BOLIVIA

THE BANK’S COUNTRY STRATEGY WITH BOLIVIA
2008-2010

This document was prepared by the project team consisting of: Pablo Roldán (CSC/CSC); Gerhard Lair (CAN/CAN); Guillermo Zoccali (CSC/CSC); Andrea Otero (CSC/CSC); Lena Siciliano Bretas (CSC/CSC); María Teresa Frías (CSC/CSC); and Yony Orbegoso (CAN/CAN). Also assisting in the preparation of this document were Joel Branski (Representative, CAN/CBO); Rodolfo Gastaldi (Deputy Representative, CAN/CBO); Eddy Linares (CAN/CBO); Marcelo Lucio Barron Arce (CAN/CBO), and Headquarters functional division specialists.
## EXECUTIVE SUMMARY

I. THE DOMESTIC CONTEXT .................................................................................................................. 1

   A. Political and social context ........................................................................................................... 1
   B. Recent economic transformations ................................................................................................. 2
   C. Current macroeconomic assessment and outlook ........................................................................ 2
   D. Poverty, inequality, and opportunities .......................................................................................... 4

II. THE GOVERNMENT’S NATIONAL DEVELOPMENT PLAN AND THE COUNTRY’S MAIN DEVELOPMENT CHALLENGES ........................................................................... 4

III. THE PREVIOUS STRATEGY .............................................................................................................. 5

IV. THE BANK’S COUNTRY STRATEGY WITH BOLIVIA 2008-2010 ............................................... 6

   A. Level of post-debt-forgiveness assistance and the “blend” scenario ........................................ 7
   B. Objectives and strategic focus: Central pillars of the country strategy ...................................... 7
      1. Productivity, employment, and productive infrastructure ....................................................... 8
      2. Social welfare and water and sanitation development ........................................................... 10
      3. Opportunities for the majority and development with identity .......................................... 11
      4. Institutional strengthening at the national and decentralized level ..................................... 12
   C. Implementation of the country strategy ....................................................................................... 12
      1. The country’s fiduciary framework ......................................................................................... 12
      2. Country financing parameters (CFPs) .................................................................................. 13
      3. Instruments to be used in implementing the country strategy ............................................. 13
      4. Harmonization and coordination with other donors ............................................................ 13
      5. Consultations with civil society ............................................................................................. 14

V. RISKS ASSOCIATED WITH IMPLEMENTING THE COUNTRY STRATEGY ................................. 15

   A. Indirect risks to implementation of the Bank’s country strategy .............................................. 15
   B. Direct risks to implementation of the Bank’s country strategy ................................................. 16
**ANNEXES**

<table>
<thead>
<tr>
<th>Annex I</th>
<th>Current macroeconomic assessment and outlook</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annex II</td>
<td>NDP: Progress toward the Millennium Development Goals by 2015</td>
</tr>
<tr>
<td>Annex III</td>
<td>The National Development Plan and the country’s main development challenges</td>
</tr>
<tr>
<td>Annex IV</td>
<td>Previous strategy and portfolio: Main lessons for the new strategy</td>
</tr>
<tr>
<td>Annex V</td>
<td>Matrix of Country Financing Parameters (CFPs)</td>
</tr>
<tr>
<td>Annex VI</td>
<td>The consultation process</td>
</tr>
<tr>
<td>Annex VII</td>
<td>Possible effects of institutional changes in the hydrocarbons and mining sectors</td>
</tr>
<tr>
<td>Annex VIII</td>
<td>Illustrative operations program 2008-2010</td>
</tr>
<tr>
<td>Annex IX</td>
<td>Bank disbursements and flows with the country</td>
</tr>
<tr>
<td>Annex X</td>
<td>Matrix of international cooperation intervention areas</td>
</tr>
<tr>
<td>Annex XI</td>
<td>Bibliography</td>
</tr>
</tbody>
</table>
ABBREVIATIONS

ABC  Bolivian Highways Administration
BCB  Central Bank of Bolivia
CAF  Andean Development Corporation
CSAC Civil Society Advisory Council
CCLIP Conditional credit line for investment projects
CFP  Country financing parameters
CIMDM Interagency Committee for the Millennium Development Goals (Bolivia)
COMIBOL Corporación Minera de Bolivia [Bolivian Mining Corporation]
DFID Department for International Development (United Kingdom)
EU   European Union
FDI  Foreign direct investment
GruS Grupo de Socios para el Desarrollo de Bolivia [Bolivia Development Partners Group]
HIPC Heavily Indebted Poor Countries
IIRSA Initiative for the Integration of South American Regional Infrastructure
ILO  International Labour Organisation
IMF  International Monetary Fund
INE  National Statistics Institute
MDGs Millennium Development Goals
MDRI Multilateral Debt Relief Initiative
NLF  New Lending Framework (IDB)
OC   Ordinary Capital
NDP  National Development Plan
PRS  Poverty Reduction Strategy
SCF  Structured and Corporate Financing Department
SEP  Social Entrepreneurship Program
SIGMA Integrated System of Management and Administrative Modernization
SINAFID National Development Finance System
SWAp Sector-wide approach
TC   Technical cooperation
UDAPE Economic and Social Policy Analysis Unit
USAID United States Agency for International Development
VIPFE Vice Ministry of Public Investment and External Financing
YPFB Yacimientos Petrolíferos Fiscales Bolivianos [State oil company]
EXECUTIVE SUMMARY

After nearly 20 years of relative political and social stability, at the beginning of the new millennium Bolivia faced a crisis of multiple dimensions: political, economic, social and institutional. Between 1985 and 2005, seven constitutional governments succeeded each other, supported by a system of governance based on coalition pacts negotiated among the traditional political parties represented in the National Congress. This system, referred to as “pact democracy,” was undermined by the lack of any significant progress in reducing poverty and also by a patronage approach to managing the State apparatus, which in the end served to alienate civil society and social movements from the political parties, sparking the collapse of the system.

The election in December 2005 of President Evo Morales and of prefects in the country’s nine departments opened a new stage in the democratic process and in the relationship between the State and society, and gave rise to a new constellation of political and social players in Bolivia. The political agenda of this new stage entails great challenges. Issues such as social and political inclusion, as well as open recognition of the country’s ethnic reality, have taken on greater importance and will be key factors in the new modus operandi that will determine the relationship between the national State and Bolivian society, as they seek to overcome the exclusion and the corporatist practices of the past that were widely seen as serving special interests.

The government of President Evo Morales is embarked on a program very different from that pursued since 1985, one that seeks to overcome structural bottlenecks in the political, social, institutional and economic spheres. The new thrust of public policy is to give indigenous groups a leading role, in both urban and rural areas, with greater State intervention in the economy, especially in the management of the country’s important natural resources. Bolivia is now engaged in a debate over the feasibility of this approach, and its ability to avoid falling into a corporatist vision of economic and social management. In this context, building a sustainable system of governance is a key challenge.

The Constituent Assembly process that began in July 2006 concluded with the approval of a new text, but it has not yet garnered consensus among the different political factions represented in that body. Therefore, the country’s new Constitution is still an unsettled matter, and the mechanism for adopting it will ultimately have to be approved and ratified by two successive referendums, expected to take several months. This has heightened the uncertainty surrounding the country’s future social and economic organization.

Recent macrofinancial indicators for Bolivia have performed well, giving the government some leeway for achieving its goal of reorienting the development model. Since 2006, the Bolivian economy has been helped by a favorable international setting: prices for Bolivia’s exports have been rising, international interest rates are low, external remittances have increased, and the Latin American region is recording sustained rates of economic growth. The government’s macroeconomic policy has successfully absorbed significant surpluses from mining and oil and gas production, and has accumulated record levels of international reserves, while maintaining relative price stability, albeit with a fresh outbreak of moderate inflation recently. In addition, forgiveness of a large part of Bolivia’s foreign debt by multilateral and bilateral cooperation agencies has allowed Bolivia to reduce its vulnerability
on this score, cutting the country’s total public debt to 30% of GDP. In this context, the prospects for fiscal sustainability of the debt have improved greatly, giving the country more financial breathing room.

Despite the ambitious economic and institutional reforms launched in Bolivia since the mid-1980s, results have been disappointing in terms of reducing poverty and inequality. Data for 2005 show that nearly 60% of the population is still poor, and this figure reaches 80% in rural areas. Extreme poverty currently afflicts 37% of the population nationwide, and 55% of the rural population, with indigenous people suffering most from the lack of education, health, sanitation and other basic services. In 2005, Bolivia’s Gini coefficient was 0.60, placing the country among the most nonegalitarian in Latin America.

Looking ahead, any slowdown in the regional and global economies could reverse the currently favorable international prices for Bolivia’s raw materials exports, a prospect that underlines the importance of mitigating the domestic risk factors related to debt sustainability as well as to growing expenditure pressures in the context of fiscal decentralization, the recent inflationary pressures, institutional weaknesses, and shortcomings in public management, the high degree of dollarization in the financial system, and the uncertainties and costs associated with the eroding business climate’s ability to attract private investment and create jobs. It should be noted that current levels of domestic investment, and more importantly of foreign investment, would have to rise sharply to achieve the investment and growth forecasts in the government’s National Development Plan (NDP). In particular, the country’s image as a reliable energy supply and the commitments it has assumed with respect to the export and industrialization of gas will require significant investments in this sector. While the short-term risks for oil and gas are less than those facing the mining sector (thanks to mechanisms for indexing the price of gas to baskets of fuels), there are still risks associated with fluctuating international demand. Consequently, the management of windfall revenues is a crucial issue for fiscal policy, and has led the government to consider creating an intergenerational stabilization and savings fund.

The deep divides along ethnic, social, productive and regional development lines that characterize Bolivia are a barrier to the unity and cohesion of society and, if they persist, will hold back the country’s economic and social progress. The NDP notes that finding solutions to ethnic, social and productive issues will be crucial for progress toward a more competitive and inclusive development model. The Bank sees much room for complementarity between its proposed activities described in this document and the NDP, and considers that one way of closing those gaps is through a comprehensive model of productive development that will offer opportunities for the country’s majority and will strengthen its institutions.

Bolivia is currently going through a process of profound political, cultural, social and economic changes. The intensity and depth of those changes remains to be seen, and like any process of change, this one brings with it a degree of uncertainty about the future, which clouds the reliability of long-term projections. The drive for greater departmental autonomy now under way and the decisions being taken by the Constituent Assembly entail critical and far-reaching structural reforms that could take a long time to implement. To support a process of this magnitude more effectively, this Country Strategy covers the remainder of
the presidential term (2008-2010) and has been designed with sufficient flexibility to adapt to the country’s new political and social dynamics.

In this context, the Bank will adjust its activities to the guidelines that emerged from the process of dialogue and consultation with the national authorities. Achieving a sustainable reduction in poverty will remain the general objective guiding those activities, within the framework of the general objectives identified in the NDP. Given the many and varied kinds of development support that the country needs to reduce the poverty gap, the new strategy calls for closer targeting of the Bank’s activities in Bolivia, which in turn will support priority sectors and enable international cooperation to be coordinated more effectively.

Within this framework, the Country Strategy would focus work in the following four strategic areas, dealing with: (i) productivity, competitiveness and productive infrastructure as needed to promote balanced and sustained economic growth centered in areas with high economic potential and clear comparative advantages; (ii) development of the water and sanitation sector and socially productive development centered in municipalities where poverty levels and vulnerability are high; (iii) creating opportunities for the majority and development with identity; and (iv) strengthening the State apparatus through institutional development at the national level and enhanced decentralization that will produce a more efficient and effective public sector. The guiding theme of new interventions will be to develop better channels of interaction between the public sector (central government, prefectures and municipalities), civil society and the productive sector, and to give special attention to close coordination and harmonization with the donor community. The Structured and Corporate Financing Department (SCF) can round out the financing requirements of medium- and large-scale production-oriented enterprises in the sectors within its mandate. In the short term, the majority of opportunities should lie in agroindustry, manufacturing, and the capital market. Such loans have been shrinking as a share of total approved lending, due mainly to changes in the legal and regulatory environment and the prevailing business climate in the country.

Internal decisions about the country’s political, social and institutional organization, the mechanisms for applying economic reforms, and to a lesser extent the external setting and natural threats constitute the most important risks in implementing the Bank’s new strategy with the country. The risk analysis looked at two angles or channels for classifying the transmission of impacts. On one hand, the analysis identified those risks that condition the country’s political, institutional and economic setting and that indirectly affect implementation of the Bank’s country strategy. On the other hand, it grouped those risks that could impact directly on its implementation, and for which mitigation measures will be considered in the design of projects and programs to be financed.

In response to this risk typology, the design of the country strategy is sufficiently flexible for the Bank to adapt and respond effectively to the dynamic changes occurring in the country’s priority strategic sectors. In addition, the use of programmatic approaches and flexible instruments under the New Lending Framework will give the Bank the necessary headroom to address risks as they arise.

