
SUMMARY OF FINANCIAL MARKETS IN BOLIVIA: SECONDARY SOURCE SURVEY

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NOTE

This document was prepared by Arthur Young and summarizes existing literature describing the country. Secondary sources were obtained from the International Monetary Fund, the World Bank, the Inter-American Development Bank, the African Development Bank, the Asian Development Bank, the United Nations, and other relevant commercial sources.

BOLIVIA

SUMMARY OF FINANCIAL MARKETS SURVEY

A. ENVIRONMENT

1. Unstable political history

Bolivia has had a turbulent political history, and has experienced frequent changes in leadership since independence. Sr. Victor Paz Estenssoro and his Movimiento Nacionalista Revolucionaria (MNR) staged a popular uprising in 1952, and held power until 1964 when he was overthrown by the military. Since the 1964 military coup, Bolivia has been governed by a series of military juntas and several different presidents. In July, 1985, elections were held a year early because the incumbent, Sr. Hernan Siles Suazo, lacked the support of Congress and the people. Sr. Victor Paz Estenssoro was elected president for the fourth time.

In an effort to curb hyperinflation, and to win the support of the IMF, Estenssoro instituted an austere economic program upon taking office. This program was met with widespread opposition and numerous strikes which precipitated military intervention. Bolivia's future political stability will depend on Estenssoro's ability to enforce his severe economic policy measures and turn the economy around without inciting another coup.

2. Unstable economic climate

Bolivia's economy is in critical condition, showing negative or negligible growth every year since 1981. Plaguing Bolivia's economy are:

- huge external debt; GOB has been unable to service its debt since May, 1984
- plummeting world market prices for tin, Bolivia's major legitimate export
- hyperinflation (estimated to be over 20,000% in the 12-month period ending August, 1985) has led to the growth of a black market economy which operates on US dollars; current estimates suggest that three fourths of the economic activity in the country are conducted in the informal sector

- rampant inflation has also hurt investment and production as low real interest rates have made currency speculation more lucrative than productive investment
- major western powers (especially the U.S.) are pressuring GOB to clamp down on the cocaine trade, Bolivia's most profitable export and major source of US dollars (cocaine is estimated to earn US\$1 billion per year)

Recovery has been stifled by instability in the government and the absence of a coherent economic policy. GOB attempts at recovery through austerity measures have been thwarted by worker resistance and uncontrollable inflation.

Sr. Estenssoro's economic program looks capable of turning the economy around. It's success, and Bolivia's future economic stability, will depend on worker willingness to take a cut in their already low standard of living (real wages are currently 80% of 1977 levels.)

3. Stable social system

- a. The Bolivian population is primarily composed of Indians (25% Quechua and 17% Aymara) and mestizos (30%); there is a smaller population (12%) of whites of European descent; the remaining 4% are classified as "other."
- b. The official language is Spanish, although most mestizos are bilingual in Spanish and one Indian language, and some Indians in remote areas speak only their indigenous language.
- c. 90% of the population are Roman Catholic, however the Church holds little economic, social or political power.

4. Substantial international assistance

- FAO
- ILO
- IMF
- UN
- WHO
- Andean Sub-regional Common Market
- Economic Commission for Latin America
- Inter-American Development Bank
- Latin American Integration Association
- OAS
- World Bank

5. International trade agreements
Bolivia participates in a number of regional trade agreements:

- ALADI (formerly ALALC) - Latin American Free Trade Association; Bolivia currently receives 41% of imports from ALADI countries
- URAPABOL - Uruguay-Paraguay- Bolivia Commission
- Argentina has granted Bolivia a free zone in the port of San Nicolas
- Bolivia's north west border town of Cobiya is a free zone to Brazil
- Trade and co-operation agreement with the EEC

B. ECONOMY

1. The last five years have seen a serious deterioration in the Bolivian economy. Inflation soared to 20,000% in the 12-month period ending August, 1985. Real GDP fell 20.1% between 1980 and 1985. Both exports and imports declined during the period; with exports moving from \$942 million to \$556 million, and merchandise imports from \$707 million to \$477 million. A discussion of the components of this tremendous economic deterioration follows.

a. External debt

Bolivia's enormous external debt (currently \$3.2 billion; estimated \$924.9 million for 1985 alone) has created many of the country's economic problems. Bolivia has had problems meeting debt obligations since 1982, and declared an official moratorium on principal and interest payments in May, 1984. In 1985 the cost of servicing Bolivia's debt was greater than its entire income from legitimate exports.

b. Public sector deficit

Central government current expenditures rose from 17.9% of GDP in 1981 to 26.8% in 1984. This growth is due primarily to additions of personnel.

c. Inflation

Inflation has been a serious problem for Bolivia. Inflation began to get out of control in 1983 when the inflation rate rose from 36% at the beginning of the year to 228% by year end. Many factors have fueled Bolivia's runaway inflation. One major contributor has been the fact that GOB has financed a growing proportion of the public sector debt through the Central Bank. The domestically financed portion of the fiscal deficit grew from 3% of GDP in 1981 to 25.8% in 1984.

