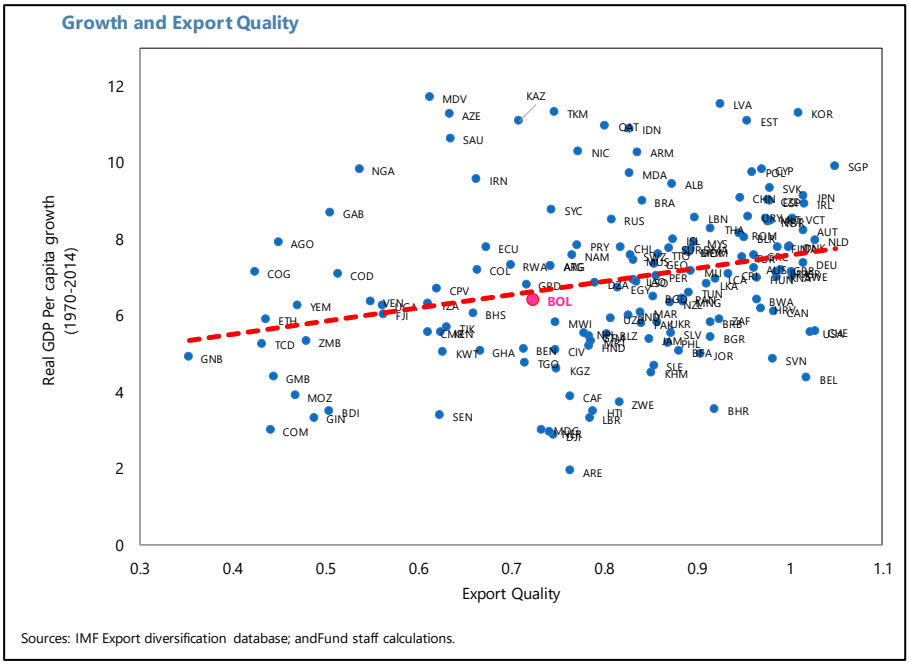
7. Export diversification is also associated with more stable growth. More diversified exports can help shield the economy from external and idiosyncratic sectoral shocks. This is particularly so for primary product exporters, which are vulnerable to negative terms-of-trade

[5] The empirical model controlled for possible endogeneity—to ensure that export diversification does indeed drive up growth, not the other way around—and included all relevant candidates for growth determinants (IMF 2014).

shocks. Analyzing the growth pattern between the most and least diversified country groups, real GDP per capita growth is found to be higher and more stable for those in the more diversified group.



8. 'Quality' upgrading is associated with higher growth per capita (Henn, Papageorgiou, & Spatafora, 2013). An increase in export 'quality' involves raising institutional, human, and technological capacity, all of which have positive implications for economic growth since they typically boost productivity growth. Diversification and 'quality' upgrading should be viewed as complementary in the growth development process. Hwang (2007) argues that countries need to enter sectors with long "quality ladders" that they can climb over time. This does not mean that producing higher 'quality' goods means abandoning production of existing goods at prevailing 'quality'. Instead, the process of expanding the range of goods exported, and upgrading 'quality' should be complementary (Box 1).



Box 1. Understanding Export Terms

The IMF Export Quality Database covers 166 countries over the period 1960–2014 using COMTRADE trade values and quantities at the SITC 4-digit level (Standard International Trade Classification-SITC).[1] 'Quality' is unobservable and higher export 'quality' is assumed to be sold at a higher price. IMF (2014) derives export 'quality' based on export prices, adjusted by: (i) the export country's income *per capita,* to capture production costs; and (ii) the distances between countries to control for higher transportation costs in export prices.

The term export 'sophistication' is also used in the literature. 'Sophistication' and `quality' are related to some extent. 'Sophisticated' exports, as identified in Hausmann *et al.* (2007), are associated with higher productivity levels and per capita incomes, and can be an important contributor to overall growth. Cherif *et al* (2018) found that export `sophistication' is the key determinant of growth among the other standard determinants, including human capital and institutions. Intuitively, the typical export basket of high-income countries would likely be viewed as relatively 'sophisticated' as compared to that of a lower-income commodity exporter.

[1] IMF "Export Diversification and Quality Database" that ensures consistency in cross-country analysis. See (https://www.imf.org/external/np/res/dfidimf/diversification.htm or http://data.imf.org/exportquality)

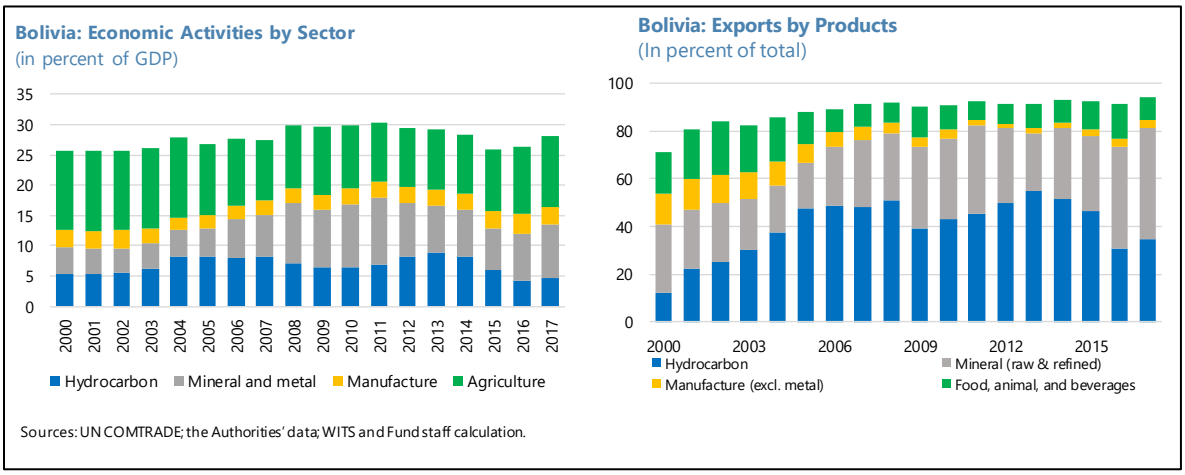
C. The Structure of Bolivian Trade

Since 2000, Bolivia has experienced strong and stable growth. GDP per capita increased from US$1,000 to US$3,400 and growth has been stable, averaging 4.3 percent annually despite sizeable negative terms-of-trade shocks. With that record, why would it be important for the landlocked country to diversify? Fiscal and external revenues have become more dependent on hydrocarbons while the terms of trade forecast is negative over the medium term (WEO 2018). Continued accommodative policies to support growth are not sustainable and a different growth strategy is needed to move towards a more business-friendly, private investment driven model, away from dependence on minerals and hydrocarbons. Recent research finds that export diversification and higher 'quality' exports hold the keys to broad-based growth in real incomes.

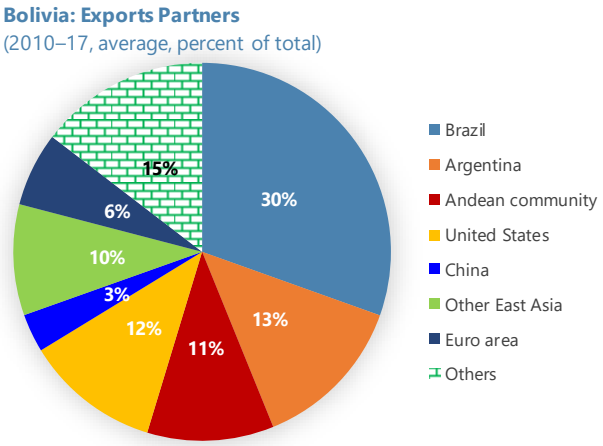
9. Bolivia has always had vibrant economic activity in the mining and hydrocarbon sectors. Minerals and metals have been a dominant feature of Bolivia's economy since the 16th century when the city of Potosí was the main supplier of silver to the Spanish Empire. Since natural gas production surged in the mid-2000s, the structure of the economy shifted: activity in the hydrocarbon and mineral sectors increased from about 10 percent of GDP in 2000 to 17 percent of GDP in 2014, at the peak of the commodity boom. Over the same period, the traditional tradable sector, particularly agriculture, declined by 3 percent of GDP.