The following strategy matrix shows that the activities proposed by the Bank are in line with the country’s priorities. This matrix reflects the strategy’s flexible design, which will allow
it to respond to possible changes of direction or priority in the country’s policies. The matrix contains relatively few indicators, and it can be reasonably expected that they will be achieved. Consequently, tracking them will help to determine the most appropriate response from the Bank. The matrix will be monitored in conjunction with the annual performance review of the Bank’s portfolio.
# STRATEGY MATRIX
## THE BANK’S COUNTRY STRATEGY WITH BOLIVIA 2008-2010

### Key targets in the National Development Plan (NDP) and the Bank’s country strategy
- Average GDP growth exceeding 5%, on a rising path: Baseline: 4.6% (2006)
- Steady progress in reducing moderate poverty to 50% (2011): Baseline: 59.6% (2005)
- Reduction of inequality: Baseline: Gini coefficient 0.60 (2005)

<table>
<thead>
<tr>
<th>Selected NDP objectives</th>
<th>NDP Medium-term development impact indicators</th>
<th>Medium-term intermediate and operational objectives to which the Bank’s country strategy contributes</th>
<th>Bank activities</th>
<th>Country strategy pillars and proposed Bank activities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1. Productivity, employment and productive infrastructure</td>
</tr>
<tr>
<td>“Productive Bolivia”</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


2. Indicators/targets based on information available as of February 2008; to be adjusted during the strategy implementation period as individual projects are designed and approved.
<table>
<thead>
<tr>
<th>Selected NDP objectives&lt;sup&gt;1&lt;/sup&gt;</th>
<th>NDP Medium-term development impact indicators</th>
<th>Medium-term intermediate and operational objectives</th>
<th>NDP Medium-term intermediate and operational objectives to which the Bank’s country strategy contributes&lt;sup&gt;2&lt;/sup&gt;</th>
<th>Bank activities Active portfolio</th>
<th>Country strategy pillars and proposed Bank activities</th>
</tr>
</thead>
</table>

**“Dignified Bolivia”**

<p>| Eradicate poverty and exclusion and expand access to basic services | The under-five child mortality rate declines fast enough to meet the MDG goal of 30 per 1000 live births (Baseline: 92 deaths per 1000 live births in 2002) | | | | 2. Social welfare and development of the water and sanitation sector |
| Increase the coverage of water and sewer services | 1.9 million additional residents provided with drinking water service between 2006 and 2010 (Baseline: 2.6 million -26.9% without access in 2006) | Strengthened institutional framework for the water and sanitation sector | Financing of new projects as demand arises, and clear rules for channeling funding to the sector | Loans - PROAGUAS I - La Paz drainage system <strong>Nonfinancial products</strong> - Sector strategic plan in water and basic sanitation a) Water and sewer - Small Communities Water Program – PROAGUAS II - Water and sanitation for peripheral areas - La Paz drainage system II |</p>
<table>
<thead>
<tr>
<th>Selected NDP objectives</th>
<th>NDP Medium-term development impact indicators</th>
<th>Medium-term intermediate and operational objectives</th>
<th>NDP Medium-term intermediate and operational objectives to which the Bank’s country strategy contributes</th>
<th>Bank activities Active portfolio</th>
<th>Country strategy pillars and proposed Bank activities</th>
</tr>
</thead>
<tbody>
<tr>
<td>A more equitable society</td>
<td>Extreme poverty declines steadily to 27% in 2011 (Baseline: 36.7% in 2005)</td>
<td>Improved human development indicators in communities with high poverty rates</td>
<td>Pilot programs for social welfare and community development in selected urban and rural communities</td>
<td>Technical cooperation</td>
<td>- Preparation of the water program for periurban areas</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Loans</td>
<td>- Communities in action (pilot)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Expanded PROPAS II</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Neighborhood improvements – Phase II</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Nonfinancial products</td>
<td>- Study on teenage sexual activity, pregnancy, and motherhood</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Study on reproduction and life satisfaction: Evidence from Bolivia</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Quality and relevance of secondary education in Bolivia</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Strengthening of territorial management of public education</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Strengthening of local management in education</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Technical cooperation</td>
<td>- Emergency assistance for rain, flood, and landslides</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>b) Social welfare and community development Loans</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Communities in action II (rural area)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Reciprocal communities (urban areas)</td>
</tr>
<tr>
<td>“Democratic Bolivia”</td>
<td></td>
<td></td>
<td></td>
<td>Civil registry system</td>
<td>3. Inclusion of the majority and development with identity</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>institutionalized and made universal by 2010</td>
<td>- Support for the civil registry system</td>
</tr>
<tr>
<td></td>
<td>Improve Bolivia’s score in Transparency International’s Corruption Perceptions Index (Baseline: 2.9 in 2007)</td>
<td>Greater capacity to exercise civil rights and more democratic access to basic services</td>
<td></td>
<td>Technical cooperation</td>
<td>- Educational opportunities for teenagers in Potosí</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>- Inclusion strategy for trade and integration</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>MIF</td>
<td>- Evaluation and certification of job skills</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Nonfinancial products</td>
<td>- Support for analysis of fiduciary systems</td>
</tr>
<tr>
<td>Selected NDP objectives¹</td>
<td>NDP Medium-term development impact indicators</td>
<td>Medium-term intermediate and operational objectives</td>
<td>NDP Medium-term intermediate and operational objectives to which the Bank’s country strategy contributes²</td>
<td>Bank activities Active portfolio</td>
<td>Country strategy pillars and proposed Bank activities</td>
</tr>
<tr>
<td>--------------------------</td>
<td>-----------------------------------------------</td>
<td>---------------------------------------------------</td>
<td>---------------------------------------------------------------------------------</td>
<td>--------------------------------</td>
<td>---------------------------------------------------</td>
</tr>
<tr>
<td>“Sovereign Bolivia”</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>International cooperation aligned with the country’s priorities</td>
<td>Improvement in the indicators of the Paris Declaration on Aid Effectiveness (2005) consistent with the Santa Cruz Declaration (2006)</td>
<td>Alignment and coordination procedures strengthened</td>
<td>Increase in operations co-financed and harmonized with other cooperation agencies</td>
<td>- Active participation in the Bolivia Development Partners Group and the Coordination Mechanism</td>
<td>- Continue aligning the Bank’s work with government priorities and the activities of other donors</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Better programming of international cooperation resources</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Annual disbursements increase as a % of the active portfolio amount</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Net flows of cash and loans are positive</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Portfolio quality</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

¹ Selected NDP objectives refer to the overall objectives of the National Development Program.
² NDP Medium-term intermediate and operational objectives are specific targets set for the program's implementation.
I. THE DOMESTIC CONTEXT

A. Political and social context

1.1 At the beginning of the new millennium, after nearly 20 years of relative political and social stability, Bolivia faced a crisis of multiple dimensions: political, economic, social and institutional. Between 1985 and 2005, seven constitutional governments succeeded each other, backed by a system of governance based on coalition pacts negotiated among the traditional political parties represented in the National Congress. The election in 2005 of President Evo Morales and of prefects in the country’s nine departments opened a new stage in the democratic process and in the relationship between the State and society, and gave rise to a new constellation of political and social players in Bolivia. The government of President Evo Morales is embarked on a program very different from the one pursued since 1985, in which it is seeking to overcome structural bottlenecks in the political, social, institutional and economic spheres. The new thrust of public policy is to give indigenous groups a leading role, in both urban and rural areas, with greater State intervention in the economy, especially in the management of the country’s important natural resources.

1.2 In July 2006, elections were held for the Constituent Assembly and the Referendum on Departmental Autonomy (RA). The Constituent Assembly had a very broad agenda for debate. Among the crucial and hotly debated issues were: (i) the concept of the State as plurinational or unitary; (ii) the features of the new development model; (iii) the type of property-holding system (private, community, collective); (iv) the model of autonomy to be adopted for the departments, regions, municipalities, and the new indigenous territories; (v) the new organization of the executive, legislative and judicial branches; (vi) reelection of the president and other authorities; (vii) ownership of natural resources, particularly land; and (viii) the role that private investment (domestic and foreign) should play. The Constituent Assembly concluded its work in December 2007 with a newly approved text for the country’s new Constitution, but there is still no consensus among the different political factions represented in that body, and this has delayed the process of adopting it, which calls for two referendums, one to approve the text and the other to ratify it, a process that in itself could take several months. New developments in 2008 confirmed how complex the sociopolitical situation is in Bolivia, when the country’s four eastern provinces (Santa Cruz, Tarija, Bení, and Pando) held referendums approving autonomous charters for their regions. Meanwhile, President Morales and the Senate agreed to hold a national referendum in August 2008, putting to a vote the mandate of the president, vice president, and eight prefects (governors) of the regional departments. The preliminary results of this popular consultation indicate a clear victory for President Morales, with 65.9% of the valid votes; the prefects confirmed in office in Santa Cruz, Tarija, Bení, Pando, Potosí, and Oruro; and the prefects of La Paz and Cochabambu unseated.

1.3 The main challenge now is to build a new institutional and governance structure that will embrace the various political tiers that dominate the country’s political and social landscape. A first tier of governance is represented by the Congress, and...
depends on the relationship between the government parties and the opposition. A 
second tier depends on the alliances that are forged between the national and 
departmental levels of government. The third tier of governance relates to the way 
the government handles its relations with the social movements that in recent years 
have acquired great social and political clout. In the meantime, the stability of these 
three tiers will depend on the success of the Constituent Assembly in cementing the 
structure of governance.

B. Recent economic transformations

1.4 The election of President Evo Morales marks a turning point in the country’s 
development model. The government’s economic and social agenda is set out in the 
National Development Plan (NDP) which starts from the notion that State 
capitalism, neoliberalism and neocolonialism are responsible in a structural sense for 
Bolivia’s economic stagnation, its dependency and its poverty. Given the 
disappointing results produced by previous models, the government is proposing a 
new pattern of integral and diversified development, one in which the central players 
are the State, economic agents and social organizations, within an intercultural 
framework. The objective, as set forth in the NDP, is internal accumulation, the 
redistribution of wealth and the eradication of poverty, creating thereby a new era of 
State ascendancy, with the recovery and industrialization of the country’s renewable 
and nonrenewable natural resources.

1.5 In moving toward this new development model, the government of President 
Morales has undertaken a series of substantive reforms. The first move was to 
nationalize the oil and gas industry in 2006. The second focus of action was the 
agrarian reform. In this connection, the government sponsored legislation 
reinstituting the agrarian reform on a community basis and launching the 
“Mechanized Agrarian Revolution.” Its objective is to see that any land not fulfilling 
a social and productive function will be redistributed among the indigenous 
population and communities. A third focus is to re-assert the pre-eminence of the 
Corporación Minera de Bolivia (COMIBOL), whereby the State, through the 
Ministry of Mining and Metallurgy, is to have a greater role as the driving force 
behind development of the mining industry.

C. Current macroeconomic assessment and outlook

1.6 Recent macrofinancial indicators for Bolivia have performed well, aided by the 
favorable international conditions of recent years, particularly from 2006 onward: the 
price scenario for Bolivia’s principal export commodities continues to trend upward, 
international interest rates are low, external remittances have increased, and the Latin 
American region is recording sustained rates of economic growth. At the same time, 
Bolivia has benefited from further and substantial forgiveness of its debt to 
multilateral and bilateral cooperation agencies.

1.7 Macroeconomic policy has also benefited from significant surpluses from mining 
and hydrocarbons production, making it possible to build up record levels of international 
reserves while maintaining financial stability. The country’s fiscal position has a

---

positive track record since 2002, moving from a global deficit of around 9% of GDP in that year to overall and primary surpluses of 2% and 3% of GDP, respectively, in 2007. This sound fiscal performance was assisted by the favorable external economic situation, greater domestic activity, improvements in the domestic tax collection system, and changes in the taxation and ownership structure of the basic enterprises, primarily in the oil and gas sector.

1.8 Against this backdrop, economic growth accelerated to 4.6% in 2007, with growth projections of 5.5% to 6.0% in 2008, accompanied by a sustained decline in the open unemployment rate to 5.1% in 2006. Stronger economic activity and aggregate demand was accompanied by greater pressure on the price structure, with the annualized consumer inflation rate rising from 5.0% at end-2006 to 17.3% in June 2007. The external sector showed robust performance, running surpluses in the current account of the balance of payments equivalent to 12% of GDP in 2006, and 14% of GDP in 2007, due mainly to record prices for the basket of exported goods, whose value neared US$5.5 billion in 2007.

1.9 The country’s total public debt has fallen sharply from 74% of GDP in 2005 to 34% currently (US$12.8 billion). In net present value terms, the debt now stands at 30% of GDP, and is only 17% of GDP when government deposits in the financial system are factored in. Actions taken under the Multilateral Debt Relief Initiative (MDRI) have played a particularly important role here, reducing Bolivia’s debt by nearly 25% of GDP. The very positive trend in the country’s solvency and liquidity indicators has left them well below the sustainability risk thresholds established for the Heavily Indebted Poor Countries (HIPC) Initiative, and under a base-case macroeconomic policy scenario they are expected to decline further in coming years.