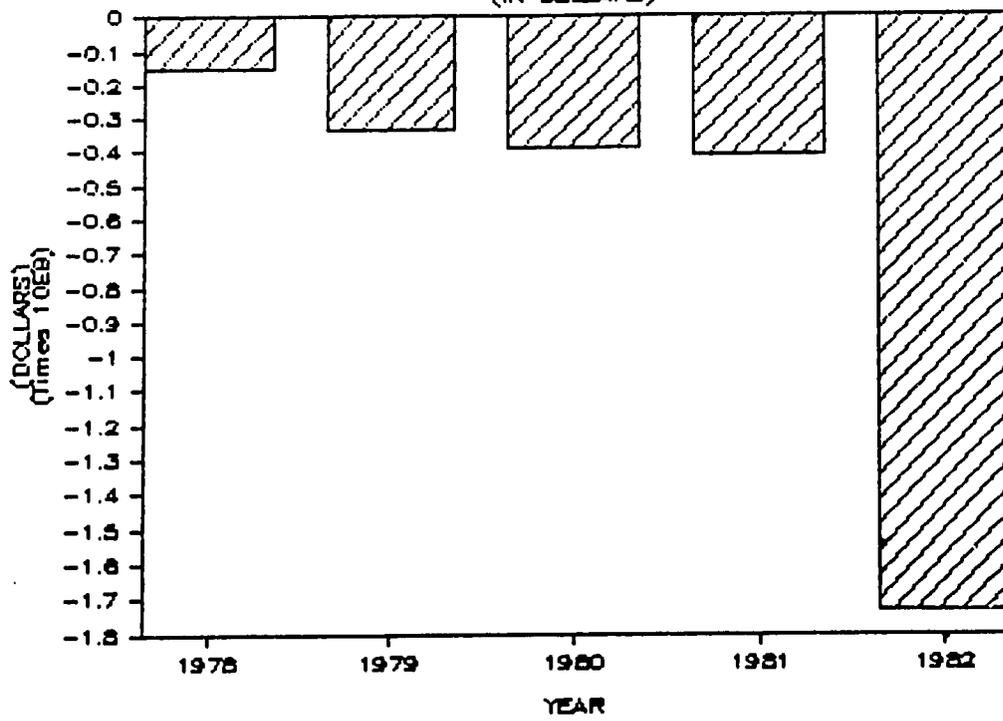
The GOB policy of holding interest rates far below the inflation rate also added inflationary pressures by eroding real deposits in the domestic banking system. Thus, the increased domestic financing of the public debt was being issued from a smaller base. When this policy was changed in March, 1985, the real value of currency and deposits rose.

- d. Mining exports
Bolivia ranks third in the world in tin production. Mining accounts for more than 40% of legitimate export earnings; with tin the largest single earner. The recent decline in the world market price for tin has seriously hurt Bolivia. In 1984 Bolivia experienced a 27% drop in the value of mining exports and a 23% decrease in the volume of mining output.
- e. Agriculture
Bolivia is still recovering from 1983's natural disasters of droughts in the highlands and floods in the lowlands. Damage was so severe that agricultural output fell 23% in 1983, and huge financial outlays were necessary to repair roads, bridges and water systems, and to import food. Although output grew 7.5% in 1984, substantial amounts of food were still imported.

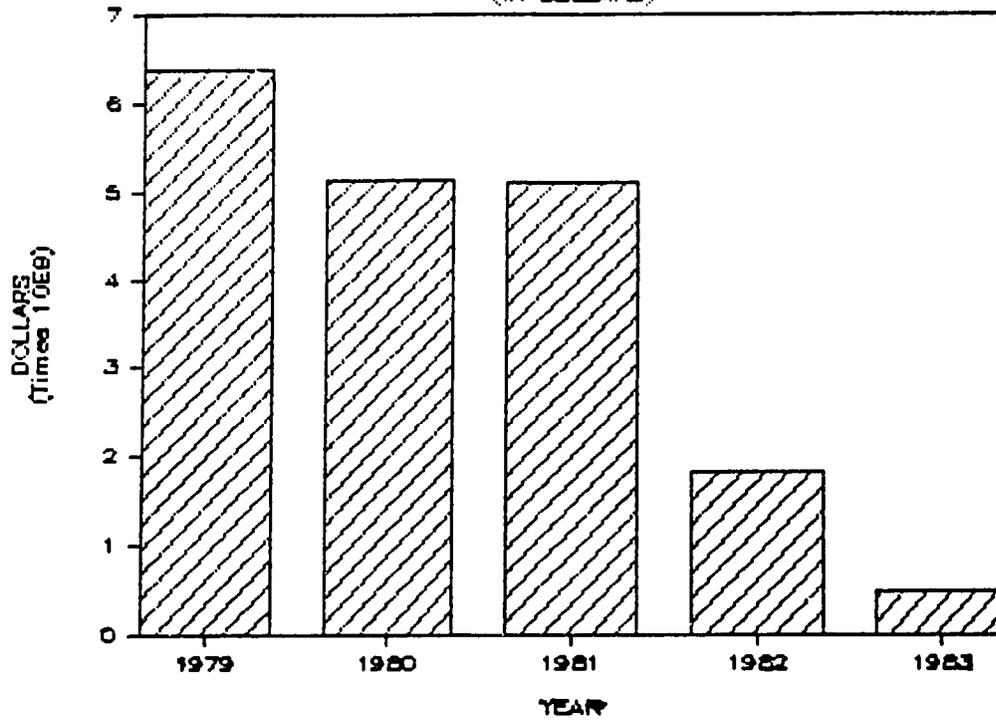
2. Labor force analysis

- a. Population: 6.25 million (mid-1984)
Population growth rate: 2.7%
- b. Literacy: 68% (1981)
- c. In 1983 the labor force was comprised of 31.4% of the population. Approximately 15% of the labor force was unemployed.
- d. Approximately 50% of the labor force is employed in agriculture. However, 62% of agricultural activity is subsistence farming.