10. Exports of manufactures fell significantly while minerals and natural gas exports expanded. Natural gas exports contributed about one half of total exports, on average, during 2010-2015 and mineral exports, mainly zinc, silver, and tin, contributed about one third. Exports of

manufactures were led by soya derivatives and, more recently, fuel products. Although economic activity in manufacturing has remained relatively stable, exports of manufactured goods declined more noticeably after 2004. The authorities implemented some import substitution policies, namely high import tariffs on manufactured goods and some export restrictions aimed at protecting domestic producers and securing supplies to meet domestic demand. These are likely to have contributed to the decline in exports of manufactured good (Section D).



11. Bolivia's products are mainly exported to South America, and to a lesser extent Europe and Asia. Brazil has been the main export destination followed by Argentina, although their main import is natural gas. Nontraditional exports to these countries is smaller than 5 percent of total exports (or 0.2 percent of Bolivia's GDP). Brazil and Argentina account for almost 45 percent of Bolivia's total exports and the Andean community—Colombia, Peru, and Ecuador—accounts for 11 percent.



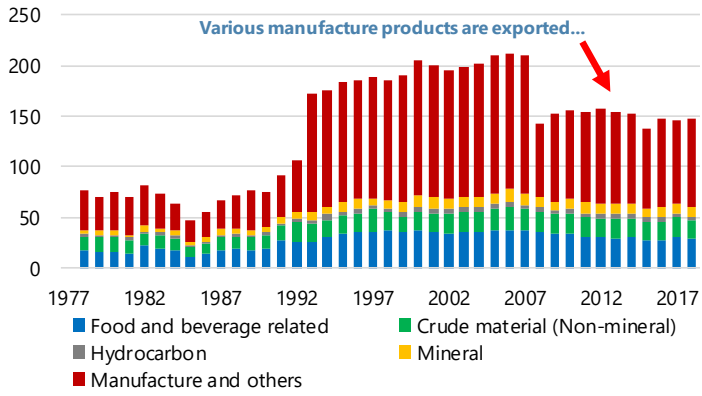
Sources: IMF Direction of Trade database;and Fund staff calculations.

D. What Explains the Level of Export Diversification?

12. Export revenues are driven by two main sectors, although Bolivia exports many different types of goods (Box 2). Trade data with SITC3 digits in 2017 shows that Bolivia exported 147 different items, of which 60 percent were manufactured goods. This supports Bolivia's measure of export diversification under the "extensive margin" concept as the country exported an array of

different products.[6] However, these manufactured goods are produced and exported on a very small scale and explain only 3 percent of total exports, while minerals and hydrocarbons together explain 81 percent of goods exports. This export composition explains weak "intensive margin" and contributes to low export diversity (Box 2).

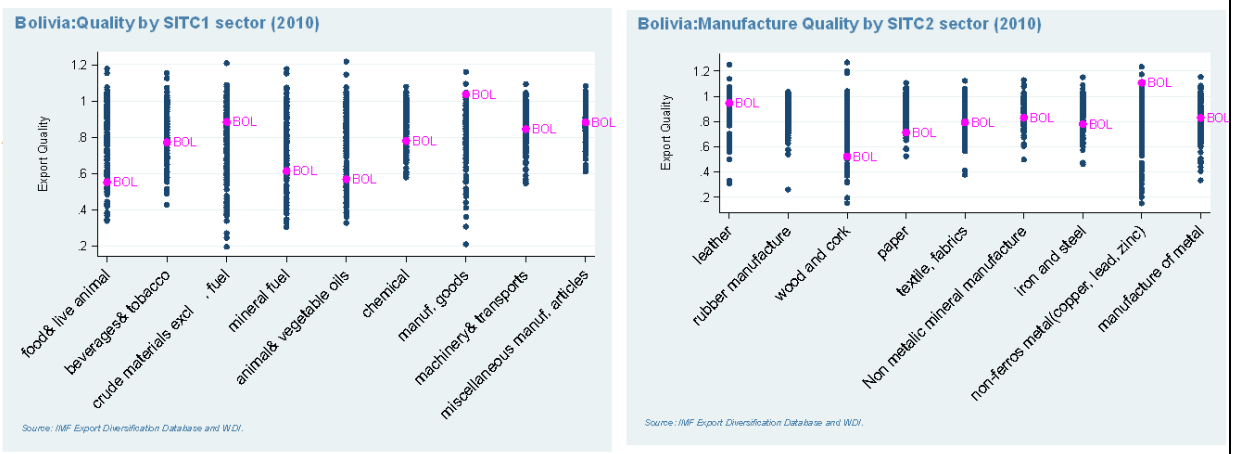
Bolivia: Number of Exports



Sources: UN COMTRADE; the Authorities' data; WITS and Fund staff calculation.

13. Bolivia's export 'quality' varies by sector, although overall 'quality' is low. This is explained by the dominance of a few large export sectors: agriculture, minerals, and hydrocarbons. Export 'quality' in manufactured goods appears to be generally high, but this is explained mostly by one subsector (SITC 2)—metals, which alone pushes up 'quality'. Other nontraditional manufactured goods tend to have low 'quality'. In general, analyzing sectoral data suggests that a country can improve overall export 'quality' in two ways: (i) by improving the `quality' of goods that represent a large share of the total; or (ii) by increasing the volume of exports that have already achieved higher `quality'. In this context, Bolivia could increase the 'quality' of existing agriculture products or increase export volume of higher 'quality' products, such as leather and textiles.

Bolivia: Export Quality by Sector



Sources: UN COMTRADE; the Authorities' data; WITS and Fund staff calculation.

[6] This basic classification, known as SITC 3, groups all commodities into headings suitable for economic analysis. SITC is recommended by the United Nations in the classification of external trade data with the aim of promoting international comparability of trade statistics. SITC 3 has more detailed groups of commodities than the SITC2 category (see ¶13).

Box 2. The Concepts of 'Intensive' and 'Extensive' Margin

Following Henn et al. (2013), export product diversification is measured by the Theil index which can be decomposed into "between" and "within" sub-indices:

$$Theil\ Index = \frac{1}{N}\sum \frac{Export\ value_i}{Average\ Export\ value}\ln\left(\frac{Export\ value_i}{Average\ Export\ value}\right)$$

$$Theil\ Index = Theil\ Index_{between} + Theil\ Index_{within}$$

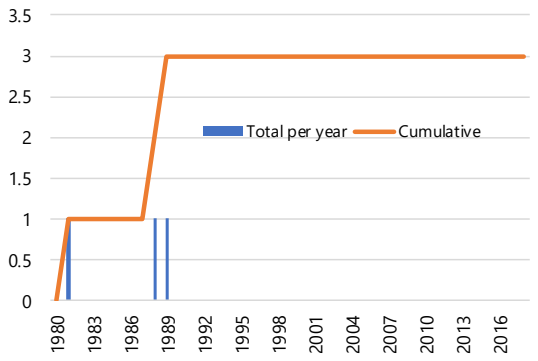
… where i represents the product index and N the total number of products. The "between" Theil index captures the *extensive margin* of diversification, i.e., the number of different types of products. The "within" Theil index captures *intensive margin*—product shares in total exports.

Intuitively, extensive margin (between) measures the number of different export goods, which reflects also ongoing development of new products, while intensive margin represents the balance of existing export goods.