1.10 The conclusion that Bolivia’s prospects for fiscal and debt sustainability have improved significantly is backed by an independent analysis of the performance of oil and gas revenues, the likely mechanism and dynamics of their distribution (either for constituting a stabilization fund or for accelerating public expenditure and investment), and potential public expenditure and savings paths over the period 2006-2015.² These assessments of the risks to the country’s debt sustainability are compatible with the results of the IMF exercise conducted in 2006-2007,³ which suggest that debt ratios would remain within the limits of sustainability over the long term even under an alternative scenario of lower oil prices. The Bank classified Bolivia as having a low risk of debt distress in the context of the proposal for implementing the Debt Sustainability Framework and Enhanced Performance-based Allocation System.⁴

² For further technical details and the result of simulations, see Navajañ, Fernando, Daniel Artana, Juan Luis Bour and Marcelo Catena (2007), “Bolivia: Tópicos Marco-Fiscales Seleccionados y Perspectivas de Sostenibilidad Fiscal,” IDB.
³ IMF (2006), “Bolivia: 2006 Article IV Consultation—Staff Report; Staff Statement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Bolivia,” Country Report No.06/270, July.
1.11 In short, to sustain a high level of equitable growth in Bolivia within a framework of macroeconomic stability and debt sustainability, it will be particularly important to mitigate further the factors of domestic risk, such as growing expenditure pressures in the context of fiscal decentralization, the recent inflationary pressures, institutional weaknesses and problems in public management, the high level of dollarization in the financial system, and the uncertainties and costs associated with the eroding business climate’s ability to attract private investment and create jobs. Annex I presents a more complete version of the economic analysis.

D. Poverty, inequality, and opportunities

1.12 Despite the ambitious economic and institutional reforms launched in Bolivia since the 1980s, results have been disappointing in terms of reducing poverty and inequality. Data for 2005 show that nearly 60% of the population is still poor, and this figure reaches 80% in rural areas. Extreme poverty currently afflicts 37% of the population nationwide, and 55% of the rural population, with indigenous people suffering the most. There are also significant differences in poverty levels among departments: the extreme poverty rate in Santa Cruz is 25.1%, while in Potosi it is 66.7%.

1.13 Inequality also remains high, and has worsened in some cases. Between 1997 and 2002, Bolivia’s Gini coefficient averaged 0.58, and it rose to 0.60 in 2005, placing the country among the most nonegalitarian in Latin America. This situation can be explained by the persistent substantial differences in access to services and sources of income, the concentration of assets (particularly education and land) in the hands of a few groups, and significant income differences between men and women, and between indigenous and nonindigenous people.

1.14 Despite this, indicators relating to the Millennium Development Goals (MDG) have shown encouraging progress over the last five years, including an increase in the average literacy rate and years of schooling, a decline in malnutrition, an increase in institutionalized childbirth, the eradication of diseases, and greater availability of drinking water and sanitation services (see Annex II). Nevertheless, some of the 2015 goals seem ambitious, particularly if they are analyzed exclusively in terms of the indigenous population, for whom the human development gaps are much greater than the national average. The outcome will depend to a large extent on implementation of the NDP, and on its success in channeling resources to the most isolated and vulnerable population groups.

II. THE GOVERNMENT’S NATIONAL DEVELOPMENT PLAN AND THE COUNTRY’S MAIN DEVELOPMENT CHALLENGES

2.1 The NDP proposes a new policy framework, starting from macroeconomic stability in the real sectors and on the fiscal, external and monetary/exchange fronts, with the goal of securing greater growth and social equity. It calls for a new development model based on recovery and industrialization of natural resources, and promoting economic solidarity based on complementarity and community. NDP activities are grouped around four principal pillars: (i) Bolivia Productiva (“Productive Bolivia”): the objective here is to bring about a radical decrease in poverty levels, by linking
productive issues with social challenges—the challenge of productivity; (ii) *Bolivia Digna* (“Dignified Bolivia”): the government is seeking to create a new State fabric comprising peoples, communities and regions in order to arrive at a socially fair, multicultural and community-based State that guarantees access to basic services and employment—the challenge of social and cultural inclusion and unity in diversity; (iii) *Bolivia Democrática* (“Democratic Bolivia”): the government intends to give the State a new role on the political, institutional, social and economic fronts, by fostering an institutional organization for redistributing economic surpluses in an equitable manner—the challenge of governance; and (iv) *Bolivia Soberana* (“Sovereign Bolivia”): the country’s international relations.

2.2 The Bank has analyzed the NDP both from the viewpoint of overall macroeconomic sustainability and in terms of each of its pillars, identifying challenges and risks associated with the proposed policies. That analysis is reflected in the document entitled Proposal for Policy Dialogue, the IDB Contribution to Bolivia’s National Development Plan, which was discussed with the government in December 2006. That analysis produced a series of recommendations relating to the institutional framework that would be needed to enhance its implementation. Annex III summarizes what the Bank considers the major challenges to implementation of the plan, with a brief description of the policy approaches under each component. Chapter IV of this document describes the areas proposed for future IDB intervention in the country.

### III. THE PREVIOUS STRATEGY

3.1 The general objective of the Bank’s country strategy with Bolivia for 2004-2007 was to help address the challenges facing the country in order to close the gaps that have characterized its development and to reduce poverty. Given the political and social divide prevailing in Bolivia and the difficulty in reaching the consensus needed to implement a medium and long-term development policy that would guide public expenditure or multilateral and bilateral assistance, the 2004-2007 country strategy was conceived as an interim or transitional strategy, identifying interventions that, in coordination with other donors, would lessen the risks of economic and social instability and avoid backsliding in the social achievements of the previous decade. On the basis of those elements, the country strategy focused the Bank’s proposed interventions around the following three themes: (i) improve the management capacity and transparency of the State; (ii) support competitiveness and sustainable development of the private sector; and (iii) enhance efficiency and equity in basic social services delivery. At the same time, recognizing on one hand the great need for resources to enhance the country’s productive infrastructure and, on the other hand, the resource allocation priorities set by bilateral cooperation, it was determined that fresh Bank funding under the country strategy should be targeted largely at efforts to improve the country’s competitiveness.

---

5 The proposal was accompanied by various technical notes and studies, and was then discussed with the Bolivian authorities. See IDB (2006), “Bolivia. Propuesta para el Diálogo de Políticas,” December, [http://re1//h-od1/Documentos/Dialogo.htm](http://re1//h-od1/Documentos/Dialogo.htm)
3.2 Given the country’s situation and the priorities established by the government, the Bank concluded at that time that its support was helping to harmonize short-term objectives. In that context, solid execution of the portfolio was deemed the most important input for achieving results over the medium term. The portfolio showed a significant concentration of funding for enhancing the delivery of basic social services, where Bank financing represented a significant portion of international cooperation earmarked for these sectors. The portfolio also held the potential for taking funds from loans that were nearing their commitment or disbursement deadlines and redirecting them into operations that could have an impact on the quality of people’s lives.

3.3 Bolivia’s recent political and social turmoil has had an impact both on activities that were already under way and those that were planned for implementation with Bank support as part of the strategy: some have experienced delays while others have been dropped as the result of changes in policy and instability and weaknesses in the executing agencies. Despite this, it may be said that in general the strategy was appropriate to the country’s problems, in two major respects: first, its implementation was generally aligned with government program priorities and it produced concrete results in terms of the proposed objectives; and second, the Bank demonstrated flexibility in its capacity to respond and accommodate itself to shifting priorities and to the institutional vagaries of the three successive governments that held office during the period of the strategy. Nevertheless, despite the favorable regional and international economic context, and positive and rising growth rates over the period, the impact on reducing poverty and the gap between urban-rural and indigenous-nonindigenous indicators was only modest. Annex IV summarizes the Bank’s main contributions during the period, and presents an analysis of portfolio performance and of lessons learned from implementation of the 2004-2007 country strategy with Bolivia.

IV. THE BANK’S COUNTRY STRATEGY WITH BOLIVIA 2008-2010

4.1 Bolivia is engaged in a process of profound political, cultural, economic and social change. The intensity and depth of those changes remains to be seen. Any change brings with it uncertainties that affect the reliability of long-term projections. Recognizing this, the Bank’s country strategy with Bolivia proposes to work to shorten time horizons within a conceptual framework that retains flexibility for adapting to the country’s political and social dynamics. The drive for departmental autonomy that is now under way and the decisions taken by the Constituent Assembly entail structural reforms that will have multiple impacts and could take several years to implement. To support a process of this magnitude more effectively, this country strategy covers the remainder of the presidential term (2008-2010) and has been designed with sufficient flexibility that it can adapt to the country’s new political and social dynamics. Annex VIII presents a table illustrating a possible operations program for the period 2008-2010 and the inventory of potential future actions.
A. Level of post-debt-forgiveness assistance and the “blend” scenario

4.2 The debt relief through the Fund for Special Operations (FSO) approved by the Bank in 2007 under the MDRI took effect retroactively to 1 January of last year and, as noted above, represents for Bolivia a reduction of US$741 million in principal on its debt to the Bank, and an interest savings of US$307.3 million. The Bank’s approval of debt relief was accompanied by a reform of the mechanism for allocating the Bank’s concessional resources in the form of parallel lending until 2015, involving a blend of FSO and Ordinary Capital (OC) funds. During the transitional period 2007-2008, Bolivia will continue to receive an important concessional element (37%), with an annual allocation of US$74.3 million (30% FSO and 70% OC).

4.3 Toward the end of 2008 the Bank will assess implementation of the FSO debt relief through the MDRI and the concessional financing program approved by the Board of Governors in early 2007. That assessment could provide an opportunity to consult with Bank Governors on the possibility of granting additional financing to Bolivia from OC resources, as the Bolivian authorities have informally requested. Under this scenario, Bolivia could be considered as one of the countries eligible for the Intermediate Financing Facility (IFF). In order to move forward with a proposal of this nature, the Bank would first have to analyze the legal, financial and technical requirements and implications, something that will take time and will depend to a large extent on the outlook for the country’s debt sustainability and the performance of the active portfolio. A detailed projection of approvals of new operations, disbursements, and cash flows is given in Annex IX.

B. Objectives and strategic focus: Central pillars of the country strategy

4.4 Issues related to portfolio execution have been the starting point for the Bank’s support to the government of President Evo Morales. With the new approaches and priorities in the country’s development model, the Bank has deemed it important to analyze the relevance of the outstanding portfolio and its consistency with government objectives. Execution delays and the relatively high number of projects in the portfolio, viewed against the country’s current institutional capacities, justified the effort at rationalizing the portfolio, which began with an initial exercise approved by the Board of Executive Directors in August 2004, and another approved in May 2006.

4.5 Bank activities will respect the guidelines that emerged from the dialogue and consultation process with the national authorities. Achieving a sustainable reduction in poverty will remain the general objective guiding those activities, within the framework of the general objectives identified in the NDP. Given the many and varied kinds of development support that the country needs to reduce the poverty gap, the new strategy calls for closer targeting of the Bank’s activities in Bolivia, which in turn will allow them to be coordinated more effectively with other donors.

4.6 Bank support will focus on four strategic areas, dealing with: (i) the challenges of economic growth, employment and governance: productivity, competitiveness and productive infrastructure as needed to promote balanced and sustained economic growth; (ii) the challenges of improving living conditions: development of the water and sanitation sector and socially productive development; (iii) the
challenge of social inclusion and unity in diversity: **creating opportunities for the majority and development with identity**; and (iv) the challenge of making government action transparent and efficient: **strengthening the State apparatus through institutional development at the national and decentralized level**. In this last area, attention to subnational levels of management could be complemented with institutional strengthening programs to promote consistency and coordination among the different levels of government. The guiding theme of new interventions will be to develop better channels of interaction between the public sector (central government, prefectures and municipalities), civil society, and the productive sector.

4.7 As noted above, the Bank’s country strategy will be of a transitional nature, and will be reviewed once the constitutional referendum process is wrapped up. In this context, and recognizing the effect of debt relief on the availability of new funds, the Bank’s attention during the initial phase of the country strategy cycle will focus on the active portfolio and on working out with the government a clearly delimited field of action. Given the current capacities of the executing agencies, that field of action will concentrate on financing projects relating to road infrastructure, social and productive development, and improving the lives of the poorest. Once the concrete results of the Constituent Assembly are known, particularly as they affect decentralization and the State’s role as economic agent, a second phase of implementing the strategy will be launched, setting out a menu of options in the strategic areas proposed.

1. **Productivity, employment, and productive infrastructure**

4.8 Bolivia faces many challenges relating to productivity, competitiveness and employment. The need to reconcile economic growth with equity must translate into actions to remove obstacles to production and to involve the poor more actively in the process of wealth generation. The central items of this orientation will be to enhance transportation infrastructure and energy availability, and to guarantee the security of assets, in particular in land and housing, while incorporating considerations of gender equity and cultural relevance.

4.9 In principle, Bank support in this area could revolve around two broad lines of action: (i) promoting regional integration and market access by financing upgrades to transportation infrastructure, in particular the road network, which in its current level of development and functionality is the preponderant mode of transportation; and (ii) boosting economic growth and employment generation by improving the productive infrastructure and fostering productivity and competitiveness.

a. **Upgrading the transportation infrastructure**

4.10 Bank support in the transportation sector will be devoted primarily to enhancing efficiency in the use of transport infrastructure, in particular the road network, by promoting modern and sustainable management in terms of upkeep and maintenance, and moving toward cross-country connectivity. To this end, support could focus on: (i) rehabilitating and improving local roads and secondary networks and integrating them into the trunk systems and the continental integration corridors; (ii) highway investments to improve geographic connectivity, with priority to regions of high productive and export potential; (iii) developing institutional and financial
arrangements that will give priority to the upkeep of existing infrastructure; (iv) developing, rehabilitating or upgrading other modes of transport, in conjunction with the roads network, so as to enhance the productivity and competitiveness of the economy; (v) defining the institutional and administrative arrangements best suited to managing the country’s road network efficiently in a context of decentralization; (vi) strengthening the government agencies and entities resulting from the previous measures; and (vii) coordinating sector policies and activities more thoroughly. The programming and preparation of transportation projects will take account of the sector’s institutional framework, its resource absorption capacity, and the need to prioritize interventions carefully against technical criteria and economic returns. The Bank’s support will be provided under a conditional credit line for investment projects (CCLIP).