OVERALL DEFICIT/SURPLUS (IN DOLLARS)

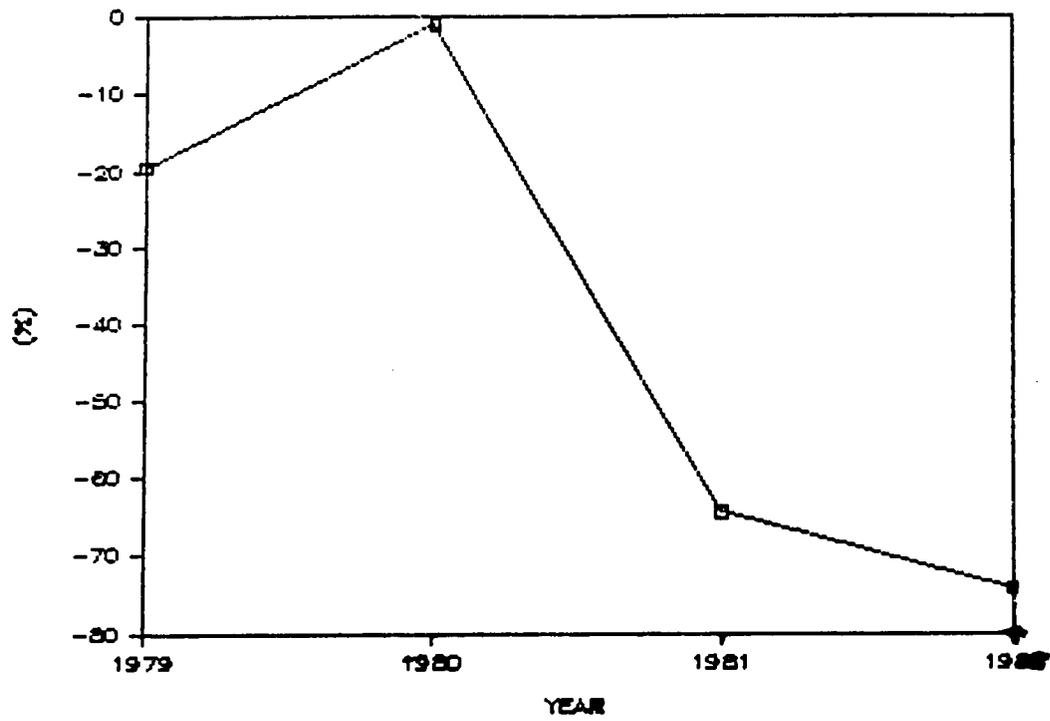


GROSS DOMESTIC PRODUCT (IN DOLLARS)

