

# Executive Summary

In 2016 the global economy continued to register a modest performance, keeping the low growth trend experienced in the last years and showing the lowest expansion rate since the international financial crisis of 2008-2009. The slowdown of the global trade during this year was equally significant, reaching a growth pace even lower than that of the global activity. As it has been experienced for several years, emerging market and developing economies have been the driving force of the global economic dynamics; while advanced economies had a weaker than expected growth.

Meanwhile, after reaching minimum levels during the first quarter, the international prices of commodities experienced a slight improvement by the end of 2016, although still below the levels of previous years. In line with this performance, the major advanced economies registered a rise in their inflation indicators, causing changes in the perception of the future evolution of their monetary policies. In regards to the financial and foreign exchange markets, there was a response to the uncertainty caused by political and economic events.

In the regional context, South America showed a second consecutive year of negative growth, with heterogeneity among countries. In regards to inflation, the price variation of some neighboring countries still remains above target levels, subtracting space to the central banks to adopt monetary policies to stimulate demand, although few countries lowered their reference rates by the end of the year.

Given a more adverse international context than initially expected, economic authorities decided

to continue the implementation of countercyclical policies in an effort to support the economic dynamism and the social protection programs.

In this sense, the Central Bank continued with the expansionary orientation of its monetary policy initiated in mid-2014. Without abandoning the preservation of the price stability, such orientation allowed high levels of liquidity and interest rates of public securities close to zero. These issues, together with the Financial Services Law provisions, contributed to sustain the credit dynamism and, therefore, to boost economic activity, especially among sectors whose performance had a greater degree of association with liquidity levels and monetary and fiscal policies.

The Central Bank reduced the weekly placement of monetary securities, which helped to generate net redemptions during this year. Also, the anticipated redemptions of claimable securities option was exercised and significant amounts of seasonal liquidity at the beginning of the year were regulated in order to reinject these resources later, during periods of greater liquidity requirements. In the last quarter, with a view to regulate seasonal excess liquidity, monetary securities were issued and their offer in auction was increased, leading to a gradual rise in the rates of these monetary instruments. This also contributed to recover monetary policy spaces that would allow an eventual accommodative orientation in 2017.

In regards to the exchange rate policy, contrary to the high volatility in foreign exchange markets of neighboring economies, Bolivia's exchange rate stability contributed to anchor public expectations and to avoid the emergence of external inflationary

pressures, supporting an expansionary monetary policy. Additionally, such stability was important to consolidate the de-dollarization process. It is remarkable that positive results in external inflation control and deepening remonetization have been obtained without the generation of persistent misalignments of the real exchange with respect to its long term equilibrium explained by its fundamentals. On the other hand, the Executive Branch of the Government continued applying various measures that contribute to ensure price stability and food security and sovereignty.

In coordination with the Executive Branch of the Government, the Central Bank continued supporting social and economic development through the financing of Strategic National Public Enterprises (EPNE, for its acronym in Spanish) and the trust fund established with the National Fund for Regional Development. New monetary disbursements to strategic projects and to provide local counterparts for investment projects of Departmental Governments were carried out. At the same time, transfers to pay the Juana Azurduy Bond and the supply of bonds to small savers as a financial option with better yields than that of the Financial System were sustained. Like such measures, the orientation of the exchange rate policy also supported the economic growth and the redistribution of income.

Despite the adverse external context, GDP available information by September 2016 prove that the dynamism of economic activity of Bolivia remained solid, reaching a growth rate of 4.4%, resulted from the strength of domestic demand that respond positively to countercyclical policies of the Central Bank and the Executive Branch of the Government. This performance was reflected in positive results among all economic sectors (except for hydrocarbons sector), especially non-extractive sectors and those which are more linked to the impulses of monetary and fiscal policies. In this line, it is expected by the end of 2016 that the country reach the highest growth rate in South America for a third consecutive year and for the fourth time since 2009.

On the supply side, the output growth was explained through the good performance of Manufacturing Industry, Financial Institutions, Insurance, Real Estate

and Services provided to companies; Transport and Communications; Public Administration Services; Commerce; Construction; together with the rebound of mining activity. On the expenditure side, consumption continued underpinning the economic growth through its significant contribution to the domestic demand; stimulus through public expenditure and investments, together with the social protection programs, also contributed to boost aggregate demand.

Additionally, Balance of Payment estimates to December reflect a decrease in the Current Account deficit from 5.7% of Gross Domestic Product (GDP) in 2015 to 5.6% of GDP in 2016. The trade deficit was mostly caused by the fall of exported value due to a price effect, while exported volumes increased in most cases. To be noted are the lower deficit in Services Balance due to greater income from inbound tourism; the improvement in the net result of primary income due to higher returns of the Net International Reserves; and the increase of secondary income explained by worker remittances.