4.11 In this context, the Bank could assist the country in analyzing the potential environmental impacts of transport projects, recognizing that its ecosystems are fragile and its soils prone to desertification. Among other aspects, with respect to potential Bank-financed projects in road facilities and productive infrastructure: (i) they should figure in territorial or local development plans that have been assessed for their potential environmental, social and cultural impacts; and (ii) each specific project must be covered by a social and environmental feasibility assessment and environmental and social management plans that include specific measures to avoid, mitigate or offset possible impacts on ecosystems, biodiversity, and indigenous communities.

b. **Productive infrastructure and the promotion of productivity and competitiveness**

4.12 The country’s complicated and shifting economic, technological and institutional setting makes competitiveness an issue of the greatest importance for government policies, and calls for combining and redefining geographically the policy for promoting entrepreneurship and the policy for regional and local development. The strategy’s objective is to help consolidate territories with viable and sustainable economies, creating arrangements that will link small farms to dynamic business schemes and will expand nonfarm employment opportunities in those territories. To this end, the strategy proposes that a certain number of target territories be identified within poor regions of the Altiplano and the inter-Andean valleys, from a territorial or local development approach that includes not only agriculture but also rural industries, tourism, handicrafts and services, so as to build into the strategy the option for nonfarm work.

4.13 The design of operations within the strategic framework could require support for strengthening the institutions involved in agricultural development, in the areas of productivity and credit access, through the National Development Finance System (SINAFID). A programmatic approach will be used, insofar as possible.

4.14 The Bank’s new private-sector department (SCF) could help meet financing requirements for medium and large-scale productive undertakings. SCF will continue working with local entities and enterprises, public and private alike, in seeking opportunities to support the country in infrastructure and capital market development,
and more especially in some of the new sectors within its mandate. In the short term, most opportunities are likely to be found in the sectors of agroindustry, manufacturing and capital markets. Loans of this kind have declined as a proportion of total lending, due primarily to changes in the legal and regulatory framework and in the country’s business climate.

2. Social welfare and water and sanitation development

4.15 In its support for implementing the social policy aspects of the NDP, the Bank will give priority to further investment in water and sewer services, and to a program of social welfare and comprehensive community-based development. While standing by its intent to target its activities in the country, the Bank will continue to provide technical support through nonfinancial products and nonreimbursable technical cooperation in those sectors that it supported in the past, such as education and health.

a. Water and sewer services

4.16 Despite advances in coverage over the past five years, Bolivia’s health indicators with respect to water and sewer services are the lowest in the region. Many people, in particular the poor living in rural and periurban areas, have no access to improved drinking water sources or sewer systems. The treatment of wastewater in metropolitan areas is completely inadequate, and this creates unhealthy conditions in areas downstream. Service operators are weak, their operating and financial performance is inefficient, and they do not generate enough revenues to guarantee reliable and sustainable services. The institutional framework for planning and regulation of the sector also needs to be consolidated.

4.17 The government needs a strategic plan to address the infrastructure deficit (which is critical in metropolitan areas) and the financial weakness of the water utilities (EPSAs), and it needs a policy framework for planning and regulation. The overall goal of the strategic plan should be to achieve universal service coverage so as to make a sustainable improvement in living conditions. In coordination with other donors under a sector-wide approach (SWAp), the IDB will continue to support investment projects for expanding water and sewer service to the poor, especially in periurban and rural areas, as part of its strategy of inclusion and community development. It will also support projects for achieving the MDG environmental targets relating to sewage and wastewater treatment in the country’s largest metropolitan areas (La Paz, Santa Cruz and Cochabamba).

b. Social welfare and community development

4.18 The Bank is supporting implementation of a new intervention model that involves making conditional transfers to rural communities, which individually assume the collective responsibility of improving their social development indicators (for example, vaccination and child nutrition in the health field, primary school enrollment in the education field). The model will be tested in pilot projects in selected communities where poverty rates are high. It includes options such as financing productive projects, social infrastructure and environmental improvements. At the same time it offers options for financing human capacity-building initiatives
and community self-management projects with cultural and territorial identity, as well as initiatives for intersector and interagency coordination and complementarity for improving social and economic conditions in those communities. In January 2007, the Bank approved a US$10 million pilot program that will serve as the basis for a broader program in the future (Social Safety Net Development Program, document PR-3138 of December 2006).

4.19 The Bank could also provide financial support for designing an intervention model for integral community development in urban areas, with an associated pilot program, in which case it would evaluate the feasibility and relevance of a set of projects dealing with the following themes: promotion of community economic initiatives, social and productive infrastructure, environmental improvement, and strengthening human capacities and community self-management.

3. Opportunities for the majority and development with identity

4.20 Bolivian society still has one of the widest gaps between rich and poor, leading to serious problems of exclusion and frustrating people’s efforts to escape poverty. Consistent with the thrust of the NDP, the Bank believes that to lay the foundation for a more equitable society will require measures to broaden opportunities for the majority (which in Bolivia’s case consists largely of people of indigenous origin). To this end, the Bank intends to use various instruments to generate innovative projects that will promote social integration and inclusive growth, with tangible results for all.

4.21 To achieve these goals, it is essential to identify and register that majority, recognizing that a high percentage of such people lack the identity documents needed to pursue any formal productive activity and to qualify for basic services and civil rights (in the country’s poorest areas 55% of people have no birth certificate and 84% have no Identity card). The Bank could thus assist the government’s efforts to modernize the civil registry system.

4.22 Nor can the desired objectives be achieved without addressing the extreme distortions in the labor market with exploitative practices such as indentured labor and debt bondage, as well as forced labor in agriculture and remote rural areas. The Bank could assist the country in designing and implementing a national action plan for the elimination of forced labor.\(^6\)

4.23 A crucial element for achieving inclusive economic growth is to promote financial democracy and the establishment of an “entrepreneurship pact.” Access to financial services remains one of the greatest challenges facing micro and small enterprises, especially in rural areas and for productive activities. Through small projects financed by the Multilateral Investment Fund (MIF) and initiatives such as the Social Entrepreneurship Program (SEP) and support for indigenous entrepreneurs, the Bank will boost its support for microfinance institutions in improving their credit technologies so that they can offer financial services in niches and zones that are now

---

\(^6\) The Ministry of Labor has initiated the project for the Eradication of Servitude, Forced Labor, and Similar Practices under Supreme Decree 29292, which follows the main outline of Convention 169 of the International Labour Organisation (ILO), which is the conceptual and legal touchstone on such issues.
ignored, while helping to broaden the base of grassroots entrepreneurs through training and advisory services.

4.24 Another key element for inclusion of the majority is proper access to basic services and infrastructure (water, sanitation, electricity, urban transportation and rural roads), the lack of which has a direct impact on poverty and exclusion. In this respect, the Bank’s support for social and productive projects will stress the need to reinforce and improve targeting methods so as to extend service coverage to rural municipalities and indigenous communities that are home to the bulk of the most vulnerable population.

4. Institutional strengthening at the national and decentralized level

4.25 The Bank could continue to support the modernization of public administration at the central level, targeting its intervention so as to achieve greater progress in key areas such as government budgetary and financial management, tax and customs administration, and combating corruption. Continuing its cooperation in strengthening the budgetary process, the Bank could support the introduction of multiyear budgeting and management for results in budgetary, financial and assets administration and in procurement. As well, recognizing that exports are important for sustainable growth, the Bank could continue its assistance for strengthening the institutions that facilitate exports, integration and investment promotion. Recognizing the importance of the oil and gas sector for the Bolivian economy, especially in terms of exports, the Bank could also work with the government to identify areas where technical support for institutional and financial development of the sector would facilitate and promote public and private investment.

4.26 As a crosscutting theme in the Bank’s activities with the country, support could also be given to strengthening the legal and institutional framework of organizations responsible for protecting the environment. At the central level, the Bank could also help strengthen risk management capacities for dealing with the impact of natural disasters on the country’s social and productive infrastructure.

4.27 At the decentralized level, the Bank could focus its efforts on two fronts: (i) the development of departmental and municipal institutions as part of the decentralization process; and (ii) strengthening human resource management. This support could be geared to programs for devolving responsibilities and transferring resources so that public investment decisions can be taken at the regional and local levels, thereby reducing interregional inequalities and making management more efficient.

C. Implementation of the country strategy

1. The country’s fiduciary framework

4.28 Bolivia’s management systems still need strengthening, in order to improve the use of public funds and to develop an adequate capacity for designing and implementing policies. In recent years the Bank has supported a number of initiatives that recorded successes but also revealed weaknesses: improving public management is still a work in progress that demands persistence and commitment.
4.29 At the central government level, the most pressing need is to strengthen annual and multiyear budgetary management. Of particular importance here is the operation financed under Sub-account A of the Program to Implement the External Pillar of the Medium-Term Action Plan for Development Effectiveness (PRODEV) for the Program to Develop Management for Results in Bolivia. Modernizing the financial administration will also require the revision and extension of the SIGMA, which is essential for the country’s financial management, and integration of the different expenditure management information systems, including the personnel management system, the procurement system, and the assets administration system.

2. **Country financing parameters (CFPs)**

4.30 During the preparation of this strategy, the Bank revised the conditions in the CFP matrix and it was agreed with the government that the reference framework established in the current matrix provides suitable conditions for implementing IDB projects and achieving the development goals of the NDP. In this context, the Bank could offer financing of up to 100% of the cost of each project, and it could apply the flexibility offered in the new cost financing policy, especially for taxes and duties and, in justified cases, recurrent costs. Annex V contains the CFP matrix.

3. **Instruments to be used in implementing the country strategy**

4.31 The proposed framework of activities is consistent with the Bank’s New Lending Framework (NLF), in that it is geared to achieving greater development effectiveness by promoting management for results, applying a country focus, and using new instruments. In this respect, the Bank is working with the government and with other international partners to structure a SWAp operation for the water and sanitation sector. The Bank has also programmed a CCLIP operation with the country to meet the future needs of the road sector, once the Bolivian Highways Administration (ABC) has strengthened its institutional capacities. As well, the country has expressed interest in continuing the public management improvement program under the second programmatic loan. The Bank has also proposed a programmatic focus for implementing the strategy for territorial development and support to the SINAFID. In this way, a large portion of the Bank’s lending operations with Bolivia would take advantage of these new instruments, through which the Bank seeks to improve the performance of its portfolio in the country and to reduce transaction costs.

4. **Harmonization and coordination with other donors**

   a. **The importance of international cooperation for implementing the NDP**

4.32 Consistent with the increase in public investment, multilateral and bilateral cooperation agencies disbursed more than US$3 billion between 2002 and the first quarter of 2007. Of this amount, 37% represented grants and 63% was divided between commercial and concessional loans. External funding amounted to 9% of GDP as an annual average, constituting an important source of budgetary support and a significant contribution to the growth and development of the Bolivian economy (in monetary terms, international funding in fact exceeded total public investment until 2006).
b. The contribution of international cooperation and its alignment with the NDP

Between 2002 and 2007, the multilateral financial agencies that disbursed the most funds were the Andean Development Corporation (CAF, US$882.1 million), the IDB (US$574 million) and the World Bank (US$481.6 million). Among bilateral donors, the greatest disbursements came from the United States Agency for International Development (USAID, US$314.7 million), the European Union (US$222.4 million) and Germany (US$188.6 million). There is currently a balance of US$2.034 billion in international cooperation funds awaiting disbursement. Those funds are expected to be distributed among the four pillars of the NDP, with a primary focus on support for “Bolivia Productiva” (US$1.460 billion), mainly through credit instruments. Donor coordination produced the sector division of labor presented in Annex X.

c. Harmonization measures taken by the IDB

Recognizing the commitments made by partner countries in the 2005 Paris High-Level Forum on Aid Effectiveness, the Bank is participating actively in the following coordination efforts: (i) with the government, through the “Mechanism for Coordination between the Government of Bolivia and International Cooperation;” (ii) with other donors in the Grupo de Socios para el Desarrollo de Bolivia [Bolivia Development Partners Group] (GruS), to achieve more effective coordination among donors in their interventions and support for the government; and (iii) through the analysis and future preparation of a common standard for the procurement of national goods and services for all donors, with a view to simplifying procedures and reducing transaction costs. The Bank will head the GruS coordination team during the first half of 2008.

The Bank has aligned its work in Bolivia with the priorities and activities of other donors. The strategic areas proposed were disclosed and discussed during presentation of the policy dialogue document in December 2006, with representatives of various agencies accredited in Bolivia (World Bank, IMF, CAF, European Commission, DFID, the embassies of Denmark, France, Italy, Japan, the Netherlands and Sweden, the United Nations, and USAID). Subsequently, views were exchanged with international cooperation agencies in March 2007, with respect to the Bank’s future plans in Bolivia, and possible areas of joint work were identified in the context of the Paris Declaration on harmonization and alignment.

5. Consultations with civil society

Consultations were conducted in a series of meetings held between December 2006 and August 2007 with various representatives of civil society, in which opinions were shared concerning the Policy Dialogue Document prepared by the Bank, and inputs were received for preparing this strategy. The process included individual consultations with private businesses and NGOs. The proposals were discussed with the Civil Society Advisory Council that was recently set up to assist the work of the Bank’s Country Office in Bolivia. This Bank initiative was welcomed by all those consulted. A more detailed description of the process is included in Annex VI.
V. **Risks Associated with Implementing the Country Strategy**

5.1 Internal decisions about the country’s political, social and institutional organization, the mechanisms for applying economic reforms, and to a lesser extent the external setting and natural threats constitute the most important risks in implementing the Bank’s new strategy with the country.