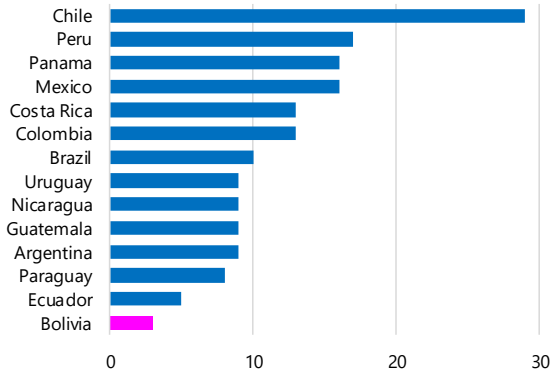
Although countries can stimulate growth by increasing both the extensive and intensive margin, there is some evidence showing that EMDEs would benefit from increasing diversification at the extensive margin. However, this is not the case for Bolivia, where high intensive margin has been driving the decline in diversification. In Bolivia, exports of hydrocarbon and minerals have been the dominant export revenue, even though the country exports a wide variety of different goods.

14. Most of Bolivia's exports go to a few key markets in the region. Compared to neighboring countries that have engaged actively in regional trade agreements, Bolivia has joined very few multilateral trade pacts, having signed only three regional agreements with the last one dating from 1988 under the Global System of Trade Preferences among Developing Countries (GSTP). Bolivia has signed a few bilateral trade agreements, but these are focused narrowly on Central or South America (Trade Policy Review, 2017).

Bolivia: Regional Trade Agreements



Number of Regional Trade Agreements



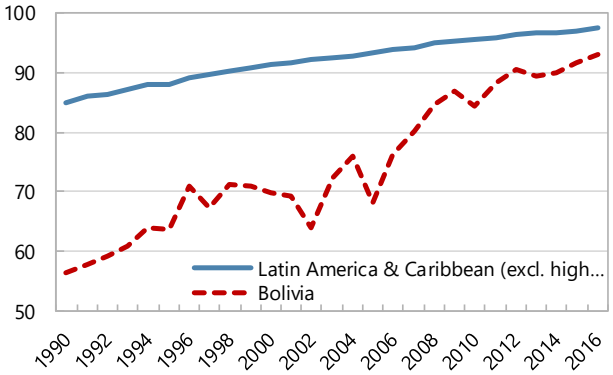
Sources: World Trade Organization, RTA database; Fund staff calculations.

E. Four Pillars to Support Enhanced Export Diversification and Quality

To support greater export diversification, policies should focus on ways to improve export 'quality' and raise 'intensive' margin in Bolivia's export basket. Given the existing export profile, this would involve creating an environment that facilitates and encourages the expansion of production and exports by small and medium-sized producers in particular. To build this foundation, structural reforms could focus on building four pillars: (i) good infrastructure to help lower transportation costs to promote exports; (ii) flexible labor and goods markets; (iii) stronger institutions to motivate technology; and (iv) a more open trade policy to promote competition.

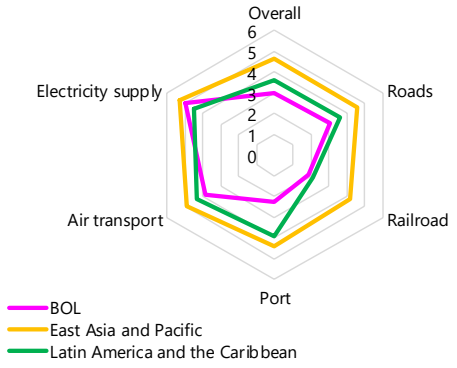
15. Robust infrastructure. This is an essential ingredient for promoting trade because it significantly lowers business operating costs. While the state of infrastructure in Bolivia has improved significantly since 2000, trade-related infrastructure is still weaker than in regional peers, in part due to high costs associated with the land-locked geography. In per capita terms, "access" to roads is relatively strong (International Roads Federation), but the quality of transport and logistics is found to be weak (World Bank, 2018).[7] More recently, staff found the efficiency of public investment to be relatively low, suggesting scope to prioritize capital spending in areas that support exports, while strengthening the effectiveness of investment (Annex V, Country Report No. 17/395).

Access to electricity
(% of population)

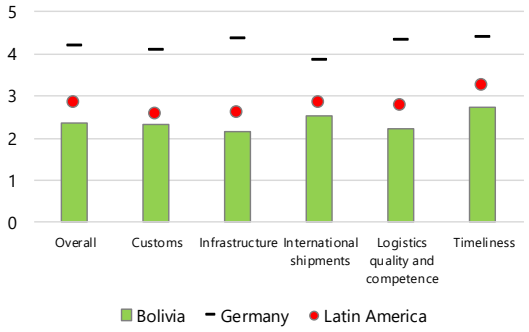


Source: World Bank - World Development Indicators

Quality of Infrastructure
(High index indicates better)



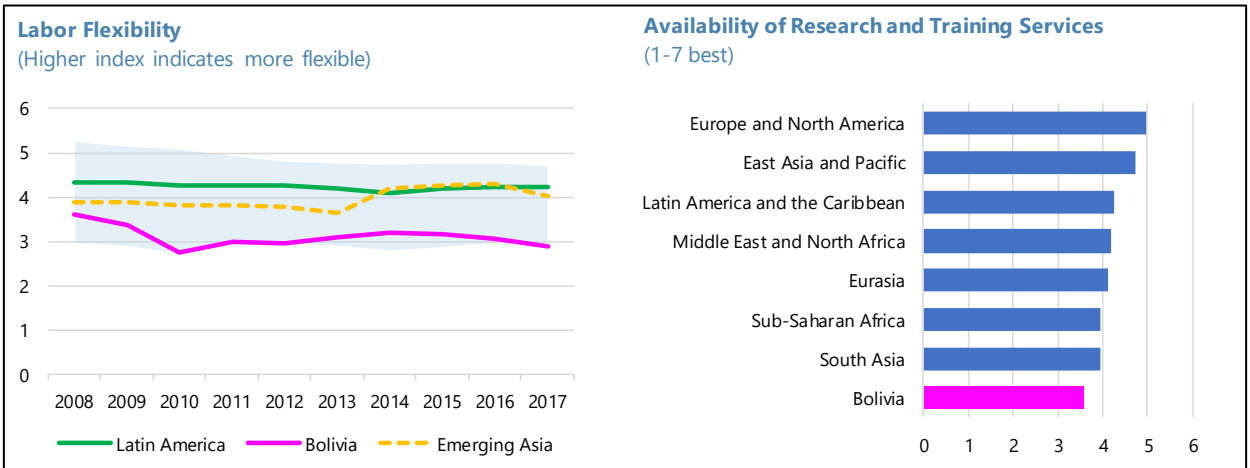
The Logistic Performance Index
(1-7 better, 2018)



Sources: World Economic Forum, *Global Competitiveness Report (2016-2017)* ; World Bank, *Logistic Performance Index (2018)* ; Fund staff calculations.

[7] WEF Global Competitiveness Index is a perception-based indicator, measuring the quality of infrastructure on an absolute scale of 1-7. For example, 'electricity supply' is a measure of electricity free from interruptions and shortages so that businesses can work uninterrupted. WDI measures the percent of the population with access to electricity.

16. A more agile labor market. Labor market regulations are extensive, adding significant cost and uncertainty to business and thereby deterring employment and formality. For example, the 2009 Constitution makes it extremely difficult to adjust the number of employees in a firm, something essential for efficient and fluid business operations, and directs the state to resolve conflicts between employers and employees (Articles 49.3 and 50), an unwieldy prospect in an efficient private sector. There are many other regulations, such as a limit on the number of foreign nationals allowed in any firm of 15 percent of the total. Overall, a more updated labor code that sets strong minimum standards for workers' rights and benefits, accompanied by minimum wage laws, would be a much stronger basis for a well-functioning labor market. It could preserve existing rights under current laws, for instance those guaranteeing the rights of association and to organize and bargain collectively. A modern and transparent wage determination process would also help firms compete based on costs and quality (see Staff Report).



