

Executive Summary

The world economy growth has weakened throughout 2018, while the performance divergence between regions and countries has intensified. This weakening is mainly explained by the trade tensions escalation and less encouraging growth forecasts of the world's leading economies. While the US showed a starker growth than other advanced economies, its performance is still at low levels with a slowdown in the second part of the year. This performance heterogeneity correlates to the inflation dynamics and the monetary policy normalization rate.

The differences between emerging and developing economies were accentuated, amid less favorable financial conditions and a loss of momentum in the commodities exporting countries recovery. The international commodity prices had a mixed behavior, but most notably after high international prices in the first part of the year, the oil registered a drop since mid-October. Alongside, the growing commercial tensions and the expected economy performance moderation had a negative effect on the international prices behavior. In South America, growth prospects were revised downwards, mainly due to the expected contraction in Argentina and the lower growth in Brazil, while inflationary pressures remained moderate in general terms, with the exception of Argentina. In the region, most of the currencies depreciated and the space to exert monetary stimulus has been reduced. In this context and despite the specific external shocks linked to the demand for natural gas, Bolivia stands out with the highest expected growth for 2018, one of the lowest inflations accumulated, exchange rate stability and the implementation of important expansive policies.

The BCB maintained the accommodative orientation of its monetary policy, which began in mid-2014, in order to help maintain the dynamism of economic activity and social protection programs without ignoring the domestic prices stability. This monetary orientation consisted in channeling resources to the local economy to maintain adequate levels of financial system liquidity and low interest rates, characteristics that helped maintain the credit level. This resource injection was implemented by using several economic instruments: reducing the banking legal reserves proportion in foreign currency, reducing the supply of monetary regulation securities, reducing the liquidity window fees, applying early securities redemption, and using other measures in coordination with the National Government. These actions increased the financial system credit which reached a notorious height and has been instrumental to meet the goals of the Law of Financial Services.

In the context of the depreciation of most of the region's currencies, the exchange rate stability policy helped to keep the public's expectations on the value of the dollar anchored, keep imported inflation under control, deepen the de-dollarization process and allow an expansive monetary policy. Likewise, it should be noted that the orientation of the exchange policy has not generated persistent misalignments of the real exchange rate in relation to its equilibrium level.

In coordination with the National Government, the BCB continued contributing to the economic and social development of the country through direct Strategic National Public Firm financing, giving credits to the local governments through the National

Fund for Regional Development trust and financing the payment of the Juana Azurduy transfer program. Likewise, other BCB policies applied in recent years support this goal in line to the Constitution of the country and the Productive Community Social Economic Model that also contributed to achieving outstanding macroeconomic results.

In 2018 macroeconomic stability was maintained despite a difficult regional context. Inflation remained controlled registering a year-on-year rate of 1.5%, the lowest value in the last nine years and the second lowest in South America. The inflation trend indicators showed a downward trajectory, which indicates that the price level stability was well and continuously established over its components. This behavior was explained by the correct application of the monetary and exchange policies, the good agricultural year and the constant supply of various basic basket products and services.

The national economic performance stood out in 2018, mainly in the non-extractive sectors. In spite of the weak external context, Bolivia's third-quarter GDP growth was 4.04%, one of the highest in South America. The annual growth rate in the second quarter reached 4.61%, which allowed the issue of the second Christmas bonus payment according to the current regulations. The economic growth most influential sectors up to September were: Agriculture, Forestry, Hunting and Fishing; Financial Services; and Manufacturing Industry. Likewise, we should highlight the recovery of Mining. On the expenditure side, domestic demand continued to be an important contribution to growth thanks to the fiscal and monetary impulses.

Regarding the external performance, in 2018 the deficit in Current Account to September was reduced due to the improvement in the Balance of Trade. The export growth in December was 9.5% - due to value increases of hydrocarbon exports, mining and nontraditional - higher than imports (7.9%). On the other hand, family remittances performed well contributing to the national income increase. The Financial Account reflected a positive liabilities issuance explained by the inflows of direct investment, the portfolio investment assets reduction, the assets for commercial loans reduction in the Other Investment account and the use of reserve assets. These better results, together with

the high international reserves level and sustainable external indebtedness, reflect the country's external strength.

On the other hand, credit and savings in the financial system increased during the year mirroring this sector's continuous contribution to the economy. The solvency and profitability indicators continued to reflect the soundness of the financial system. The financial system credit to the private sector kept growing significantly, driven by the accommodative monetary policy and the provisions of the Law of Financial Services, registering a historical record flow, highlighting the credits channeled to the productive sector and social interest housing. Likewise, the de-dollarization of portfolio and savings continued to strengthen, becoming a major achievement even internationally. In the same way, the monetary base and the monetary aggregates showed average growth rates higher than those of the previous administration.

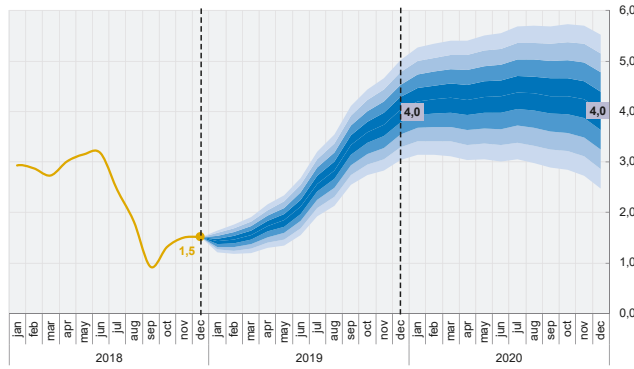
Regarding the world outlook for 2019, the global economy is expected to weaken persistently, according to the behavior observed mainly since the second half of 2018. This expectation is mainly explained by a scenario characterized by uncertainty related to trade negotiations, the effects of the increases in international interest rates, the commodities prices volatility - particularly oil -, the geopolitical tensions in some regions of the world, and other region specific occurrences. Within this environment, the growth of the external GDP relevant to Bolivia for both 2018 and 2019 is lower than previously expected.

The Bolivia economic performance is expected to be resilient to the unfavorable external shocks as it did before. The growth would be based again on the strength of domestic demand, which would encourage us to achieve a GDP growth of around 4.5% at the end of 2019. This result would rely on the non-extractive sectors, mainly the Agriculture and Livestock Sector, the Manufacturing Industry and Financial Services, among others, which would place us as one of the most solid economies in the region.

In this context, the projections in the baseline scenario indicate that inflation for both the end of 2019 and 2020 would be around 4.0%. Likewise, the quantitative and qualitative analysis indicates that 2019 inflation, with a 90% probability, would be between 3.0% and 5.0%.

Since the balance of risks shows equilibrium between the upward and downward factors, it isn't expected biased movements that could divert inflation from its base projection.

Inflation observed and projected
(In percentage)



Source: Central Bank of Bolivia
Notes: The chart includes confidence intervals around the central scenario. The clearest part of the graph is consistent with a 90% interval

While balancing the price stabilization policy, fostering the economic growth and contributing at the same time to the economic and social development, the BCB will continue implementing the accommodative monetary stance in coordination with the National Government. The orientation of the exchange rate policy will continue to reinforce the inflation control process, promoting the consolidation of de-dollarization to preserve the stability of the national financial system and the mitigation of the effects of external shocks. Finally, it should be noted that Bolivia maintains important financial buffers to sustain the aforementioned countercyclical orientation of policies, supporting the economic growth and the social protection programs. If necessary and in the event of any deviation from the objectives and goals, the National Government and the BCB will use the policy instruments at their disposal to correct these diversions.