5.2 The risk analysis looked at two angles or channels for classifying the transmission of impacts. On one hand, the analysis identified those risks that condition the country’s political, institutional and economic setting and that *indirectly* affect implementation of the Bank’s country strategy. On the other hand, it grouped those risks that could impact *directly* on its implementation, and for which mitigation measures will be considered in the design of proposed projects and programs. A more detailed analysis of specific risks is found in a study commissioned by the Bank, analyzing risks to the Bolivian economy.\(^7\)

A. **Indirect risks to implementation of the Bank’s country strategy**

5.3 In response to the risk typology that was subsequently developed, the design of the country strategy is sufficiently flexible for the Bank to respond effectively to the dynamic changes occurring in the country’s priority strategic sectors. In addition, the use of flexible instruments, where possible of a programmatic nature, will give the Bank the necessary headroom to address risks as they arise.

5.4 **Risks associated with the social, political and institutional setting.** The complex political situation, which is marked by issues of regional autonomy, control over oil and gas revenues, and land redistribution, is further complicated by uncertainties over the new Constitution, in the context of the Constituent Assembly. The mechanism for adopting the new Constitution will have to be approved and ratified by two successive referendums, according to the law expanding the Constituent Assembly. Those referendums could take several months, and are bound to heighten the uncertainty surrounding the country’s future social and economic organization.

5.5 **Risks associated with the macroeconomic and financial environment.** The fact that the Bolivian economy depends so heavily on the mining and hydrocarbons sectors poses specific challenges and risks to sector policies (see details in Annex VII). Expectations as to the distribution of profits from natural gas are leaving the economy more vulnerable, in circumstances where public sector financing is hostage to the oil and gas price cycle and the volume of production and reserves. In addition, social and regional pressures on public spending and the institutional weakness of the State apparatus, including that of the critical energy sector, pose constraints on the ability of the National Treasury to provide for future development projects and to pursue countercyclical policies as needed. In this respect, rising inflationary pressures could blunt the effectiveness of poverty reduction efforts and programs.

---

5.6 **Risks associated with natural hazards.** Bolivia is exposed to various natural threats: those of the greatest potential impact are earthquakes and the flooding and droughts associated with the El Niño phenomenon. Most of the infrastructure programs now underway in Bolivia are in fact vulnerable to such threats. Generally speaking, the natural environment is deteriorating and people and productive activities alike are highly exposed to natural threats. This fact, together with the lack of solid institutions for managing and reacting to natural phenomena, means that the country is vulnerable to natural disasters, and it increases the risk of physical, social, economic and environmental losses.

B. **Direct risks to implementation of the Bank’s country strategy**

5.7 The strategy would further target the Bank’s activities in Bolivia in areas that have been prioritized to reduce or mitigate the risks associated with their implementation. The essential criteria used for setting priorities in the initial phase of the strategy were: (i) the Bank’s prior experience in each area, and its capacity to add technical value; (ii) the technical background and institutional capacity of the potential executing agencies; and (iii) the portion of funding from other multilateral and bilateral donors earmarked for each sector.

5.8 **Risks associated with improving economic and social infrastructure.** Changes in the Bolivian Highways Administration (ABC) or in the execution of public investment at the national, departmental and municipal levels as part of the decentralization process, could affect the economic and social infrastructure projects associated with the Bank’s country strategy. Consequently, until the outcome of the constitutional process is known, future Bank activities in the road sector (primarily maintenance) will be confined to the basic network. Because roads are the primary responsibility of the central government, through the ABC, that institution’s capacities are being strengthened through the Bank’s support to the Northern Corridor Integration Program approved in 2006, for which the ABC will be the executing agency.

5.9 Natural hazards also increase the risks to Bank projects, particularly road projects, which are one of the pillars of the country strategy. The Bank will seek to ensure that project design incorporates the necessary technical standards and specifications to mitigate the risks associated with natural disasters.

5.10 **Institutional risks at the central and the decentralized levels.** Implementation of the governance pillar of the strategy could be affected by the scope of political and social changes that the drafting of the new Constitution may entail. Amendments to the Constitution, and the consequent adjustments to sector legislation, could affect the quality and efficiency of public management. Depending on the outcome of the departmental autonomy process, there could also be risks to municipal-based welfare programs and water and sanitation projects. As well, the new Constitution could alter the distribution of resources and the form of territorial organization.
CURRENT MACROECONOMIC ASSESSMENT AND OUTLOOK

Recent macrofinancial indicators for Bolivia have performed well. The Bolivian economy has been bolstered by the favorable international setting since 2006: prices for Bolivia’s exports have trended upward, international interest rates are relatively low, external remittances have increased,\(^1\) and the Latin American region is recording sustained rates of economic growth. At the same time, Bolivia has benefited from further and substantial forgiveness of its debt to multilateral and bilateral cooperation agencies.

Macroeconomic policy has also succeeded in absorbing significant surpluses from mining and hydrocarbons production, and has built up record levels of international reserves, while maintaining financial stability, albeit with a moderate outbreak of inflation recently. The country’s fiscal position has improved sharply since 2002, moving from a global deficit of around 9% of GDP in that year to a primary and global surplus of 2% and 3% of GDP, respectively, in 2007. This sound fiscal performance was assisted by the favorable external economic situation, greater domestic activity, improvements in the domestic tax collection system, and changes in the taxation and ownership structure of basic enterprises, mainly in the oil and gas sector.

Economic growth accelerated to 4.6% in 2007, with 2008 growth projected at between 5.5% and 6.8%, accompanied by a steady decline in the open unemployment rate to 5.1% in 2006. Rising levels of economic activity and aggregate demand were coupled with greater pressures on the price structure, with the annualized rate of consumer price inflation climbing from 5.0% at end-2006 to 17.3% in June 2007. The external sector has been robust, with the balance of payments recording a current account surplus of 12% of GDP in 2006, and 14% of GDP in 2007, due mainly to record prices for the basket of exported goods, whose value rose to nearly US$5.5 million in 2007.\(^2\)

Stronger economic growth has been accompanied by greater inflationary pressure, mainly from the second half of 2007 onward. Annualized inflation has continued to climb, closing 2007 at 11.7%, and June 2008 at 17.3%. Rising prices have been felt most severely in foods and beverages. As the first half of 2008 ended, these had increased at an annual rate of 31.6%, accounting for some 80% of the total inflation rate. According to the Central Bank of Bolivia, the fresh outbreak of inflation relates primarily to more imported inflation from steadily rising international prices for Bolivia’s food and energy commodity imports. Other factors to consider would be greater inflationary expectations and more and more pressure being put on aggregate demand by robust private consumption in a setting of supply constraints on farm produce as a consequence of climatological phenomena.

---


\(^2\) Between 1984 and 2003, the average annual ratio of exports to GDP never exceeded 20%. In fact, exports have more than tripled in the last seven years. See technical note on Trade and Integration, prepared for the Policy Dialogue Document by Paolo Giordano, Christian Volpe Martincus, Luiz Villela, Erick Zeballos and Adriana Suarez (INT/ITD), IDB 2006.
Recently, the economic policy response of the monetary authorities has favored the ongoing use of open market operations and a higher rate of appreciation of the Boliviano, to limit the expansive effects on monetary aggregates of the positive external shock and remonetization of the financial system. In a context of gradually slowing global growth, greater depreciation in trading partners, and continuing fiscal austerity, the authorities expect inflation to decline gradually to around 12% at end-2008, and out of the double digits in 2009.

Despite appreciation in response to the positive shock in the current account and international inflation, the real exchange rate has remained at a relatively depreciated level when viewed against historic averages and the rates observed in some of the country’s principal regional trading partners. This has helped protect the competitiveness of nontraditional exports. Official international reserves have risen steadily, together with progressive dedollarization of the financial system: 71% of deposits and 83% of loans are denominated in dollars: this represents a factor of vulnerability in the broader context of uncertainty over the business climate and the political decisions that will emerge from the Constituent Assembly.

Foreign direct investment (FDI) represented approximately 1.2% of GDP in 2007, down from 2.4% of GDP in 2006. Private investment has been dampened by the intense social and political conflicts of recent years, changes in the Hydrocarbons Law, the reversal of privatizations and the State’s reentry into certain activities (in particular hydrocarbons and

---

3 According to the Central Bank of Bolivia (BCB), the average real exchange rate for the period 1990-2006 was around 25% higher than the current level, producing a significant margin of competitiveness, particularly for nontraditional exports. See BCB (2007), “Tipos de cambio y cotizaciones de monedas,” https://www.bcb.gov.bo/sitio/estadisticas.php?n2=0&n3=0&n4=0&pi=t3p7a2
telecommunications): private investment flows have been well below the levels recorded in the 1990s. For the future, uncertainty over the changes that may emerge from the Constituent Assembly (in particular the legal framework governing the extractive industries) and the announcement that Bolivia will withdraw from the International Centre for Settlement of Investment Disputes (ICSID) could exacerbate doubts about the environment of certainty as to the law offered by the country, and have a further impact on FDI and the business climate in general. By contrast, budgeted public investment rose by some 33% in 2007, to 10.3% of GDP. A breakdown of that investment shows that it is concentrated primarily in infrastructure (51%), followed by social investment (25%), production support (18%) and minor extractive sectors (6.4%). 34% of public investment was financed externally, 23% of it through foreign loans.\(^4\)

The country’s total public debt has fallen sharply from 74% of GDP in 2005 to 34% currently (US$12.8 billion). In net present value (NPV) terms, the debt now stands at 30% of GDP, and is only 17% of GDP when government deposits in the financial system are factored in. Actions taken under the Multilateral Debt Relief Initiative (MDRI) have played a particularly important role here, reducing Bolivia’s debt by nearly 25% of GDP. In 2006 the IMF and the World Bank reduced Bolivia’s external debt by some US$1.7 billion. At the beginning of 2007, the IDB granted additional debt relief of US$741 million in principal and US$307.3 million in interest, bringing the current external public debt down almost to 20% of 2006 GDP.\(^5\) Bolivia’s domestic public debt, on the other hand, has been growing since 1994. This very positive trend in the country’s solvency and liquidity indicators has left them well below the sustainability risk thresholds established for the Heavily Indebted Poor Countries (HIPC) Initiative,\(^6\) and under a base-case macroeconomic policy scenario they are expected to decline further in coming years.

The conclusion that Bolivia’s prospects for fiscal and debt sustainability have improved significantly is backed by an independent analysis of the performance of oil and gas revenues, the likely mechanism and dynamics of their distribution (either for constituting a


\(^6\) In this connection, the World Bank, the IMF and the IDB acted jointly to channel technical assistance and supplementary funding to the country through institutional mechanisms created to enable the successive rounds under HIPC Initiatives I and II.
stabilization fund or for accelerating public expenditure and investment), and potential public expenditure and savings paths over the period 2006-2015.\footnote{For further technical details and the result of simulations, see Navajas, Fernando, Daniel Artana, Juan Luis Bour and Marcelo Catena (2007), “Bolivia: Tópicos Marco-Fiscales Seleccionados y Perspectivas de Sostenibilidad Fiscal,” IDB.}

The simulations conducted during that independent analysis show net public debt in GDP terms falling by nearly one-half from the level at the beginning of 2006, indicating a low risk of debt service problems. For a combined adverse shock in all exogenous variables used in the exercise (oil prices, interest rates, real exchange rate and growth rate, with a probability of 5%), the debt path as a proportion of GDP tends to rise by around five percentage points, converging at 40% of GDP, due primarily to uncertainties over oil prices. The more problematic shocks, in terms of long-term fiscal sustainability, relate to a scenario where public expenditure rises systematically, or faster than revenues, or where gas exports to Argentina fall short of rising commitments (Chart 1.5). These assessments of the risks to the country’s debt sustainability are compatible with the results of the IMF exercise conducted in 2006-2007,\footnote{IMF (2006), “Bolivia: 2006 Article IV Consultation—Staff Report; Staff Statement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Bolivia,” Country Report No.06/270, July.} which suggest that debt ratios would remain within the limits of sustainability over the long term even under an alternative scenario of lower oil prices.
The Bank classified Bolivia as having a low risk of debt distress in the context of the proposal for implementing the Debt Sustainability Framework and Enhanced Performance-based Allocation System.\textsuperscript{9}

In general terms, the favorable development of the country’s solvency and liquidity indicators puts it well below the sustainability thresholds established under the Heavily Indebted Poor Countries (HIPC) initiative for countries with average institutional performance, like Bolivia. However, the Bolivian economy’s dependence on external conditions, the difficulty of sustaining recent levels of growth, and less fiscal discipline observed in the last two years represent major risks for public debt sustainability.