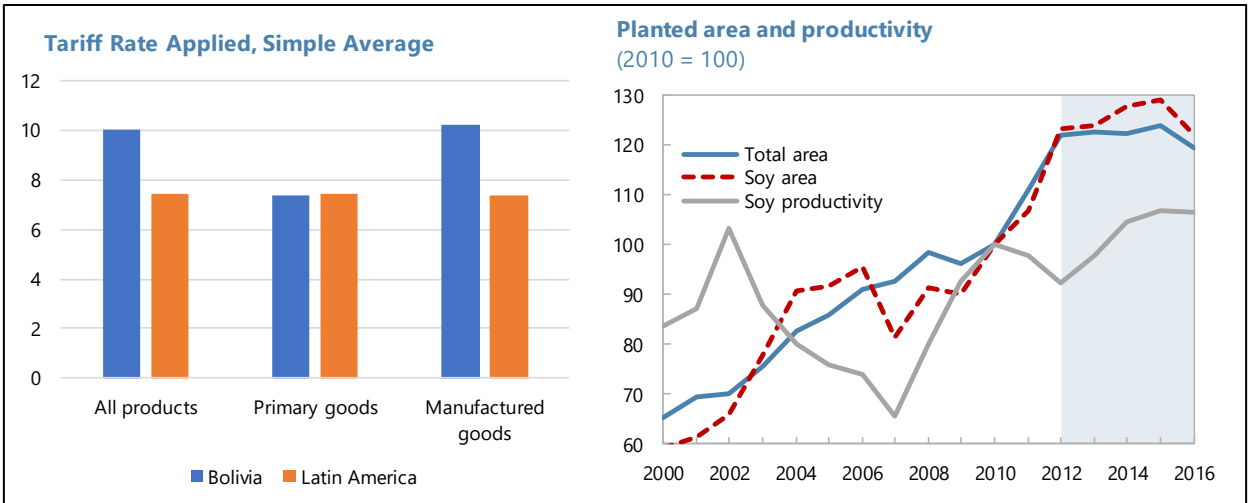
Sources: World Economic Forum, *Global Competitiveness Report (2016-2017)* ; World Bank, *Logistic Performance Index (2018)* ; Fund staff calculations.

17. Strong institutions to motivate technology innovation. According to several international surveys (e.g., the Global Competitiveness Index Report 2016-2017), Bolivia's institutions do not adequately protect intellectual property and investors, a foundation of private investment in the promotion of technology-based productivity growth. While Bolivia's primary education level is on par with peers, research and training availability is low and could reap significant returns.

18. An open trade regime. This will help expand the number of products and raise efficiency.

- **Reduce import tariffs.** Many countries tend to protect (domestic) agriculture production against imports. In Bolivia, the highest average tariffs of 40 percent are on clothing while the average tariff on agriculture products is 11.1 percent. This protection, which is much higher than the regional average, stifles investment and the spread of technological advances. The government could lower tariffs while taking offsetting measures, including promoting exports and competition by providing training or research support to local companies to help bring export `quality' into line with international markets. Advancing efforts to join more bilateral and regional free trade agreements is also worth considering.

- **Phase out export restrictions.** Free export of goods is guaranteed except in cases where the government has concerns about sufficient supply for the domestic market. When restrictions were lifted on products like sugar and chicken in December 2017, exports of these products rose in 2018. Soya derivatives, once Bolivia's major export representing about 3-4 percent of GDP, are still under restrictions. The private sector noted that quota limits complicate planning about how much to invest and produce. A direct result of this is a decline in the area under soya harvest since the law was introduced in 2010. (The existence of managed supplies to influence prices has a similar incentive effect on producers.)



Sources: UN COMTRADE; WITS; Authorities' data; and Fund staff calculations.

F. Concluding Remarks

19. While Bolivia is in a good starting position relative to other EMDEs, the trend declines in export diversification since 2010 suggest the need for reform. Bolivia is an interesting case since it exports a large number of different types of products, both existing and new, but the decline in overall diversification is driven by the small scale of export volumes of existing manufactured goods. International experience finds that developing and exporting new products is the hard part, whereas Bolivia has found some success in that regard. However, low export 'quality' compared to the region is a concern given its implications for growth and since it takes many years to improve.

20. Reforms are needed to help small and medium sized companies flourish and expand production. These would aim to counter the de-diversification trend while improving 'quality' by supporting established businesses in their efforts to meet international 'quality' standards, to achieve greater economies of scale ('intensive margin'), and to adopt new technologies. Taking steps to build the four pillars outlined above would help put Bolivia on a path toward greater export diversification and higher 'quality' exports. Micro reforms to improve the business climate would complement these pillars well toward the same objectives (see SIP "The Business Climate in Bolivia").

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THE BUSINESS CLIMATE IN BOLIVIA[1]

A. Introduction

1. Bolivia has experienced economic stability since the mid-2000s and one of the highest rates of growth in the region. An important element of this success was the sharp increase in hydrocarbon -related revenues and public investment driven by the commodity "super cycle". At the same time, Bolivia's dependence on the extractive sectors has increased significantly while private investment—both domestic and foreign—has been relatively weak. With commodity prices expected to remain moderate, new sources of productivity and growth are needed outside of the extractive sectors in order to sustain and broaden growth and the recent impressive gains in socio-economic indicators.

2. Low private investment rates are related in part to structural issues impeding private sector activity. This includes labor market regulations, the tax system, government interventions, and the regulatory framework governing commerce and trade. International business surveys have flagged these impediments in recent years. Bolivia's performance in the global competitiveness index (World Economic Forum), economic climate index (*Fundação Getulio Vargas*) and the Doing Business report (World Bank) has been deteriorating steadily, with assessments in the latter worsening for almost every indicator. While these studies have their limitations, including an element of subjectivity, they contain valuable information that should be mined for constructive policy ideas. Given the macro-critical importance of private investment for productivity, growth and formal employment (Staff Report), it makes sense to exploit their qualitative content to better inform our macro-structural policy advice.

3. The purpose of this study is to strengthen our understanding of the information contained in the Doing Business (DB) report about impediments to private investment. The study aims to: (i) identify the most important impediments to business activity and private investment; and (ii) develop key reform ideas and remedies. The latter focus on priorities and possible low hanging fruits, i.e., reforms that could be easiest to implement. While these could also improve Bolivia's performance the DB report, "rank-seeking" is not the purpose, though it could be an indirect benefit.

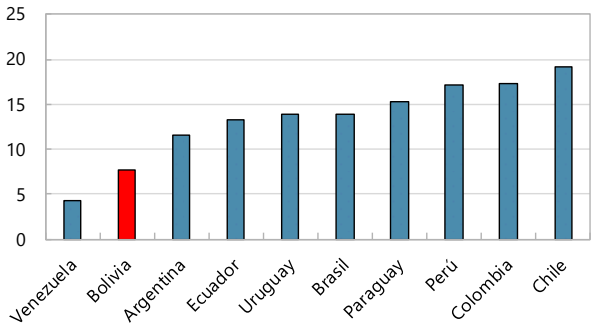
B. Context

4. The large increase in investment since 2004 is due mostly to growth in public investment. As a percentage of GDP, total investment rose from about 14 percent in the early 2000s to 21 percent in 2017, similar to levels experienced during the privatization era in the 1990s. Public investment rose from about 6 percent of GDP in the early 2000s to a peak of 14 percent in 2017. It is among the highest in the region, averaging 11 percent of GDP over the last decade, while private investment has remained weak since 2004, averaging about 8 percent of GDP annually—

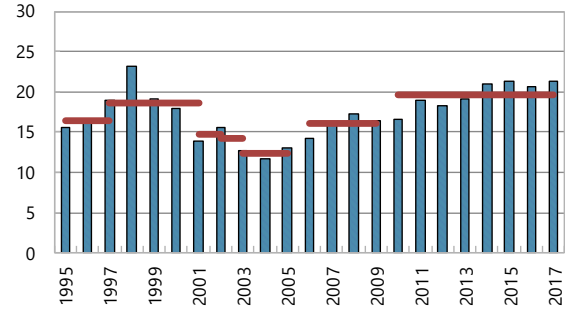
[1] Prepared by Sergio Cárdenas Rossel

among the lowest in South America. Foreign direct investment (FDI) is also low compared with some neighboring countries and consists mainly of reinvested profits—about 70 percent on average—in the hydrocarbon and mining sectors that are allocated mostly to maintaining existing operations.