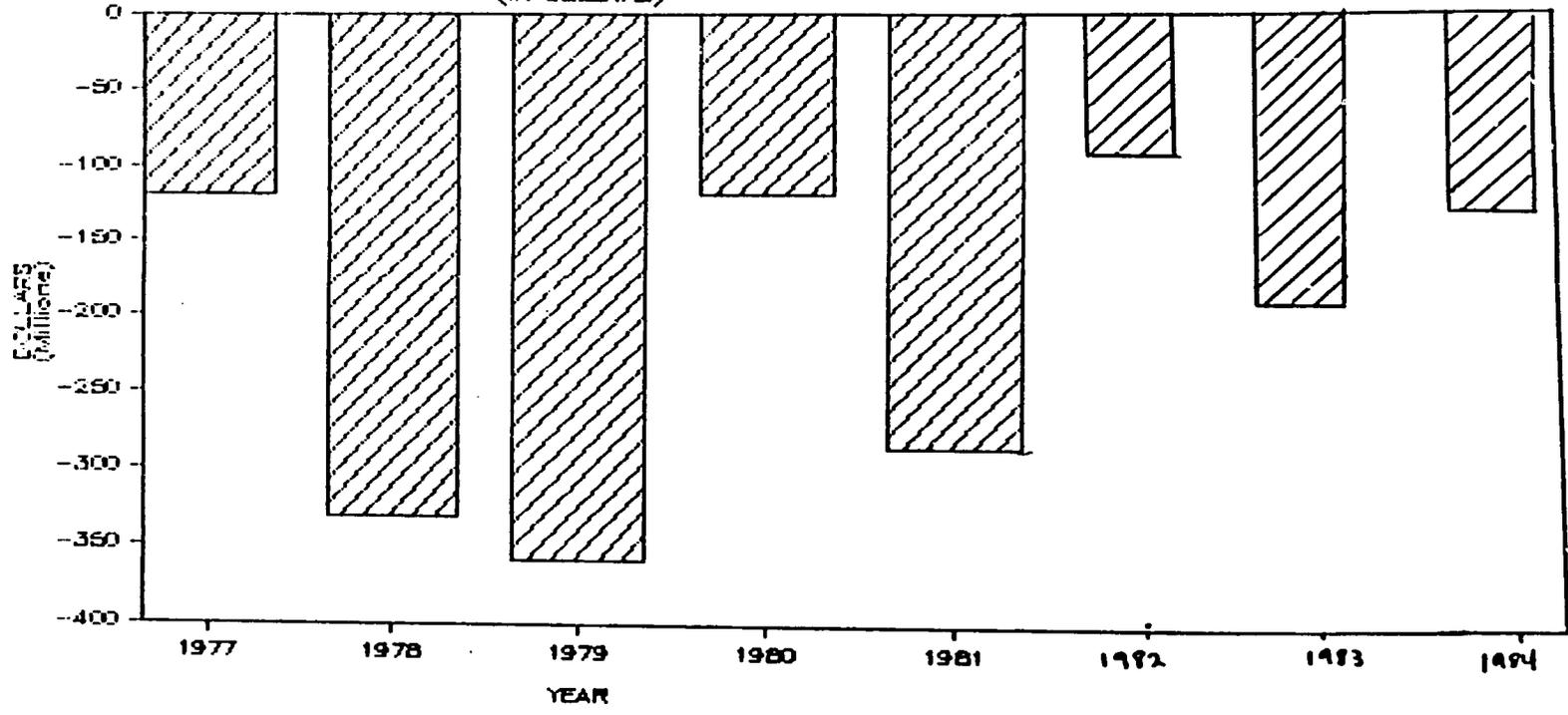


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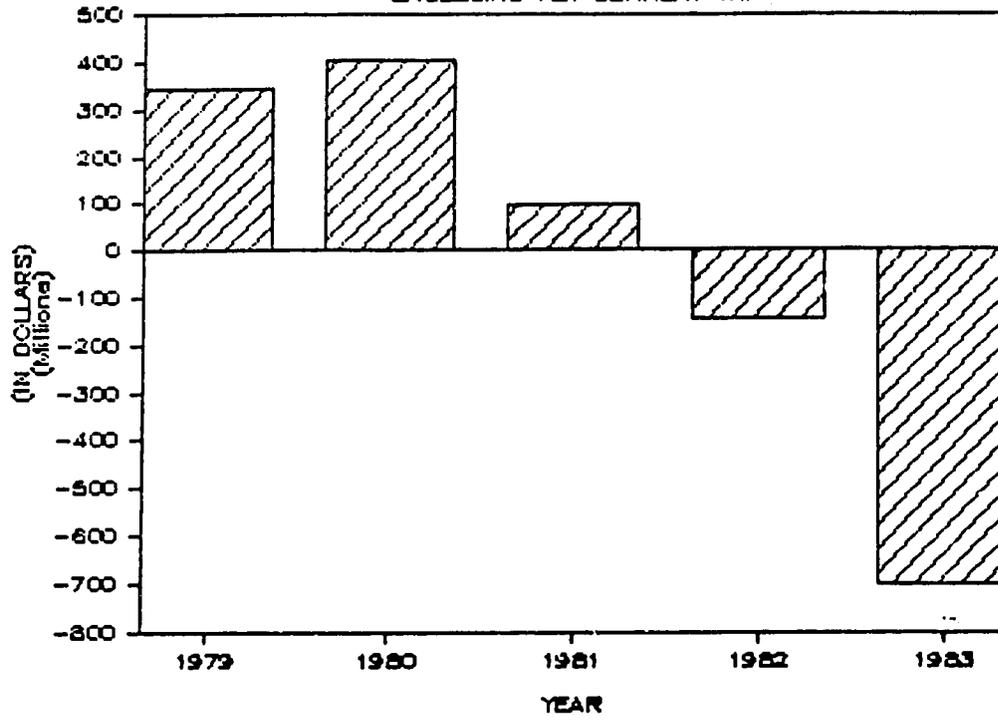
GROWTH RATE OF GROSS DOMESTIC PRODUCT



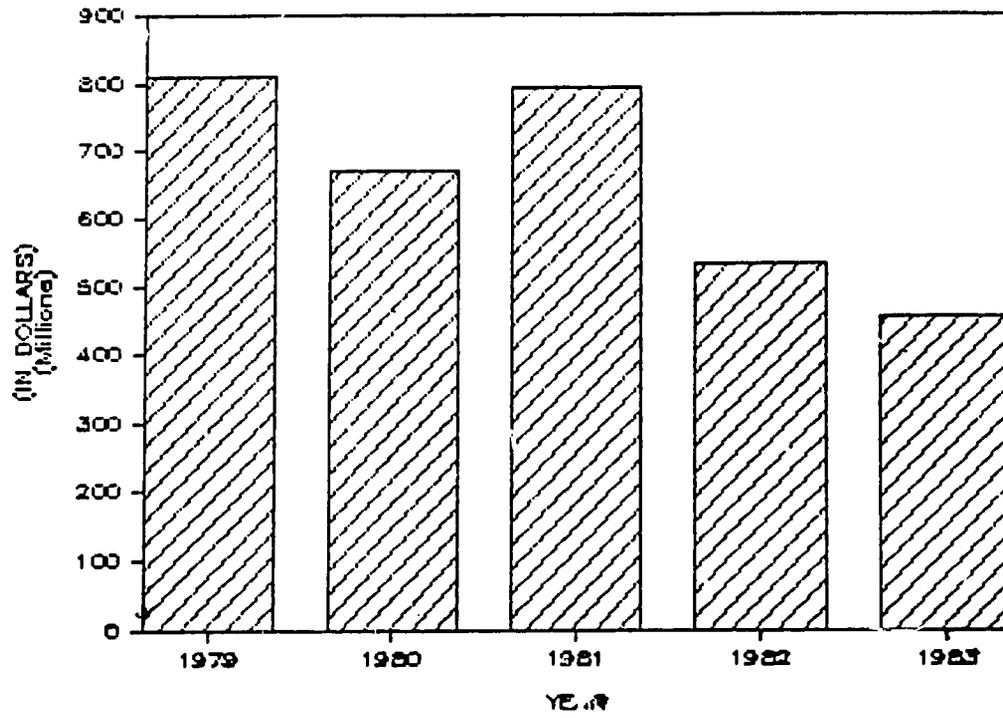
CURRENT ACCOUNT BALANCE (IN DOLLARS)