In short, to sustain a high level of equitable growth in Bolivia within a framework of macroeconomic stability and debt sustainability, it will be particularly important to mitigate further the factors of domestic risk, such as growing expenditure pressures in the context of fiscal decentralization, institutional weaknesses and problems in public management, the still-high level of dollarization in the financial system, and the uncertainties and costs associated with the eroding business climate’s ability to attract private investment and create jobs. Current levels of domestic investment, and more importantly foreign investment, would have to rise to achieve the investment and growth forecasts in the NDP. In particular, the country’s reputation as a reliable energy supply and the commitments it has assumed with respect to the export and industrialization of gas will require significant investments in this sector. While the short-term risks for oil and gas are less than those facing the mining sector (thanks to mechanisms for indexing the price of gas to baskets of fuels), there are still

risks associated with fluctuating international demand. Consequently, and in light of current projections, the management of windfall revenues through a stabilization fund is a crucial issue for fiscal policy.\textsuperscript{10}

\textsuperscript{10} The NDP contemplates a fund to receive windfall oil revenues. The Ministry of Development Planning in fact recently proposed earmarking surplus revenues for a Stabilization and Development Fund, as a mechanism for dealing with temporary shocks. However, the authorities have yet to analyze this proposal.
## NDP: Progress Toward the Millennium Development Goals by 2015

<table>
<thead>
<tr>
<th>Goals</th>
<th>Indicators</th>
<th>Projection 2015</th>
<th>MDG 2015</th>
<th>Compliance by 2015</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1. Eradicate extreme poverty and hunger</strong></td>
<td>1. Incidence of extreme poverty</td>
<td>22.3</td>
<td>24.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>1. Prevalence of malnutrition among children under 3 years</td>
<td>0.0</td>
<td>19</td>
<td>✓</td>
</tr>
<tr>
<td><strong>2. Achieve universal primary education</strong></td>
<td>1. Net enrollment ratio in primary school</td>
<td>95.4</td>
<td>100</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>2. Grade 8 completion rate</td>
<td>90.0</td>
<td>100</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>3. Illiteracy rate ages 15 to 44</td>
<td>2.2</td>
<td>0.0</td>
<td>X</td>
</tr>
<tr>
<td><strong>3. Promote gender equality and empower women</strong></td>
<td>1. Gender gap among pupils completing grade 8</td>
<td>0.0</td>
<td>0.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>2. Gender gap among students completing fourth year of secondary school</td>
<td>0.0</td>
<td>0.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>3. Gender gap in the 15-44 years illiteracy rate</td>
<td>2.2</td>
<td>0.0</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>4. Proportion of women in paid employment in the nonfarm sector</td>
<td>50%</td>
<td>50%</td>
<td>✓</td>
</tr>
<tr>
<td><strong>4. Reduce child mortality</strong></td>
<td>1. Child mortality rate per 1000 live births</td>
<td>30.0</td>
<td>30.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>2. Pentavalent vaccination rate of infants under one year</td>
<td>85.0</td>
<td>95.0</td>
<td>X</td>
</tr>
<tr>
<td><strong>5. Improve maternal health</strong></td>
<td>1. Maternal mortality rate per 100,000 live births</td>
<td>104.0</td>
<td>104.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>2. Institutionalized child birth rate</td>
<td>70.0</td>
<td>70.0</td>
<td>✓</td>
</tr>
<tr>
<td><strong>6. Combat HIV/AIDS, malaria and other diseases</strong></td>
<td>1. AIDS prevalence (cases per million)</td>
<td>13.0</td>
<td>13.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>1. Percentage of municipios with a Chagas infestation rate greater than 3%</td>
<td>0.0</td>
<td>0.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>2. Malaria parasite index per 1000 inhabitants</td>
<td>2.0</td>
<td>2.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>3. TB cure rate (% of notifications)</td>
<td>85.0</td>
<td>95.0</td>
<td>X</td>
</tr>
<tr>
<td><strong>7. Ensure environmental sustainability</strong></td>
<td>1. Drinking water coverage (% population)</td>
<td>82.0</td>
<td>78.5</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>1. Sanitation coverage (% population)</td>
<td>65.0</td>
<td>64.0</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>1. Proportion of land area covered by forest</td>
<td>47.5</td>
<td>Maintain</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>2. Percentage of land area in protected areas</td>
<td>17.3</td>
<td>Maintain</td>
<td>✓</td>
</tr>
<tr>
<td></td>
<td>3. Consumption of chlorofluorocarbons (CFC), tons per year</td>
<td>0.0</td>
<td>0.0</td>
<td>✓</td>
</tr>
</tbody>
</table>

**Source:** Comité Interinstitucional de las Metas del Milenio (CIMDM) (2006), Cuarto Informe sobre el Progreso de los Objetivos de Desarrollo del Milenio Asociados al Desarrollo Humano, Bolivia, November.
THE NATIONAL DEVELOPMENT PLAN AND THE COUNTRY’S MAIN DEVELOPMENT CHALLENGES

A. Deepening the foundations for growth and employment: the challenge of productivity

The low growth and economic vulnerability that have characterized Bolivia for more than 50 years\(^1\) led the government to adopt the *Bolivia Productiva* ("Productive Bolivia") pillar. Its objective is to bring about a radical decrease in poverty levels, by linking productive issues with social challenges. Consequently, income redistribution and employment generation are dominant items on the government agenda. That agenda stresses the role of the State as a key player in development, in a system in which decisions on the allocation of public funds involve not only social services, basic infrastructure and regulation, but also productive processes.

With this productive pillar, the NDP seeks to support strategic sectors that can generate surpluses and jobs. It gives priority in this respect to the hydrocarbons sector, mining, transportation, tourism, housing and manufacturing (urban and rural SMEs), and calls for a productive matrix of sectors as the mechanism for guiding development. This model highlights the importance of infrastructure development for production and productive services.

The proposed changes will require a thorough overhaul of various institutional aspects, however. First, the Ministry of Development Planning, which has a central role in implementing the NDP, needs institutional strengthening. In addition, the National Development Finance System (SINAFID) must have a coherent normative and organizational design. Finally, because the NDP calls for major action in the hydrocarbons and mining sectors, primarily through State-owned enterprises (YPFB and COMIBOL), both the ministries and the enterprises involved require institutional strengthening and modernization.

B. Strengthening the foundations for a more equitable society: the challenge of social and cultural inclusion

The NDP sets the eradication of poverty and exclusion as its principal goal. Through the *Bolivia Digna* ("Dignified Bolivia") pillar, the government is seeking to create a new State fabric comprising peoples, communities and regions in order to arrive at a socially fair, multicultural and community-based State that guarantees access to basic services and employment. Constructing this fabric entails the generation of incomes in such sectors as agriculture, manufacturing, tourism and construction. In addition, there is the challenge of a

\(^1\) Between 1950 and 2000, annual real growth per capita in Bolivia was -0.02%. Over that same period, cumulative growth was -1%. Throughout this time, growth downturns outweighed upswings, with the result that net output per capita declined. See Harvard University (2005) “Bolivia: A Country Study on Economic Growth and Development,” Kennedy School of Government, Cambridge, Massachusetts, November.
new matrix for rationalizing public investment, ensuring equity in the distribution of revenues by giving State intervention precedence over the workings of the market, based on solidarity, community and social responsibility, and the application of “territorially oriented” intervention principles focused in particular on the poorest and most depressed areas in order to have direct impacts on marginalized, especially indigenous, people.

This pillar of the NDP stresses human capital accumulation, through education and health policies that will place great emphasis on intercultural and community aspects, in both rural and urban areas. It also emphasizes the need for mechanisms to restore traditional values and codes in the health and education sectors, and in the justice system and citizen security, calling at the same time for major investments in basic sanitation and housing to raise living standards for the most vulnerable groups.

Because the planned interventions are of an integrated nature under a “territorial” scheme, they involve some important institutional considerations. For example, there must be articulation between the levels of government for implementing decentralized social measures (on which the NDP is silent), and the capacity for statistical analysis and design of monitoring and evaluation systems must be strengthened to ensure that public investments are used efficiently and will have the desired impact on living standards.

C. Enhancing the institutional capacity of the State as an agent of development: the challenge of governance

Bolivia has been engaged in institutional and policy reforms for more than a decade, with only mixed results. On one hand, despite political instability, the democratic system is now much healthier. On the other hand, progress with institutional reforms has been slow, and there is little to show in terms of increasing efficiency at the local and national levels of government, or in developing a career civil service. The tasks of combating corruption and building an efficient and transparent judicial system have yet to be addressed.

To reverse this situation, the government seeks, through the NDP’s Bolivía Democrática (“Democratic Bolivia”) pillar, to promote a new role for the State in the political, institutional, social and economic spheres. It calls for an institutional organization that will ensure the equitable distribution of economic surpluses. In order to “dismantle State colonialism,” characterized by ethnic domination and exclusion, the political strategy is based on re-founding the country through the Constituent Assembly, building a new multicultural institutional framework, and creating a plurinational State for the equitable redistribution of economic surpluses.

Implementing this strategy raises a number of important issues that must be addressed. These include improving human resource management in the public sector, at both the regional and national levels, as well as strengthening management information systems and tools and transferring responsibilities in ways that respect the particular features of each region and prefecture, given their heterogeneity.
D. Efficient exploitation of the country’s nonrenewable resources: the challenge of sustainability and sound public investment

As is clear from the above, the pillars of the NDP, taken together, represent an ambitious program of public investment amounting to some US$7 billion between 2006 and 2010. Yet this program faces a number of institutional and political challenges that must be addressed. First, on the macroeconomic front, policies for making efficient use of these resources in order to achieve and sustain high rates of economic growth must be combined with mechanisms of fiscal sustainability that will ensure stability both in investments and in expenditures.

Second, on the institutional front, steps are still needed to achieve better coordination between the national government and the prefectures and municipios to boost investment and improve its quality. The decentralization of expenditure and investment is a central theme in the debate over reform of the State, and is now being discussed in the Constituent Assembly. The arrangements adopted for regional autonomy will have a direct effect on the quality and effectiveness of public investment and its impact on the poorest and most vulnerable groups. Also, the way expenditure and investments are financed will be crucial to the fiscal sustainability of this new institutional structure.

Third, the fact that the prefectures and municipios are dependent on revenues from natural resources, especially oil and gas, undermines the principle of fiscal co-responsibility and reduces the authorities’ accountability vis-à-vis taxpayers, thereby reinforcing the inclination of society to “live off its assets.” This poses the challenge of achieving a consensus that will relieve the current asymmetries in fiscal pressure. Those asymmetries reflect the fact that royalties and transfers are distributed among departments without regard to their expenditure responsibilities and capacities, or their own tax effort. Moreover, this financing system is hostage to the oil and gas price cycle, and to the volumes of production and reserves.2

Finally, the restructuring of the State apparatus needed to carry out the planned reforms and investments will demand a high degree of experience and human capital. Yet the policies followed to date (which have left the civil service poorly paid and staffed with political appointees) could pose serious constraints on the ambitious activities proposed under all pillars of the NDP, and thereby compromise the ultimate goal of reducing poverty and increasing equity. Consequently, fiscal sustainability and sound investment decisions will depend on changes in the arrangements for decentralization and autonomy, a complex process that will take time.

2 Zapata (2007).
A. Principal contributions

One of the Bank's most important contributions during this period was its support for strengthening the fiscal situation and preserving economic stability, supplemented by FSO debt relief under the MDRI, in which Bolivia saw the principal of its debt to the Bank reduced by US$741 million, with interest savings of US$307.3 million.

IDD support to Bolivia during the fiscal crisis of 2002-2004

It is important to note that the Bank gave significant support to Bolivia in restoring its macroeconomic balances without insisting on the condition (required for eligibility under HIPC II) that Bolivia have in place a new Poverty Reduction Strategy. The sharp political and social conflict that gripped the country from 2000 caused public spending to run out of control, producing a fiscal deficit of 8.8% of GDP in 2002, and the government was obliged to take steps to reverse that deficit. The situation was made worse by rapidly rising pension outlays associated with the reform process. In these circumstances, the Bank cooperated to make the pension administration more efficient and bring it into line with the capacity of the national Treasury. In 2003, two sector loans were approved, one of which drew on the FSO reserve fund, which allowed for significant flexibility and swift approval. In addition, through such operations as the National Customs Reform and Modernization Program (1056/SF-BO) and the Institutional Strengthening Program for the National Taxation Service (1043/SF-BO) the Bank helped generate greater public revenues. At the same time, the Fiscal Sustainability Support Program (1127/SF-BO, 1128/SF-BO and ATN/SF-8333-BO) helped to reduce the record fiscal deficit of 2002, caused in large part by spending on pensions. In the following years, through its support for exerting greater control over public expenditure, austerity measures and effective programs for reducing tax evasion and pension fraud, the Bank helped to reduce the overall fiscal deficit and the pension deficit in particular (which declined from 4.9% of GDP in 2002 to 3.7% in 2006).

The Bank support also included specific contributions in areas of high social impact such as education and health. In particular, the Bank, in conjunction with the World Bank, supported actions that raised the gross primary school enrollment rate to nearly 100% and the completion rate to over 60%, and reduced the gap between urban and rural enrollment and completion rates. In the health sector, the Bank also helped improve the organization, coverage and quality of health services, and contributed to major advances in eradicating Chagas disease and implementing an epidemiological surveillance system.