South America: Private Investment, 2017
(as percent of GDP)

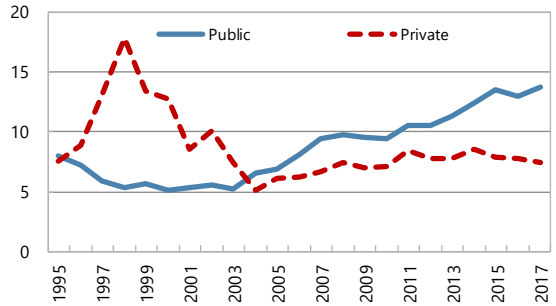


Bolivia: Total Investment
(In percent of GDP)



Source: National Institute of Statistics

Bolivia: Public and Private Investment
(In percent of GDP)

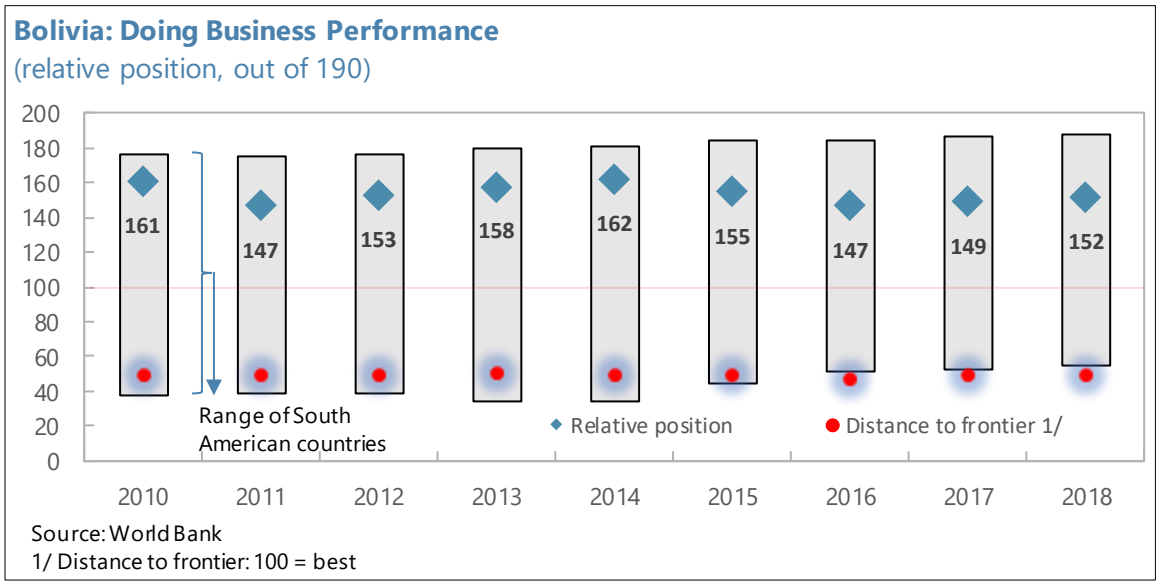


Source: National Institute of Statistics

5. Bolivia's performance in the DB Report started to deteriorate in 2007. Bolivia has appeared in the bottom quartile of the DB report since 2009 and is among the worst performers in Latin America (LA). It is important to note that the report measures performance relative to other countries so the position in each year also depends on changes in other countries in the sample. Performance in the index is measured by the "distance to frontier" (DTF) which shows the distance of each country to the best performer (the frontier) in each category (Appendix II).[2] Bolivia´s DTF has been stable at about the mid-way point over the past ten years.

6. Caution is needed when comparing the change over time in performance. The DB methodology is updated every year to incorporate new information on reforms and corrections (see Appendix II). However, indicators can undergo important changes in methodology and coverage, and they can be removed and new ones added. While the objective is to enhance and update the survey to match evolving global business conditions and challenges, it can render the time series incomparable. In addition, methodology changes can sometimes affect countries differently, including penalizing countries that are not able to adapt quickly to new standards because of weaker administrative capacities.

[2] The DTF is a scale from 0 to 100, where 0 is the lowest performance and 100 the frontier.



C. Recent Reforms to Improve the Business Environment

7. The authorities enacted the Law Against Bureaucracy for the Creation and Operation of Economic Entities in 2016. The purpose of this law was to improve efficiency in the provision of public goods and services by reducing bureaucracy in public agencies. Two key mechanisms were introduced: (i) the Electronic Gazette of the Registry of Commerce, which became the only valid and official medium for reporting business activity and results; and (ii) a virtual system called *Yuriña* that connected users to a centralized data base to verify the information provided and track procedures with the agencies involved, including the registry of commerce, the tax agency, pension funds, and the Ministry of Labor.

8. The government's plan to reduce bureaucracy and lower corruption is being implemented in two stages. The first stage was launched in June 2018 with the digitalization of public procedures to reduce the steps and costs of services provided under five key ministries, such as the mandatory registry of employers in the Ministry of Labor or verification of copyrights for a proposed company name. Actions like these can now be performed directly online. The second stage was announced in September 2018 and involves the modernization of additional processes under these same five ministries. The authorities created a new public agency (*AGETIC*) to lead these IT reforms to reduce bureaucratic processes. In addition, a new web portal was established that organizes and explains the requirements, costs, and time involved to undertake various procedures.

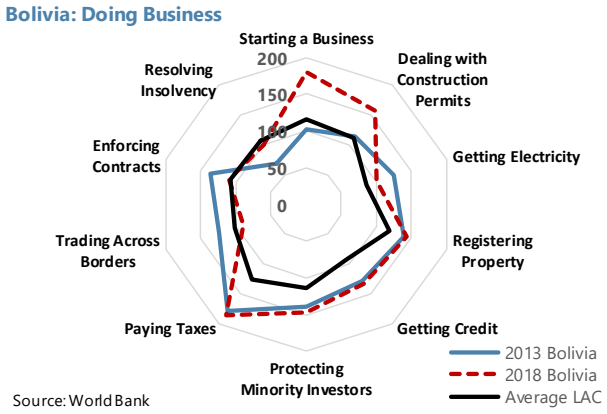
9. The government also moved to modernize systems for exporting and importing. The Bolivian customs agency developed a new web-based system—the Unique System of Customs Modernization (SUMA) in 2013 to increase efficiencies trading across borders. The system features innovations such as the use of digital signature, digitalization of documents, electronic notification, and automation of processes, among others, that permit more efficient processes to execute trade.

10. The Municipality of La Paz launched its own reforms to lower the costs of doing business. It redesigned and modernized its web portal in August 2018 so that 18 administrative procedures can be completed online, up from five. The portal includes updated cadastre data, the ability to renew or request cadastral certificates, access to information relating to the municipality and zoning, construction permits, and enquiries about taxes owed. It also provides a platform for payments to be made online.