GROSS NATIONAL SAVINGS - EXCLUDING NET CURRENT TRF

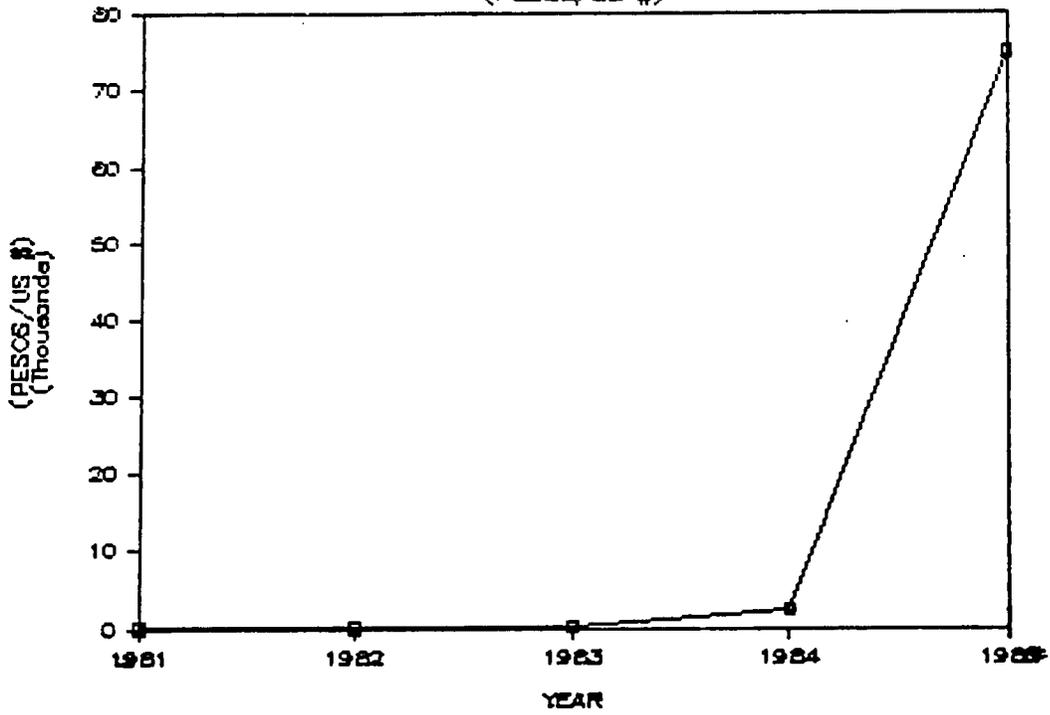


GROSS DOMESTIC INVESTMENT



MARKET EXCHANGE RATE *

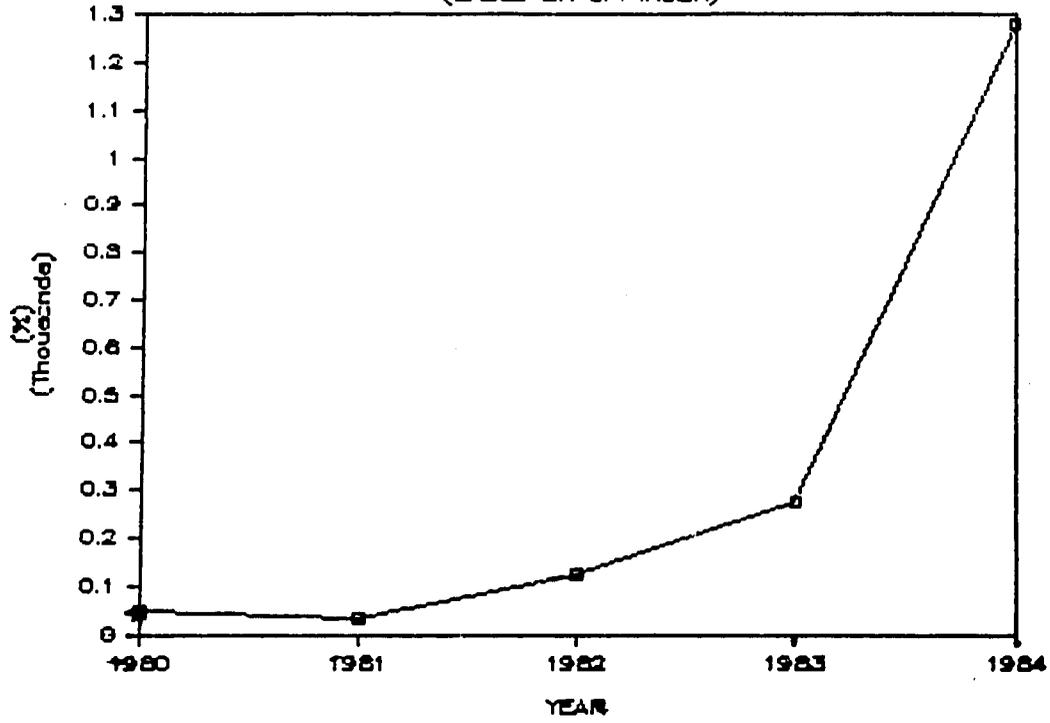
(PESOS/US \$)