The Bank has also helped to enhance Bolivia's competitiveness through construction and rehabilitation of a significant portion of its highway network, thereby reducing average trip times and transport costs. Over the last five years, projects have included the construction or

---

1 Because the previous strategy covered less than one complete government term, the following analysis of Bank activities goes beyond those contained in the strategy, and embraces the period from 2000 to the end of 2006. However, for analytical purposes, the points of reference are those of the last country strategy with Bolivia, covering the years 2004-2007. That document is available at http://re1/n-od1/od1.asp?cuerpo=TablaRoja.asp&IdNota=1742.
upgrade of the Santa Cruz-Puerto Suárez integration corridor, the Cotapata-Santa Bárbara and Río Seco-Desaguadero sections of the Beni-La Paz corridor, and the Ventilla-Tarapaya Highway, with a total of 174 km of new roads constructed and 927 km upgraded or paved (in addition to highway patrol and toll stations). In addition, the Bank has achieved good results in the microfinance sector, especially in rural areas and for productive activities, through MIF and technical cooperation projects. With this support, lending technologies for offering financial services in unserviced areas have been improved, new financial products have been designed and implemented for microenterprises and rural producers, and irrigation management tools have been developed.

B. Portfolio performance

Through the portfolio management rationalization exercises conducted in 2004 and 2006, the Bank cooperated with the national authorities in restructuring the loan portfolio and aligning it with government priorities, at a time of political and institutional volatility. Particularly noteworthy is the speed with which the 2006 rationalization was agreed with the government of President Evo Morales; that exercise cut the size of the active portfolio almost by half and focused it in priority areas of high social impact and execution capacity, where the Bank’s value added is complementary to the significant international cooperation the country receives from other sources.

The climate of instability prevailing in the country has also led to delays in project eligibility and disbursements, due primarily to institutional or staffing changes in the executing agencies. Annual disbursements as a percentage of the active portfolio have been on a downward trend (except for 2003), falling below 7% at the end of 2006 (see Annex II). In absolute terms, disbursements totaled US$557.6 million between 2002 and 2006, with some year-to-year discrepancies, although distribution by strategic area was relatively constant.

In the course of the last five years the Bank approved a total of US$594.3 million in loans to the public sector. An analysis of distribution by strategic area of the BCP approved in 2004 shows that lending focused on productivity and competitiveness, primarily through investment loans (see Charts 3.1 and 3.2), mainly for the road sector. Two sector loans were also approved in 2003 and, as discussed below, these sharply influenced disbursements in that year.

---


3 US$200 million was disbursed in 2003 alone, reflecting primarily the approval of sector loans.

4 Fiscal Sustainability Program (1127/SF-BO) and Competitiveness Program (1519/SF-BO), the latter of which included US$50 million from the FSO Emergency Reserve Fund.
A total of US$151 million was approved in loans to the private sector, concentrated primarily in 2002, with two operations: Red de Telecomunicaciones Redibol and Transredes S.A. However, loans of this kind have declined as a proportion of total lending (see Charts 3.1 and 3.2), due primarily to changes in the legal and regulatory framework and in the country's business climate.\(^5\)

Other Bank products of importance in Bolivia are TCs, Small Projects, and MIF operations.\(^6\) Between 2002 and 2006, the Bank approved a total of US$15.4 million in TCs and small projects, on a rising annual curve. Access to nonreimbursable funding has increased: 30% of TCs (for a total of 57 operations) have provided direct support for potential loan operations, with the remainder earmarked generally for opportunities for the majority and for institutional development and fiscal management. Small projects have focused mainly on microenterprises and small businesses, targeted at women, indigenous people and rural producers through the Social Entrepreneurship Program (SEP). During this time, seven TCs were approved for emergency support, primarily for El Niño-related disasters. The MIF has concentrated its support on providing credit to small producers and strengthening entrepreneurial capacity, through 22 projects totaling US$14.6 million over the last five years.

\(^5\) In fact, Transredes S.A. (a privatized gas transporter) was affected directly by the recent law nationalizing the sector. With respect to operations in execution, in 2005 the Bolivian government began the process of withdrawing from the French company Suez the concession for the Aguas del Illimani project (1151/OC-BO), and its contract was terminated at the beginning of 2007. The REDIBOL loan fell into arrears: repayment was accelerated in September 2005, and the contract terminated.

\(^6\) TC, SEP and MIF operations together amounted on average to 5% of loan approvals for Bolivia over the last five years, but the ratio was 20% in 2005.
The portfolio reviews conducted during this time sparked measures to improve the execution of operations. Of particular note are the following: (i) *strengthening the execution and management capacities of executing agencies*: executing units were given training in institutional, normative and operational mechanisms for proper administration and supervision of operations; (ii) *project reformulation and resource reallocation*: two portfolio rationalization exercises were conducted, as mentioned above, with a view to enhancing the performance of the portfolio and targeting resources more effectively; (iii) *fostering dialogue for the political feasibility of operations*: channels of dialogue were kept open to facilitate approval and ratification of operations by the legislature; (iv) *better coordination for the achievement of development goals*: further progress was made in defining outcome indicators, in conjunction with other donors, to improve coordination in the preparation, financing and monitoring of projects; (v) *procurement*: training workshops were held and executing agencies were provided with manuals and procedures for procurement transactions below the established thresholds; (vi) *financial and accounting aspects*: project audits were encouraged and supported in order to ensure that timely audited financial statements were produced; and (vii) *coordination between IDB and the Vice Ministry of Public Investment and External Financing (VIPFE)*: there was regular and productive dialogue with the VIPFE to identify any problems promptly and to move swiftly and effectively to resolve them.

C. Experience with implementation of the previous strategy and lessons learned

This period produced some lessons that should inform and guide Bank activities in Bolivia over the short and medium term. Those lessons may be of interest in countries where the portfolio situation and the political and economic environment are similar to those that Bolivia has faced in recent years, as well as countries that benefit from broad international cooperation. The following paragraphs discuss the most significant lessons relating to formulation of the new strategy, the design of new operations, and administration of the portfolio.

**Targeting of the strategy.** The Bank will have to reconcile its own funding restrictions with Bolivia's limited institutional capacity to take on new commitments, and the need for greater targeting and selectivity in the projects to be financed. As one of the main sources of concessional external financing, and faced with multiple demands, the Bank should insist that its support be focused on key themes within each strategic area, and it should follow the government's lead in promoting effective coordination with other donors.

**The institutional factor.** Project performance and the achievement of development objectives have been constrained by the recognized weaknesses of the executing agencies as well as by constant changes not only in those institutions themselves but also in the institutional setting in which the projects have been pursued during this time. Future lending scenarios should be based on a more detailed analysis of the risks associated with the
institutional setting, particularly if programs depend on complex and socially sensitive reforms (including the approval of legislation).\footnote{This was the case with the National Irrigation Program (964/SF-BO): its water management component assumed approval of the Water Law, but in fact promulgation of that law was postponed indefinitely (because it was a socially sensitive issue), and the project had to be restructured twice. Similarly, the Sustainable Tourism Development Project (1098/SF-BO) has been restructured, because one of its components (regulation and promotion of sustainable tourism) depended on a certification system that was never established.}

**Concept and design of new projects.** Some projects set objectives and goals that were too ambitious, in terms both of their outcomes and of their estimated implementation times. One way to mitigate this problem would be to opt for smaller and more targeted operations that are simpler in their design, execution and administration. The Bank's New Lending Framework enhances the Bank's capacity to design more flexible operations that can respond swiftly to sudden and unexpected changes of context.

**Harmonization and coordination.** Project preparation and execution can place a heavy burden on the executing agency when many sources of financing are involved. It is important for funding agencies to harmonize not only their goals but also their rules and procedures. In particular, generalized use of the performance-based disbursement procedure could enhance overall project effectiveness and respect for procedures.

**D. Bank disbursements and financial flows with the country**
### Flow of Bank Funds with Bolivia (in US$ millions)

<table>
<thead>
<tr>
<th></th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>a. Loan disbursements</td>
<td>84.6</td>
<td>99.5</td>
<td>195.6</td>
<td>92.4</td>
<td>111.3</td>
<td>59.7</td>
</tr>
<tr>
<td>a.1 Investment</td>
<td>84.5</td>
<td>79.3</td>
<td>65.6</td>
<td>70.3</td>
<td>86.8</td>
<td>59.6</td>
</tr>
<tr>
<td>a.2 Sectoral</td>
<td>0.1</td>
<td>20.2</td>
<td>130.0*</td>
<td></td>
<td>22.2</td>
<td>24.5</td>
</tr>
<tr>
<td>b. Repayments (principal)</td>
<td>60.0</td>
<td>66.9</td>
<td>83.1</td>
<td>83.7</td>
<td>75.7</td>
<td>73.9</td>
</tr>
<tr>
<td>b.1 FSO</td>
<td>12.2</td>
<td>6.1</td>
<td>15.5</td>
<td>13.1</td>
<td>14.2</td>
<td>18.9</td>
</tr>
<tr>
<td>b.2 OC</td>
<td>46.5</td>
<td>59.6</td>
<td>66.4</td>
<td>69.3</td>
<td>60.8</td>
<td>54.7</td>
</tr>
<tr>
<td>b.3 MDRI debt relief (FSO)</td>
<td>-9.0</td>
<td>-16.9</td>
<td>-11.3</td>
<td>-11.0</td>
<td>-13.0</td>
<td>-16.4</td>
</tr>
<tr>
<td>c. Net flow of lending (a-b)</td>
<td>24.6</td>
<td>32.6</td>
<td>112.5</td>
<td>8.8</td>
<td>35.6</td>
<td>-14.2</td>
</tr>
<tr>
<td>d. Interest and fees</td>
<td>43.2</td>
<td>33.9</td>
<td>38.7</td>
<td>34.2</td>
<td>31.2</td>
<td>28.6</td>
</tr>
<tr>
<td>d.1 MDRI II relief</td>
<td>-6.9</td>
<td>-11.8</td>
<td>-7.4</td>
<td>-7.9</td>
<td>-7.6</td>
<td>-8.2</td>
</tr>
<tr>
<td>e. Net cash flow (c-d)</td>
<td>-18.5</td>
<td>-12.2</td>
<td>73.8</td>
<td>-25.4</td>
<td>4.4</td>
<td>-42.8</td>
</tr>
</tbody>
</table>

Includes convertible and nonconvertible funds from FSO, OC and others, excluding PRI.

* Includes US$50 million from the FSO Emergency Reserve Fund
### Matrix of Country Financing Parameters (CFPs)

<table>
<thead>
<tr>
<th>Item</th>
<th>Parameter</th>
<th>Explanations/Restrictions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Financing matrix: Maximum amount of project cost that the Bank loan can finance</td>
<td>Up to 100%</td>
<td>(Bolivia has no program with the IMF, and the Poverty Reduction Strategy dates from a previous government). The medium-term outlook for fiscal and debt sustainability suggests that the effort to consolidate and limit nonconcessional borrowing should be maintained (recalling that there is now greater fiscal room). In specific projects where relieving the burden on the national Treasury would enhance the prospect of achieving the objectives, the local counterpart requirement could be reduced to zero.</td>
</tr>
<tr>
<td>2. Recurrent costs: Limits on the financing of recurrent costs</td>
<td>No specific limits</td>
<td>Consistent with the government's prudent fiscal policy, the Bank could finance recurrent costs provided the project in question is compatible with the country's medium and long-term fiscal sustainability. Recurrent cost financing will be reviewed project by project, taking into account such factors as: (i) their normal source of financing, recognizing that substitute financing from the bank could jeopardize the executing agency's capacity to negotiate future budget allocations to cover those costs once the project is completed; (ii) in principle, recurrent costs should not be financed if they would normally be covered from the revenues of departments, municipios or decentralized agencies; (iii) it would be preferable to finance only incremental recurrent costs, and only for a limited time; and (iv) the percentage to be financed should decline each year as the counterpart portion increases. If the Bank is to finance recurrent costs, whatever their nature, it must have a firm commitment from the Ministry of Finance or the subnational government or decentralized entity concerned that it will make provision for those costs in future budgets, taking into account the overall fiscal position and outlook.</td>
</tr>
<tr>
<td>3. Local costs: Restrictions applicable to the financing of local costs</td>
<td>None</td>
<td>The Bank makes no distinction between financing the cost of inputs produced in the country and those that are imported (application of procurement rules).</td>
</tr>
<tr>
<td>4. Taxes and duties: Restrictions on the financing of taxes and duties</td>
<td>None</td>
<td>The Bank may finance the cost of taxes and duties related to a project if it considers them reasonable and nondiscriminatory.</td>
</tr>
</tbody>
</table>

---

1 For each item, a ceiling is set and it may not be raised. A specific analysis of each project will determine whether the full ceiling may be used.

2 The recommendations indicated in the explanations for each parameter may result in restrictions on use of the full ceiling indicated.

3 Other expenses (e.g. land, buildings) are not regulated by this framework and a decision will be made in each case, consistent with established policy, as to whether they can be financed within the loan amount.
THE CONSULTATION PROCESS

Consultations with civil society for preparing the Country Strategy with Bolivia were conducted in two stages, in December 2006 and in August 2007, taking as a basis the Policy Dialogue Document prepared for this purpose by the Bank.

The first stage consisted of two meetings that were held on 20 December 2006 with representatives of civil society and the private sector. In those meetings, we informed participants that the Bank had conducted a special mission to discuss the Policy Dialogue Document with the government as part of the process of preparing our strategy with the country, and we presented the most significant outcomes from the discussion with the government held on 30 November 2006, as well as issues relating to rationalization of our portfolio and operational programming for the 2007 fiscal year.