D. The World Bank Report: Some Bright Spots, Many Impediments

The Ten DB Indicators

11. Positive news in a few areas was but deterioration in others (Table 1). There has been a relative improvement in two indicators: (i) the implementation of the automated customs data management system as noted above has made 'trading across borders' easier in terms of the cost and time to export and import; and (ii) a new code of civil procedures that introduced pre-trial conferences, verbal processes and on-line notifications has improved the conditions for 'enforcing contracts'. Bolivia already performs relatively well compared to regional peers in the categories 'getting electricity' and 'resolving insolvency'. The remaining six indicators have deteriorated, with the worst being 'paying taxes', 'starting a business', and 'dealing with construction permits'.



12. (1) Paying Taxes. According to the 2017 World Bank Enterprise Surveys, tax administration and high tax rates are the biggest problems for business in Bolivia after issues related to the size and activities of the informal sector. In the DB survey, the DTF on 'paying taxes' is the lowest for Bolivia. The number of tax payments and mandatory contributions during a year is reported to be 42 as compared to an average of 28 for the LA region, after Venezuela. Some payments, namely the transactions tax, employers' social security contributions, and VAT, are made monthly and in person (or physically), whereas they can be filed and paid electronically in some neighboring countries. The time to prepare, file, and make payments is reported to be more than three times the regional average at a considerable 1,025 hours, only 55 hours less than reported in 2006. The measure of total taxes and contributions paid as a share of commercial profits is 84 percent in the second year of operation (a sub-indicator), double the regional average. Labor contributions have made up 19 percent of this total since the Pensions Law was enacted in 2010 and the social security rates for employers were raised. In the post-filing part of the survey, Bolivia performs better than some of its neighbors.

Table 1. Bolivia: Summary of Findings from 2018 Doing Business

Indicators (ranking over 190 countries, DTF score 0-100)	Explaining factors
Paying Taxes (186, 21.62)	▫ Large number of taxes and contributions per year
	▫ A great amount of time to prepare, file and pay taxes
	▫ High total tax and contribution rate (as share of profits)
Starting a Business (179, 62.95)	▫ Large number of procedures, time and cost
Dealing with Construction Permits (158, 55.56)	▫ A great amount of time to complete the procedures
	▫ Low building quality control
Protecting Minority Investors (146, 40.00)	▫ No disclosure obligation and ownership/control
Registering Property (144, 49.89)	▫ A great amount of time to complete a procedure
Getting Credit (133, 35.00)	▫ Low protection of rights of borrowers and lenders
	▫ Low credit and bureau coverage
Enforcing Contracts (109, 54.65)	▫ High cost and low quality of judicial processes
Getting Electricity (101, 68.18)	▫ A lot of procedures and costly
Resolving Insolvency (99, 42.32)	▫ Low strength of insolvency framework, mainly the creditor
Trading across Borders (89, 71.59)	▫ Lot of hours to export and import

13. (2) Starting a Business. The government has made some important improvements since 2016 (Section C) that have reduced the time needed to register a private company on-line. However, the number of procedures (14) is still high compared to the regional average (8) and they involve 12 different public and private institutions. The time required takes up to 45 calendar days, also well above the regional average. Some respondents reported that certain procedures can be done simultaneously which would reduce the time by half to about 20 days.[3] The activities occupying the most time are obtaining the municipal license and registration card (12 days) and registering for national health insurance (15 days). These are also activities that could give rise to "facilitation payments" to accelerate or facilitate procedures. Finally, because of the array of procedures, implementation involves legal and accounting expertise which adds further to business costs.

14. (3) Dealing with Construction Permits. Compared to countries in the region, Bolivia performs well in "cost and procedures", two of the four elements in this indicator. The main weakness in Bolivia is the amount of time needed to complete the procedures, which can take up to one year, of which half is dealing with the municipality. This activity is understood to be another area where lengthy procedures and interactions with officials' present opportunities for "facilitation payments". Additionally, the process has become lengthier since 2017 due to the introduction of a requirement to pay for the land registry certificate at the Judiciary Council. With respect to the building quality control score, it is negatively affected by: (i) the absence of any legal requirement to obtain insurance to cover structural flaws or building problems after sale or completion, and (ii) the lack of minimum standards or certification requirements for architectural plans/drawings or building/construction supervisors.

15. (4) Protecting Minority Investors. Bolivia's DTF score on protecting minority investors is the worst in South America after Venezuela. There is no external body reviewing transactions in advance, no disclosure obligation about conflicts of interest to boards of directors, and no reporting

[3] A good example of a "low hanging fruit" that could be easy to address and clarify.

of transactions in annual reports or to the public and shareholders. An investor cannot be disqualified, fined, or imprisoned, and a court cannot void a transaction after a successful claim by shareholders unless it is proven to be a case of fraud or bad faith. The DB survey finds the lack of regulation about company ownership or control problematic. For example, a CEO can also hold the position of Chairman of the Board of Directors, and there is no obligation for independent board members or the audit committee to participate in the board of directors. In addition, the corporation is not obliged to declare dividends within any given time period, and potential acquirers can submit an offer to all shareholders upon acquiring 50 percent of the corporation. A subsidiary can also acquire shares issued by its parent company. Finally, the DB assessment finds significant weaknesses in corporative transparency with respect to the disclosure of information of ownership, board membership, compensation, and proceedings related to annual general meetings.

16. (5) Registering Property. On a positive note, the number of procedures and the cost of registering property are found to be lower than the regional average., but the time needed to complete the process is lengthy. The first steps of inspection and obtaining the cadastral plan take up to 75 calendar days with the municipality and the last step of obtaining the legal registration/title with the Real Estate Office taking another 25 days. The amount of time involved is likely to involve repeated interactions and poses further opportunities for facilitation payments. The quality of land administration is found to be very low (7 out of 30) due to a lack of electronic or digital databases or identification and transparent online access or services. Finally, the geographical coverage is not complete.

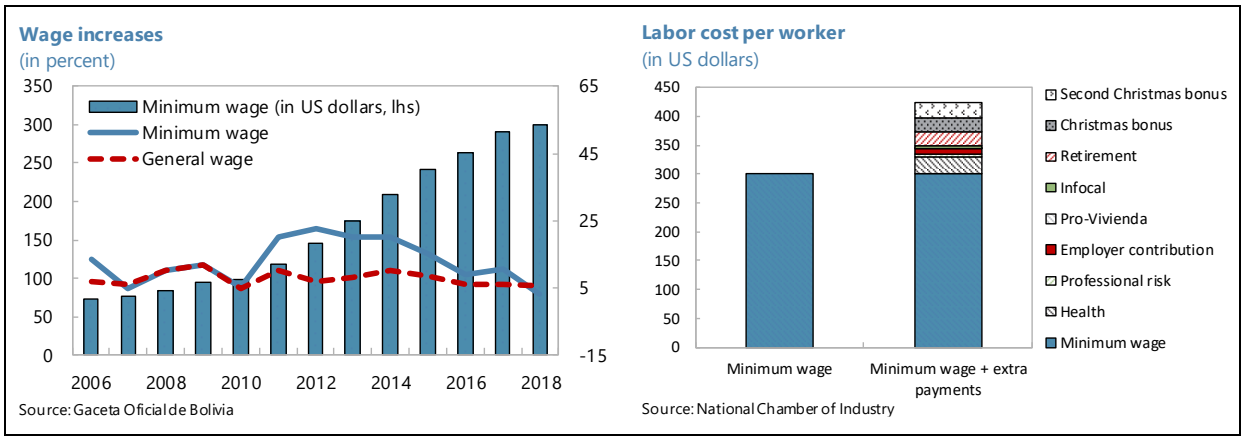
17. The following remaining indicators point to areas for improvement in due course.[4]

- **(6) Getting credit**. The degree to which collateral and bankruptcy laws protect borrowers and lenders is found to be very low, which inhibits lending and financial intermediation. Coverage of the credit registry and credit bureau in Bolivia is found to be close to the regional average, but low in a global perspective.