*Official Rate

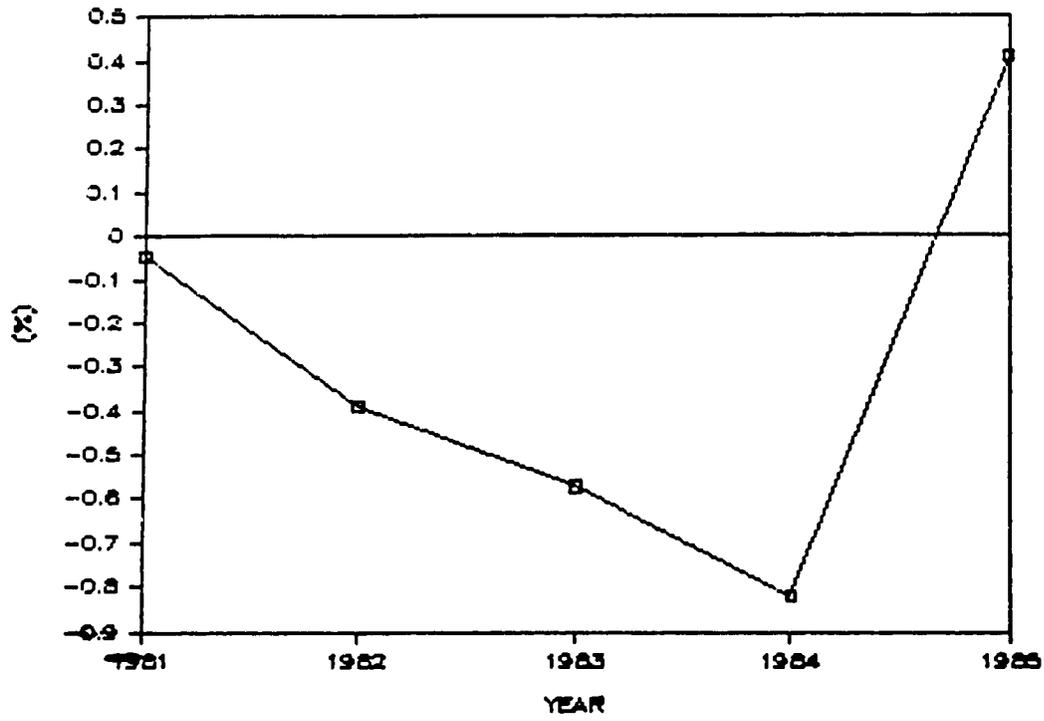
BOLIVIA'S INFLATION RATE *

(BASED ON CPI INDEX)