The meeting with private business people included Eduardo Peinado, President of the National Chamber of Industry; Alcides Casas, Manager of the National Chamber of Commerce; Tania Eterovic, La Paz representative of the Santa Cruz Chamber of Industry, Commerce, Tourism and Services; and Luis Salinas, Manager of the Bolivian Construction Chamber. Participants welcomed the Bank's initiative to include them in the consultation process for preparing the strategy. Their comments dealt primarily with the Bank's ability to work with private firms, mechanisms to access financing through the Private Sector Department, and the importance of promoting private investment as a fundamental aspect for development, growth and job creation.

The meeting with civil society representatives was attended by Patricia Miranda (Fundación Jubileo), Edwin Pereira (Federation of Municipal Associations), Armando Cardozo (National Academy of Sciences), Alfonso Alvésteugui of the Child Survival Coordination Program (PROCOSI), Daniel Cáceres (“Mecanismo de Control Social”), John Pereyra and Julio Alvarado (Bolivian Association for Economic Policy on Globalization). Mention was made at that meeting of the importance of socializing information, the consultation process, and the contributions of civil society. Participants welcomed the initiative to hold the meeting. Their comments related primarily to the Bank's ability to work with institutions of civil society, and to the mechanisms whereby entities that are not directly under the central government could access financing.

The second round of consultation took place at the first regular meeting of the Civil Society Advisory Council (CSAC), which was established on 25 June 2007 to support the work of the Bank's Country Office in Bolivia. The CSAC has the following members, drawn from various sectors of civil society: Xavier Albó, Gabriel Baracatt, Walter Limache, José Enrique Pinelo, Carlos Toranzo, George Satt and Nancy Ventiades (for more information on the makeup of the CSAC consult CAN/CBO).

The first regular session of the CSAC was held on 27 August 2007 to consider the Policy Dialogue Document, which was circulated for information as the basis of the Country
Strategy with Bolivia that the Bank has been preparing in dialogue with the government. We described for the CSAC the general aspects of the Bank's structure and financing, the course of its relations with the current government since it took office in January 2006, and the importance of the CSAC's participation in developing the strategy, which was now at its final stage of preparation. We also gave presentations on experience in Bolivia with respect to harmonization and alignment of development assistance, and the outcome of the policy dialogue with the government about the fundamental concepts underlying the Bank's strategy with Bolivia for the next three years.

The CSAC attached particular importance to the following issues in the process of preparing the final strategy:

a. Pay greater attention to the complex relationship between the central government and the subnational governments, recognizing the current tensions between those two levels over the still unresolved issue of departmental autonomy.

b. Consider opening broader channels through which the Bank could have dealings with NGOs and the various social movements in Bolivia, given their high profile in the country's economic and social dynamics.

c. Investigate how the Bank could reinforce the impact of its strategies, policies and programs on behalf of the environment and of indigenous peoples in Bolivia.

d. Include the need to exert greater control over the adverse effects that some Bank operations may have, such as greater flows of contraband and other unwanted byproducts of cross-border road integration.

e. Deepen dialogue with the Government in support of institutions dealing with environmental issues and indigenous peoples, now that the Ministry of Sustainable Development and Planning and the Ministry of Indigenous Affairs and Aboriginal Peoples have disappeared.

f. Give urgent support to shifting the current project focus that dominates the Government's development policies, in favor of a programmatic approach.

g. Help the government and other donors to move from a centralized planning focus to a decentralized one, recognizing the kind of changes that the current government seeks to foster through the PNP as well as people’s demand for decentralization.

h. Pursue a labor policy focused on sectors with broad potential to generate economic growth and employment, instead of an openly multisectoral policy with indiscriminate activities.
**POSSIBLE EFFECTS OF INSTITUTIONAL CHANGES IN THE HYDROCARBONS AND MINING SECTORS**

The special weight of the hydrocarbons and mining sectors in the Bolivian economy makes it important to consider some specific challenges and risks associated with policies in this area. The challenges identified relate to:

a. **Renegotiation of contacts and foreign direct investment.** The process now underway has been a complex one and has sparked tensions with multinational oil companies and their home countries. The new contracts that have recently been signed, and which must be ratified by Congress, constitute an important first step towards reestablishing legal security in the sector, and the outcome of this process (including pending regulations) will determine the fate of foreign direct investment in the oil sector. In this context, the Bolivian government faces the challenge of restoring international investor confidence and attracting more foreign capital.

b. **Market development.** Bolivia's natural gas, whether raw or processed, needs international markets that have absorption capacity and that are stable over time. Gas reserves amount to some 48 trillion cubic feet (Tcf). Selling this gas demands major investments in exploitation and in infrastructure for getting it to market. If Bolivia fails to develop secure markets for its natural gas it could jeopardize the sustainability of its long-term growth.

c. **Evolution of reserves and investment needs.** In the absence of greater investment to expand oil and gas exploration and production capacities, the country's ability to deliver gas could drop, according to current outside estimates, to 35 million cubic meters a day. This would represent a potential delivery shortfall of 8.2 million cubic meters a day, or nearly 20% of expected demand. Investment in this area fell in 2005 to less than US$200 million, and reached US$74 million in the first four months of this year. According to external sources, proven and probable reserves of gas have declined steadily since 2002 (from 54 Tpc to 48 Tpc in 2005), and proven reserves declined further in 2006 to 18 Tpc (from 26.75 Tpc in 2005). If this trend continues, it could pose a threat to Bolivia's capacity to deliver liquefied and condensed gas, and in particular to fulfill its contracts with Brazil and Argentina, in the face of rising domestic market needs.

d. **Externalities of oil and gas development on the rest of the economy and its institutions.** While Bolivia's hydrocarbons wealth represents a great opportunity for the country's development, its magnitude also poses significant challenges. In the first place, there is a danger that Bolivia's strong comparative advantage in gas exports could make it uncompetitive in other export branches that are important for the country's long-term development—the so-called Dutch disease—and this risk is especially acute at times of high international prices such as now prevail. There is also a risk that technological development will be stifled, when investment is concentrated...
in extractive activities to the detriment of investment in human capital and in areas of rising yields: this too could jeopardize a long-term development strategy. A further challenge lies in the institutional risk inherent in the exploitation of natural resources. The literature on this subject suggests that natural resource rents inhibit the development of the tax system and, with it, the mechanisms of oversight and discipline that societies demand of their governments. This leads to political patronage and *clientelismo* and can undermine the capacity of the State to promote social well-being. Finally, the volatility of external (and fiscal) flows adds a further dimension pointing to the need for a revenue stabilization fund.

e. **Mining Code reforms.** The reforms to the 1997 Mining Code and the Mining Taxation System now under consideration are intended to raise taxes on profits, create royalties, and eliminate accreditation at times, as now, when prices are doing well. Those reforms would no doubt produce a significant increase in tax revenues, but they could also discourage new investments by private mining companies, because of their differential impact at the macroeconomic level.
# Illustrative Operations Program 2008-2010

## Sovereign Guaranteed Operations

<table>
<thead>
<tr>
<th>Approval</th>
<th>Project number</th>
<th>Title</th>
<th>Amount (US$)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>2008</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nov 08</td>
<td>BO-L1021</td>
<td>National agricultural irrigation program with focus on watersheds</td>
<td>35,000,000</td>
</tr>
<tr>
<td>Nov 08</td>
<td>BO-L1038</td>
<td>Neighborhood improvement II</td>
<td>30,000,000</td>
</tr>
<tr>
<td>Dec 08</td>
<td>BO-L1037</td>
<td>Food and agriculture health and quality program</td>
<td>10,000,000</td>
</tr>
<tr>
<td><strong>2009</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jun 09</td>
<td>BO-L1032</td>
<td>PROPAIS II</td>
<td>10,000,000</td>
</tr>
<tr>
<td>Jun 08</td>
<td>BO-L1034</td>
<td>Water and sewerage in periurban areas</td>
<td>20,000,000</td>
</tr>
<tr>
<td>Mar 09</td>
<td>BO-L1040</td>
<td>Rural initiatives to support food security (CRIAR)</td>
<td>20,000,000</td>
</tr>
<tr>
<td><strong>Inventory</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>INV</td>
<td>BO-L1017</td>
<td>Modernize fiscal management (SIGMA)</td>
<td>15,000,000</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L1018</td>
<td>Bond underwriting for Banco de Desarrollo Productivo (BDP)</td>
<td>50,000,000</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L1028</td>
<td>La Paz drainage system II</td>
<td>20,000,000</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L1030</td>
<td>Standards-based road maintenance II</td>
<td>35,000,000</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L1031</td>
<td>Rural roads program</td>
<td>20,000,000</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L1039</td>
<td>Sustainable tourism program</td>
<td>12,000,000</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L___</td>
<td>Rural electrification</td>
<td>10,000,000</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L___</td>
<td>Development of the Northern Corridor</td>
<td>TBD</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L___</td>
<td>Revitalization and urban development of La Paz</td>
<td>TBD</td>
</tr>
<tr>
<td>INV</td>
<td>BO-L___</td>
<td>Job training: “My first job”</td>
<td>TBD</td>
</tr>
</tbody>
</table>
BANK DISBURSEMENTS AND FLOWS WITH THE COUNTRY

As agreed in the round of Bank debt relief with Bolivia that culminated in 2007, projections are for approximately US$74.3 million in new approvals annually for the 2008-2010 sovereign lending program. Projected disbursements on the portfolio of loans in execution is estimated at an annual average of US$66.5 million for the same period, and that level of disbursements will produce neutral flows on average for the same period. Projected net flows for 2008-2010 represent an expansion with respect to the 2004-2007 period, when the Bank’s financial relationship with Bolivia was characterized by a gradual decline in disbursements and negative net flows that averaged US$10.5 million per year.

Bolivia: Net Financial Flows with the IDB (in US$ millions)

<table>
<thead>
<tr>
<th>Year</th>
<th>Loan disbursements</th>
<th>Loan repayments</th>
<th>Interest and other charges</th>
<th>Other contributions</th>
<th>Net flow</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>102.0</td>
<td>60.2</td>
<td>33.4</td>
<td>1.2</td>
<td>7.2</td>
</tr>
<tr>
<td>2001</td>
<td>84.5</td>
<td>55.9</td>
<td>27.0</td>
<td>1.0</td>
<td>0.6</td>
</tr>
<tr>
<td>2002</td>
<td>97.7</td>
<td>63.2</td>
<td>21.3</td>
<td>0.8</td>
<td>12.4</td>
</tr>
<tr>
<td>2003</td>
<td>263.5</td>
<td>79.2</td>
<td>26.9</td>
<td>0.6</td>
<td>156.8</td>
</tr>
<tr>
<td>2004</td>
<td>109.8</td>
<td>79.9</td>
<td>29.3</td>
<td>0.3</td>
<td>0.3</td>
</tr>
<tr>
<td>2005</td>
<td>142.3</td>
<td>74.0</td>
<td>32.0</td>
<td>0.0</td>
<td>36.3</td>
</tr>
<tr>
<td>2006</td>
<td>62.7</td>
<td>76.4</td>
<td>32.9</td>
<td>0.0</td>
<td>-46.6</td>
</tr>
<tr>
<td>2007</td>
<td>46.0</td>
<td>58.0</td>
<td>20.1</td>
<td>0.0</td>
<td>-32.1</td>
</tr>
<tr>
<td>2008*</td>
<td>32.7</td>
<td>50.9</td>
<td>18.7</td>
<td>0.0</td>
<td>-36.9</td>
</tr>
<tr>
<td>2009*</td>
<td>66.8</td>
<td>50.1</td>
<td>14.6</td>
<td>0.0</td>
<td>2.1</td>
</tr>
<tr>
<td>2010*</td>
<td>101.2</td>
<td>50.5</td>
<td>14.0</td>
<td>0.0</td>
<td>36.7</td>
</tr>
</tbody>
</table>

Source: IDB Finance Department. LMS reports.
* Projections
## Matrix of International Cooperation Intervention Areas

### NDP Pillar

<table>
<thead>
<tr>
<th>Sector</th>
<th>&quot;Dignified Bolivia&quot;</th>
<th>&quot;Democratic and Sovereign Bolivia&quot;</th>
<th>&quot;Productive Bolivia&quot;</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>National defense</td>
<td>Education/ Vocational training</td>
<td>Natural disaster emergencies</td>
</tr>
<tr>
<td>Agency</td>
<td></td>
<td>Natural disaster emergencies</td>
<td>Development of labor</td>
</tr>
<tr>
<td>Bilateral</td>
<td>Germany</td>
<td>Belgium</td>
<td>Canada</td>
</tr>
</tbody>
</table>
BIBLIOGRAPHY

1. Internal documents used in preparing the strategy


CHAVEZ, Gonzalo et al. (2007), “Estudio de Análisis de Riesgos para la Economía de Bolivia.”


2. Other background documents


IMF (2005), “Bolivia: Ex-Post Assessment of Longer-Term Program Engagement,” J. Zettelmeyer (Head, RES), R. Balakrishnan (WHD), A. Giustiniani (MFD), P. Medas (FAD) and J. Rahman (PDR), March.


IMF (2006), “Bolivia. Selected Issues,” prepared by Antônio Furtado, Ravi Balakrishnan, Borja Gracia, Laura Jaramillo, and Mario Mansilla (WHD), Pablo López-Murphy and Alejandro Simone (FAD), and Sergei Dodzin (PDR), June.

IMF (2006), “Bolivia: 2006 Article IV Consultation—Staff Report; Staff Statement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for Bolivia,” Country Report No.06/270, July.


Rol del Estado en la Intermediación Financiera,” unpublished draft.