- **(7) Resolving Insolvency.** The key problem is found to be weaknesses in the broader judiciary, including major delays extending into years to pursue legal processes, and failure to resolve legal disputes. Inefficiency could be related to technological or capacity factors, but there is also concern that disfunction and delays could give rise to opportunities for exercise of influence and facilitation incentives.

- **(8) Trading across borders.** As noted above, there have been important efficiency gains related to automation. However, the report finds that the time required to clear goods through customs is still lengthy and costly, especially for imports, and also gives rise to opportunities for facilitation payments.

[4] 'Enforcing contracts' and 'getting electricity' are not discussed in detail, as explained in ¶ 7.



The Labor Market

18. Labor market weaknesses and wage setting practices are cited repeatedly by the private sector as major impediments to doing business. The labor market indicator is not part of the overall DB score but is presented as an annex in the Report. The annual wage increase is negotiated every year in private between the government and the main labor union, and is applied economy-wide, with some exemptions only for public sector entities. Wages have increased by 8 percent per year on average over the past decade, not including other mandatory wage costs including: (i) the "*doble aguinaldo*", a second end-year wage bonus instituted in 2013 equivalent to one month's salary and compulsory for all companies when economic growth in the four quarters to June exceeds 4.5 percent, raising nominal wages by an additional 5-8 percent on top of the annual increase; (ii) other social benefits, including a pre- and post- natal subsidy that amounts to 18 months' wages (Table 2); and (iii) mandatory extra charges for night work, overtime, and weekend shifts. While wage income growth contributed significantly to reducing poverty and income inequality between 2004-2014 (IMF 2014), real wage growth has surpassed productivity growth every year since 2013 (Staff Report).

19. The legislation governing labor market is the 1942 General Labor Law, although additional regulations have added layers of protection and rigidity. Since 2006, many restrictions have been added, including prohibiting downsizing or dismissals related to redundancy or the profitability of the enterprise. (Dismissals are allowed only for criminal reasons.) Other regulations include restrictions such as prohibiting women from working more than five days a week or at night (unless a nurse or maid) and forbidding the dismissal of parents during pregnancy and until the child reaches his/her first birthday. In addition, a dismissed worker can seek re-employment through a Ministerial resolution. In this context, companies are wary of hiring new workers and prefer short term or informal arrangements. Contractual workers enable firms to circumvent regulations that restrict their ability to adapt to changing market conditions. This has led, for example, to a boom of "one-person" companies which are more likely to operate at the margin of formality in the construction and commercial sectors. One-person companies in June 2018 represented 80 percent of all registered firms.

Table 2. Non-Wage Worker Benefits

Benefit	% of Wage	Description
Health insurance	10%	Payment to cover any health problem (illness or accident) of the worker and his/her beneficiaries
Professional risks	1.7%	To cover the common, professional and occupational risks
Employer contribution	3%	To Pensions Fund
Pro-Vivienda	2%	Other contribution to Pension Fund for housing projects
Infocal	1%	Voluntary contribution to workers training in some areas
Retirement	8.3%	Monthly contribution for retirements of workers
Christmas bonus	8.3-16.7%	A mandatory extra monthly salary, when the annual economic growth surpasses the 4.5 percent
Seniority bonus	5-50%	This benefit is paid after 2 years' work and goes from 5 percent from 2-4 years of work to 50 percent for over 25 years of work

Source: National Chamber of Industry

E. Findings and Policy Suggestions

20. The above analysis points to several areas where changes or reforms could improve the business climate. The recent government-led reforms (Section C) should improve the ease of doing business, including by reducing the amount of paperwork and procedures with public agencies. The introduction of the Electronic Gazette and the verification of copyright have already had an impact on the 'starting a business' indicator. Following through with this system, improvements are also expected in other DB indicators such as 'paying taxes', 'registering property' and 'trading across borders'. Nonetheless, this study has identified some areas where focused efforts could improve the business climate, attract private investment, and promote export diversification.

Lower Hanging Fruit

21. Recommendations are presented below in two stages: reforms that aim to address impediments quickly and hopefully relatively easily, such as with administrative or executive actions; and reforms that would involve longer term preparation and broader consultation:

a. **Reducing the number of tax payments by moving to digital and online systems.** The tax system should move to online filing and payment of taxes and other payments, including VAT payments, social security contributions by employers, and the transaction tax. This would lead to important efficiency gains and could permit a reduction in some instances in the frequency of payments, e.g., from monthly to quarterly. Regulations could also be changed to allow VAT refunds for items other than just international trade, including tourism services, goods supplied to public companies, or for capital goods purchases by entrepreneurs, as exist in other countries. Also, the tax agency should ensure that taxpayers have the information and support they need to fulfill their obligations on time and claim specific benefits available under current regulations.

b. **Making it easier to start a business.** Implementation of the plan to reduce the bureaucracy related to starting a business is a welcome initiative, especially the creation of the Electronic Gazette. The next step could include technological improvements to reduce the time and costs of: (i) obtaining a business license and registration from the municipality; (ii) registering the company deed; (iii) registering employers in the public national health insurance and (iv) registering employees with the pension system. Investments in technology could also greatly speed up and simplify other routine procedures, such as obtaining construction permits, zoning permits, the cadastral plan from the municipality, cadaster certificates, and land registry certificates and the public deed from the Real State Office. This could also facilitate full implementation of the *Yuriña* virtual system. Registration for national health insurance could be improved by strengthening the training and availability of dedicated staff. All of these changes would raise efficiency and contribute to higher private investment and formal employment. It could also lower uncertainty by removing opportunities for facilitation payments.

c. **Broadening financial protection and reforming insolvency processes**. Regulations on bankruptcy and collateral could be modified to provide better protection for borrowers and lenders. The ability and processes for resolving insolvencies is assessed to be weak, principally as regards creditor participation. The only realistic option to deal with insolvency is a costly and very long bankruptcy procedure. The current revision to the Commerce Code could help in the resolution of insolvencies, reformulating the current insolvency regimes and clearly differentiating the preventive procedures and the effective bankruptcy procedures. The new Law on the Creation of Social Enterprises has also complicated and clouded the issues related to security of private investment and insolvency processes.

d. **Supervising trade procedures**. While export compliance and the time required has improved in recent years, there remain bureaucratic obstacles to importing. Greater oversight, particularly on the work of private customs clearance agents, could help imports to be processed in fewer days. This should also include efforts to establish methods to discourage incentives for facilitation payments.

e. **Improving building quality work**. Existing building codes and regulations should be modernized to meet international standards. They should set rules on mandated inspections, mandatory insurance to cover structural flaws, and qualification requirements for experts involved in verifying compliance with architecture standards and construction norms. These regulations are extremely important now given the boom in construction during the last decade. Coordination and cooperation with regional partners on standards, training and regulation could facilitate the development and implementation of best practices.

f. **Enhancing corporate governance.** The rights of investors in Bolivia is assessed to be among the weakest in the region and among emerging markets. In particular, the biggest gaps relate to disclosure, liability, extent of ownership and control and corporate transparency. Reforms could draw on positive experiences in countries like Colombia, which is placed in the top quartile in the DB report. It would also be good to establish a common accounting standard for all companies in Bolivia, preferably based on international accounting standards.

22. Engaging with the World Bank and the private sector could help strengthen understanding of the issues and possible remedies. Given the high profile among investors of the DB Report, it would be helpful to engage with private sector respondents to better understand the issues and help identify remedies. It could also be useful to raise awareness about some features of the report, including issues related to time consistency and comparability. Consideration should also be given to resolving discrepancies identified (see Appendix I). Finally, it is worth noting that some methodology updates to indicators may negatively affect the ranking of countries with lower administrative capacity given their ability to adapt to new criteria quickly.