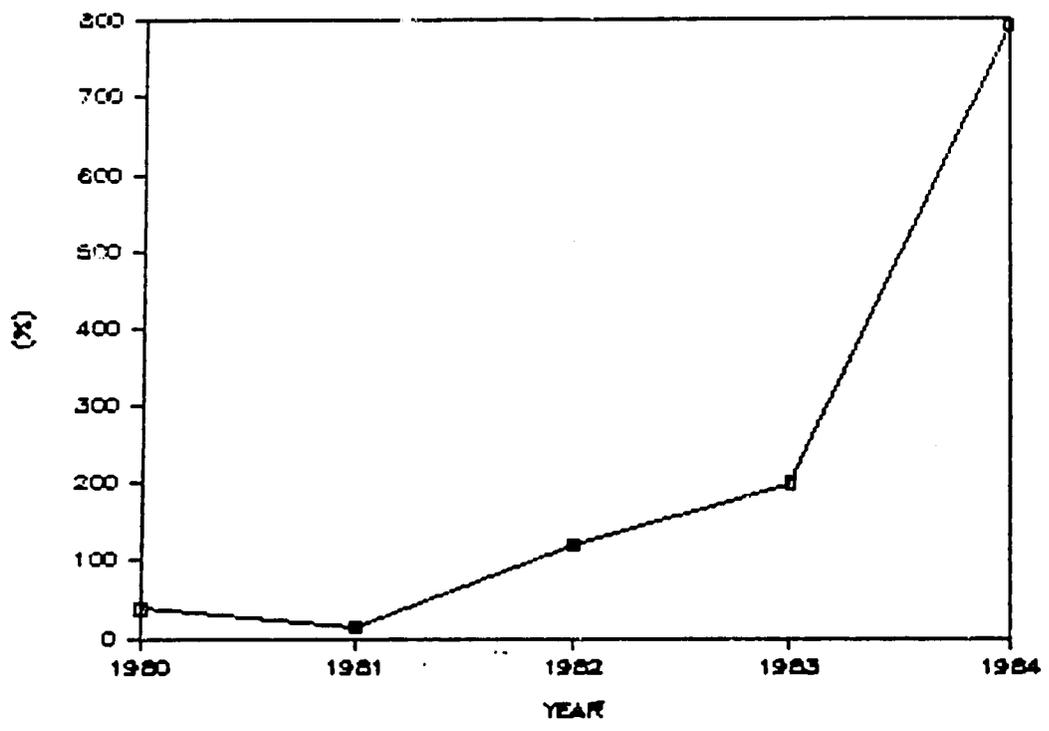


*1985 estimated inflation rate: 20,000%

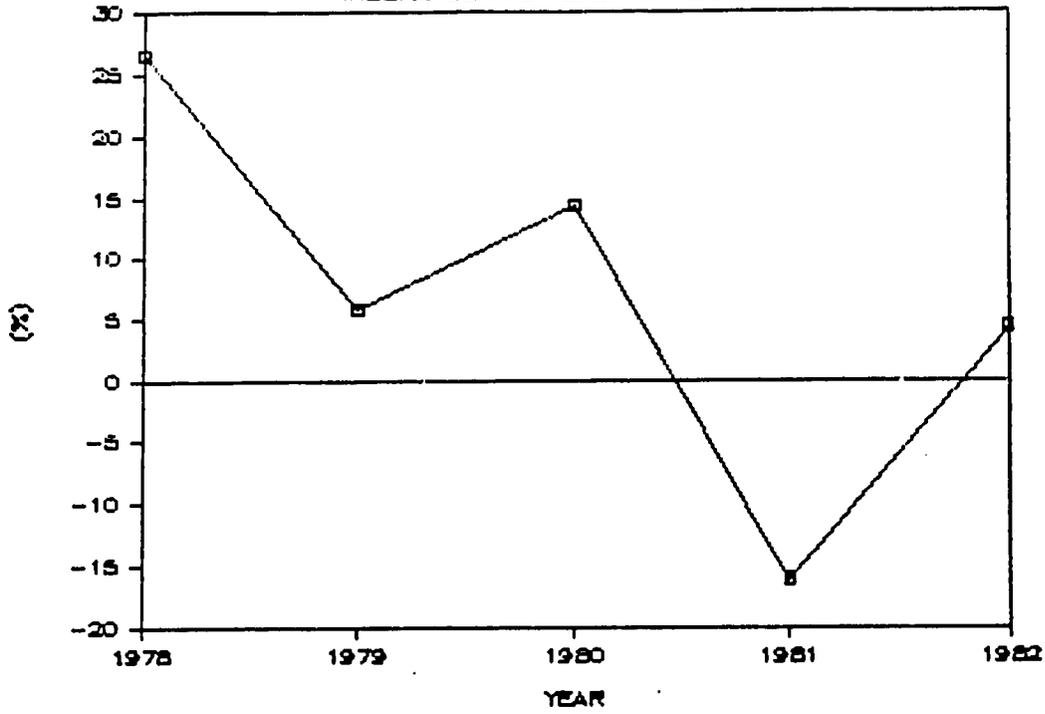
BOLIVIA'S REAL INTEREST RATE



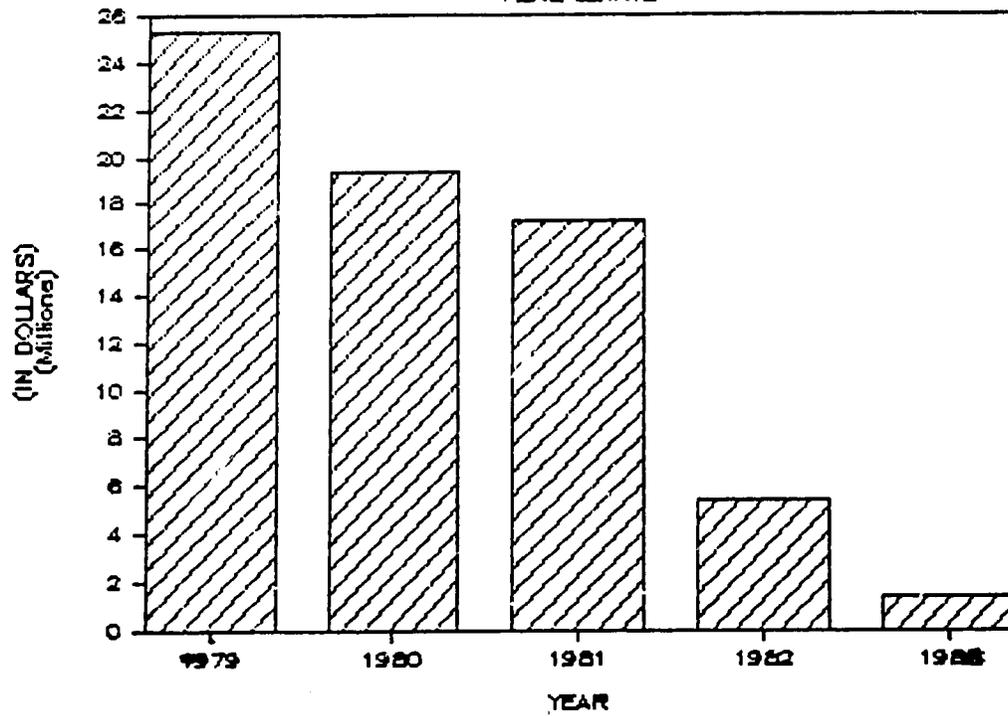
PERCENT CHANGE IN MONEY SUPPLY



GROWTH RATE OF THE BANKING,
INSURANCE AND REAL ESTATE SECTOR



GNP FROM BANKS, INSURANCE AND REAL ESTATE



C. GOVERNMENT ATTITUDES

1. The Estenssoro administration was elected in July, 1985. It is committed to solving economic problems through a free market approach. This orientation shaped the austere economic program and the regulatory changes implemented in August. The policy is also designed to win IMF approval and hopefully reduce external financing pressures.
2. Prices
GOB is attempting to allow the free market to control prices by gradually phasing out subsidies as progress is achieved in the economic development of the country.
3. Agriculture
In an effort to promote export oriented crops, the GOB has established Centros Operativos de Agropoder to foster changes in the agricultural sector, and is encouraging overseas investment in this sector.
4. Industry
The GOB is lowering levels of protectionism. Government aid is directed toward priority sectors in the following hierarchy: food industries; clothing and metal processing industries; and artisan ware production.
5. Parastatals
The new administration has espoused a policy of decentralizing public sector operations in an effort to reduce bureaucracy, increase financial control, and reduce the power of mining and petroleum employee unions. The two major parastatals, COMIBOL (the state mining company) and YPFB (the state petroleum company), ran deficits in 1984 amounting to 2.36% and 1.04% of GDP respectively.

D. REGULATORY CLIMATE

1. The following regulatory changes made by the new administration reflect the GOB's desire to allow free market processes to govern the economic activities of the country. It appears that many of these changes will improve the economic conditions in the country, however it is too early to determine the effectiveness of the measures taken.
2. Foreign exchange control
GOB has changed the policy of maintaining a fixed (and extremely overvalued) exchange rate amidst uncontrollable inflation. Appendix A illustrates the huge disparity which existed between the official and parallel exchange rates before the new economic policy was implemented in August, 1985. The new policy still maintains an official exchange rate, however the rate is adjusted at least twice weekly to align it with the market value. This measure, together with the devaluation of the peso (from 75,000 pesos to 1.1 million pesos to the US dollar, a 93% devaluation), is expected to help improve Bolivia's critical balance of payments situation.
3. Trade control/tariffs
GOB has also liberalized trade policy by abolishing all import prohibitions and reducing previously exorbitant tariffs to a flat 10% ad valorem duty plus a variable duty. This change in regulation was an attempt to reduce smuggling and thus improve revenue collection.
4. Price control
The new GOB program abolishes virtually all price controls.
5. Investment regulations
Foreign investment is governed by the Cartagena Agreement, which determines joint venture requirements, length of investment, etc. Available sources did not indicate whether investment regulations were amended under the new economic program.