Despite the better performance of the Current Account, the reduction of the Net International Reserves this year was greater due to a reversal result in the Financial Account, which registered a surplus in 2015. The explanation of this financing setback are the advance payments made by certain EPNE for capital goods manufacturing that will be incorporated to the economy in 2017. Nevertheless, it is important to point out that the national economy maintain high external solvency indicators, the Net International Reserves to GDP ratio is still the highest in the region and the International Investment Position is positive.

At the same time, the financial intermediation continued to display strong dynamism, particularly the credit to private sector, showing a similar flow to that of previous year record, mainly to the productive sector and social housing according with the Financial Services Law and the expansionary orientation of the monetary policy. The de-dollarization continued to progress, an outstanding achievement considering the international context of the appreciation of the U.S. Dollar. Likewise, Financial Intermediation Entities presented solid solvency and liquidity indicators.

By the end of the year, Bolivia recorded an inflation of 4.0%, lower than the regional average and the third

lowest rate during the last decade. It is important to highlight the price stability within a context of strong dynamism of the economic activity. During the last few months of 2016, the inter-annual inflation stood in the lower bound of the fan chart announced in the Monetary Policy Report of July 2016; such behavior was partially explained by the exchange rate stability that avoid the influence of external inflationary pressures, the price correction of perishable food prices affected by supply shocks towards the middle of the year, inflation expectations within the projection range previously announced and the moderate evolution of price variation in services.

In summary, countercyclical orientation of policies contributed to reach outstanding macroeconomic results in 2016, translated into the highest economic growth and one of the lowest inflation rates within the region. At the same time, social protection programs continued, supporting the reduction of poverty and inequality. It is important to emphasize that these achievements were accomplished by maintaining external solvency and lowering the Balance of Payment Current Account and fiscal result imbalances.

Regarding the future outlook, at the international level, it is expected a global economic revitalization in 2017, based on the emerging market and developing economies performance and the improvement of their terms of trade in virtue of greater recovery prospects of commodity prices, highlighting the expected recovery of oil prices.

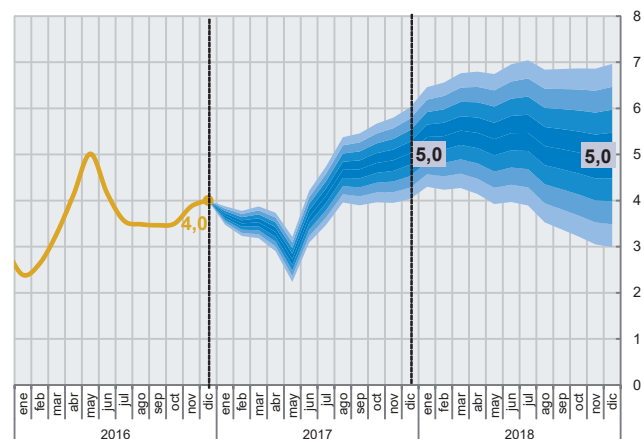
In this context, South America may come out of the 2015-2016 recession, projecting a moderate growth in 2017, with heterogeneity in the extent of recovery of all related countries. At the same time, the closing of capacity gaps and the increase of commodities prices could lead to an upward bias of inflation indicators among regional countries. In this sense, it is expected a significant acceleration in the external GDP growth and, to a lesser degree, in the external inflation relevant for Bolivian economy.

Respect to country's economic performance, it is expected an economic growth of 4.7% by the end of 2017, greater than that observed in the previous year. In presence of better internal and external conditions, such rate would be once again the highest in South

America. This performance would be based on less negative effects of adverse climatic events and a good behavior of most economic sectors, especially those closely linked to monetary and fiscal policies. On the expenditure side, the economic expansion would be sustained mainly through the domestic demand and a slight improvement in the contribution of external demand due, in part, to the price increase of main exportation products and the gradual recovery of our trading partners.

Also, the 2017 inflation probably rise slightly above the 2016 rate, mostly due to external factors, besides the statistical effect of basis for comparison. It is expected that de price variation reach a rate around of 5.0% by the end of the year, in a range between 4% and 6%, projecting a similar rate by the end of 2018.

**Observed and projected inter-annual inflation**  
(Percent change)



Source: Central Bank of Bolivia

Notes: The graph includes confidence intervals around the baseline scenario. The lightest part is consistent with a confidence interval of 90%

Respect to monetary policy, it will remain the same in 2017, with the implementation of monetary stimulus, taking into account the importance of a careful balance between preserving price stability and boosting economic activity for contributing to the economic and social development. The exchange rate policy will continue to reinforce the stabilization process of inflation, promoting the consolidation of the de-dollarization to preserve the stability of the financial system and the mitigation of external shocks effects.

Finally, it is important to point out that in addition to high growth and low inflation, it is expected that

the imbalances of external and fiscal accounts will continue to decrease in 2017. It should be noted that Bolivia maintains important financial buffers to sustain the countercyclical orientation of monetary and fiscal policies, supporting the dynamism of economic activity

and the social protection programs. If necessary and in response of any deviation from its objectives and goals, the Executive Branch of the Government and the Central Bank will use the policy instruments at its disposal to correct those deviations.