Longer-Term Reforms

23. Updating the framework governing labor market conditions. The current general Labor Law does not provide a framework that safeguards modern labor conditions or minimum international norms for workers' rights and benefits. Moreover, the wage setting process does not provide a transparent or rational approach that incorporates the relevant factors to determine wage decisions, such as inflation, productivity, market comparators, or the views of employers (see Staff Report). While existing regulations are intended to protect workers, they serve as excess constraints on businesses that discourage employment and drive business activity into the informal market where workers operate in an unregulated environment with no rights or benefits. Bolivia would benefit from a new, inclusive labor code that sets minimum standards for rights and benefits and the minimum wage, while removing the government from sector and firm-specific employment and wage decisions. This should involve broad consultation with stakeholders and possibly a social partnership between the key national players: business, labor and government.

24. Revising the tax code. The tax code dates from 2003, the period before Bolivia's new Constitution and development of the hydrocarbon sector. A new tax code should aim to broaden the formal tax base and reduce the tax burden on formal wage earners and the narrow formal productive sectors. It could also make the tax system more progressive by implementing an income tax (instead of the current RC-VAT) and could help promote foreign investment in key sectors like hydrocarbons, mining, agro-processing industry and IT.

25. Reforming the judiciary. There is widespread agreement, including among the authorities, on the need for reform of the justice system to strengthen its contribution to enforcing the rule of law and governance in the service of the people. In addition, weaknesses in the judicial system directly affect several indicators in the DB assessment, including enforcing contracts and resolving insolvencies. The decision to transfer the Real Estate Office to the Ministry of Justice is expected to improve outcomes by strengthening the skills of related personnel and IT systems, and by creating a national registry.

F. Authorities Views

26. The authorities welcomed the opportunity to examine the issues underlying the Doing Business report. In general, they find that some DB conclusions are drawn based on overly subjective answers. They believe the survey is tailored more for limited liability-type companies

which is not representative of most of Bolivia's private sector. They have concerns about the location of businesses surveyed: they believe that Santa Cruz, which has the largest concentration and diversity of private business and industries, is not sufficiently consulted as compared to La Paz. Finally, they raised questions about the survey samples, indicating that the number of respondents for some indicators are too limited. They recommended that the samples be expanded and changed over time to gather a more balanced and informed view, and that more public agencies be included in the survey given the role of the state in some sectors. The authorities nonetheless welcomed the study and indicated plans to take forward the analysis to promote private investment in Bolivia, including by launching an official website—already under development.

Appendix I. Regulations and Practices Vs. Doing Business Report

Indicator	Discrepancy and Recommendation
Paying Taxes	Social security contributions are included as a tax while other similar payments are not, including monthly payments to the national health insurance and fees paid to the Ministry of Labor to be a registered employer. Suggest making consistent and include only those considered tax payments.
Starting a Business	Some procedures can be done simultaneously, which would reduce by half the total time required, from 45 to 22 days.
Registering Property	There are observations in the quality indicators that do not appear to be noted in the report, e.g., some electronic databases and the modernization of some procedures. These could be taken into consideration in the next DB report. There are separate mechanisms for filing complaints (*Juzgados Disciplinarios*); if considered, Bolivia might receive a different score in the transparency index. There are annual statistics which do not appear to be recognized and might improve the information index.
Getting Credit	By law, the credit bureaus or registries can offer credit scores. This fact could raise Bolivia's assessment in the 'depth of credit information' index. Some questions about legal rights are very general and would benefit from specific legal evaluation to explain the rating received. Some answers classified as "negative" would not be considered negative in the Bolivia legal context. The most important example is business liquidation. When a business is liquidated, the relevant law in Bolivia stipulates that taxes and employee claims should be paid *before* secured creditors.
Getting Electricity	The case study (obtaining a 140-kVA connection) is not that relevant for Bolivia because very few projects use that much power capacity. A 30-kVA or 50-kvA connection would be more representative.

Appendix II. Doing Business Methodology

The Doing Business report comprises indicators that measure the legal and regulatory environment for local business activity in 190 countries. The annual assessment provides quantitative results on ten indicators plus data on labor markets, although, there is no quantitative ranking for the latter.

Data Sample for the World Bank Doing Business Report

The *Doing Business* indicators are based on existing laws and/or actual practices as reported by respondents in direct surveys undertaken for most indicators. For 'protecting minority investors' and 'getting credit-legal rights', only national laws are reviewed; for 'getting credit-credit information' and 'trading across borders', only practices based on surveys are compiled. Data are collected in a standardized way with questionnaires to relevant participants. The questionnaires use a simple business case to ensure comparability across economies and over time—with assumptions about the legal form of the business, its size, location, and the nature of its operations.

Questionnaires are administered to local experts, including lawyers, business consultants, accountants, freight forwarders, government officials and other professionals routinely administering or advising on legal and regulatory requirements. These experts typically have several rounds of interaction with the DB team, involving conference calls and written correspondences. For example, 68 respondents were considered in the last survey conducted for Bolivia in 2017 (Appendix III). The data from questionnaires are subjected to numerous rounds of verification, leading to revisions or expansions of the information collected. Respondents are asked to complete the survey for only one indicator. For most indicators, the number of survey respondents is low. In some cases, the "score" is based on the responses from only two contributors for many consecutive years, which implies potential risks of biased assessments. The number of respondents is published on the World Bank website and listed below.

Scores and Rank: Distance to Frontier (DTF)

The DB report introduced a distance to frontier (DTF) score for each indicator in 2005 that measures the deviation of each country from the best performer observed—the "frontier". DTF score ranges from 0 to 100, with 0 representing the worst performer and 100 the best (frontier). Calculating the DTF score involves two steps.

1. DTF is calculated for each indicator with normalization using the formula below:

   DTF = (Worst Performance – Raw number) / (Worst Performance – Best Performance)

2. The DTF scores for each indicator are consolidated by simple averaging into one DTF score for all ten topics. Thus, the final rank in the DB index ranges from 1 to 190, is decided by the average of the DTF scores in all ten categories into one DTF score that is the basis for score in the final country index, rounded to two decimals.

Methodology Updates in 2016 and 2017

Measures covered by the survey are updated every year. Only the preceding year's ranking is adjusted to reflect changes recorded in the current year t=0. This means that assessments over time between different surveys are not strictly comparable, i.e., scores in 2015 are based on different methodologies or include new or different information, hence are not consistent with scores reported in 2016. This is a significant factor in assessing continuity of the scores/rankings over time.

The Doing Business 2016 Report (DB 2016) expanded the content of five indicator sets (dealing with construction permits, getting electricity, registering property, enforcing contracts and labor market regulation); substantially revised the methodology for one indicator set (trading across borders); and implemented small updates to the methodology for another (protecting minority investors).

i. **Dealing with construction permits**. DB 2016 introduced a new measure of building quality control and its implementation which led to a large drop in Bolivia´s score in 2018.
ii. **Enforcing contracts**. DB 2016 included an index of the quality and efficiency of judicial processes while the indicator on the number of procedures to enforce a contract was dropped. The led to an improvement in score for Bolivia in DB 2018.
iii. **Trading across borders**. DB 2016 introduced a new indicator to measure the time and cost of compliance with rules and fees for exporting and importing. Improvements in custom administration and systems led to a much better score for Bolivia in DB 2018.

Doing Business 2017 had two major innovations. First, it expanded the 'paying taxes' indicator set to cover post-filing processes. Second, it expanded three indicators to include a gender dimension: 'starting a business was expanded to measure the process when all shareholders are women; 'registering property' added the issue of gender equality in property ownership rights; 'enforcing contracts' was expanded to measure equality in evidential weight for men and women.

Appendix III. Respondents by Indicator

Topics	Contributors
Starting a Business	13
Dealing with Construction Permits	6
Getting Electricity	6
Registering Property	5
Getting Credit	12
Protecting Minority Investors	3
Paying Taxes	3
Trading Across Borders	4
Enforcing Contracts	5
Resolving Insolvency	7
Labor Market Regulation	4