6. Labor unions

Labor unions are extremely powerful in Bolivia. The COB (Bolivian Worker's Confederation), is a powerful political entity, which has achieved much for workers through hunger strikes, mass demonstrations, and political demonstrations. Other powerful unions are those for transport workers, miners, and the National Confederation of Campesino Workers. There are many instances in Bolivia's history of strikes which have virtually paralyzed the country. Labor unions appear to be losing influence, as evidenced by the government's put down of nation-wide strikes opposing the new austere economic program (see section A.1.)

E. FINANCIAL MARKETS

1. Monetary system

- a. Central Bank of Bolivia
Regulates the monetary and credit expansion for the country. In addition to traditional central banking functions, the Central Bank has made extensive outlays to cover Bolivia's increasing deficit.
- b. Financial division of the Bolivian Corporation for Development
This parastatal channels multilateral and bilateral donor funds toward public and private sector projects.
- c. Commercial banks
There are currently 13 domestic and six foreign commercial banks in Bolivia (see Appendix B.) In 1977, commercial banks controlled half of total available funds. The majority of commercial bank loans have traditionally gone to the private sector; with industry receiving one half of available credit, commerce one quarter, and GOB and other sectors the remainder.
- d. Development banks
There are two public sector development banks which receive funds directly from the Central Bank:
 - Banco Minero de Bolivia - was established to assist the country's mining operations; and
 - Banco Agricola de Bolivia - was created to stimulate agricultural development.

The four other development banks were established by the private sector. Two of the private development banks (Banco Industrial and Banco de Finciamiento Industrial) specialize in providing medium to long term financing to the industrial sector. The others (Banco de Inversion Boliviano S.A. and Banco Real de Inversiones S.A.) provide funds for investment in general. Most domestic bank funds go to the agricultural sector, with the industrial sector (especially mining) second.

2. Non-banking financial institutions

a. Bolivian Social Security System (el Sistema de Seguridad Social de Bolivia)

The Instituto Boliviano de Seguridad Social (IBSS) is the central institution. Other institutions in the system include nine social security credit unions (see Appendix B), and seventeen employer-matching funds distributed throughout other economic sectors.

The IBSS is the major non-banking mobilizer of savings in Bolivia. It supplies funds to commercial banks through deposits, and provides direct loans to subscribers. The IBSS supplies long term funds primarily to the housing and construction industries, and, to a lesser extent, to the mining industry.

b. Financial institutions supporting the housing industry

There are a variety of institutions supporting the construction industry in Bolivia:

- Banco de la Vivienda - a mixed capital housing bank
- Banco Hipotecario Nacional (Seccion Hipotecaria) - funded from mixed capital and mortgage bonds
- Housing service institutes (see Appendix B) - supported by both the public and the private sectors. These institutes initiate activities designed to improve urban and rural communities (such as building projects and real estate purchases.) Housing service institutes also provide mortgages for low income families.
- Savings and loan associations - there are 17 S&Ls which are funded through the National Housing Fund (Caja Central de Ahorro y Prestano para la Vivienda)

c. Credit unions

There is an extensive credit union system in Bolivia, consisting of 180 credit unions and a national trade association as the central institution (Federacion Nacional de Cooperativos.) Credit unions are the major depositories for the general public and small businesses, as they do not require the collateral demanded by banks. They invest in direct capital for industry and in common stocks. Credit unions also provide funds to the agricultural and housing industries.

d. Insurance companies

There are 19 insurance companies, of which 15 are domestic, and four are foreign. Eleven of the companies offer life insurance. Insurance companies channel their funds through banking system deposits and direct investment in the private sector.

e. Exchange houses

There are 25 foreign exchange houses in Bolivia.

3. Bolivia has no integrated system for regulating capital markets. Securities trading occurs on a limited basis as Bolivia has no Exchange.

NOTE:

Available sources contained no information pertaining to the tax or accounting systems of Bolivia.

Information on the financial system of Bolivia is dated 1977; no more recent sources were located.

APPENDIX A

DISPARITY BETWEEN OFFICIAL AND PARALLEL EXCHANGE RATES
(Pesos per U.S. Dollar)

Date	Official Exchange Rate	Parallel Rate (Buying)	Estimated Parity Rate
-----	-----	-----	-----
1972	20		20
1979	25		35
1980	25		45
1981	25		55
12/1982	198	280	220
12/1983	505	1,300	907
3/1984	505	3,200	1,495
6/1984	2,000	3,300	3,719
9/1984	2,000/5,000	15,000	6,198
12/1984	9,000	20,000	20,892
1/1985	9,000	73,016	35,258
2/1985	45,000	141,101	99,872
3/1985	45,000	128,137	124,998
4/1985	45,000	167,428	139,483
5/1985	75,000	272,375	188,742
6/1985	75,000	481,756	337,711
7/1985	75,000	885,746	561,623
8/1985	75,000	1,182,303	934,883

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APPENDIX B

FINANCIAL INSTITUTIONS IN BOLIVIA

Social Security Credit Unions:

- Caja Nacional de Seguridad Social (National Social Security Credit Union)
- Caja Petrolera (petroleum)
- Caja Choferes (drivers)
- Caja Ferroviaria (mining)
- Caja Militar (military)
- Corporacion Boliviano de Fomento (development)
- Corporacion Boliviano Universitaria (universities)
- Servicio Nacional de Caminos (road system)
- Fondo para Empleados de los Bancos del Pais (banking)

Housing Service Institutes

- Consejo Nacional de Vivienda (CONAVI)
- Consejo Nacional de Petroleros
- Consejo Nacional de Mineros
- Consejo Nacional del Magisterio Fiscal y Fabriles
- Consejo Nacional del Constructores y Graficos

Other financial institutions for which no information was available:

- Auto Plan Pasanaku
- Capitales Unidos
- Arca de la Esperanza
- Caja de Ahorro y Credito Popular
- La Compania Boliviana de Sistema