EXECUTIVE SUMMARY

During the first quarter of 2012 global economic activity showed signs of a slight recovery. Nevertheless, due to: i) the worsening of the sovereign debt crisis in the Eurozone; ii) moderate indicators of U.S. economic activity; iii) the weakening of global demand; and iv) the consequent slowdown of emerging economies, the world economy experienced a further weakening. In this sense, projected global growth rate for 2012 (3.2%) was 0.8 percentage points (pp) below the one observed the previous year (4%).

In the Eurozone, uncertainty, financial stress and adjustment measures to reduce fiscal deficit, led this group of economies to fail into recession. Similarly, the behavior of financial markets and expectations of important fiscal adjustments, impacted negatively on the performance of U.S. economy, which had to mitigate these effects through monetary impulses and fiscal arrangements.

Slower growth in advanced economies affected negatively global demand. In this context, countries like China and India faced reductions in export earnings, contractions in their industrial sectors and lower foreign direct investment flows. As a result, these economies achieved lower growth rates although with slight recoveries later in the year.

Likewise, in Latin America, economies such as Brazil and Argentina experienced a slowdown despite the various stimulus measures implemented. In contrast, Peru, Venezuela, Chile and Bolivia, showed a good economic performance with growth rates above 5% (higher than the regional average of 3.1%), thanks to their strong domestic demand.

Commodity prices exhibited different behaviors. On the one hand, prices of minerals rebounded in the second half of the year (after a downward trend between March and July) due to the effects of supply constraints in some Asian countries and the revival of construction activity in China, among other factors. On the other hand, international oil prices, after sharp declines in the second quarter, regained their upward path in subsequent months albeit with some oscillations because of the decrease in the quantity supplied by the Organization of Petroleum Exporting Countries (OPEC). Meanwhile, food prices reflected a relatively stable trend with slight decreases by the end of the year, although remaining at elevated levels.

In this context of weak global demand and lower growth prospects, global inflation in 2012 tended to be lower than the previous year in both advanced countries (falling from 2.7% to 2% between 2011 and 2012) and emerging economies (from 7.2% to 5.9% over the same period). Within this environment, monetary authorities of these economies tended to maintain an expansionary stance in their policies.

In September, the U.S. Federal Reserve (Fed) started the third round of the Quantitative Easing Program (QE3), which involved monthly purchases of long-term mortgage securities for a total amount of $us40,000 million (MM). Additionally, through the extension of the "Twist"[1] Operation the Fed bought long-term bonds for about $us267,000 MM. These measures helped to inject liquidity into the financial system, thus reducing long term interest rates to minimum levels.

In July of 2012 the European Central Bank (ECB) decided to cut the policy rate to 0.75%, the lowest historical level. Additionally, the ECB contributed to the reduction of financial

[1] Program through which the Fed redeems long-term bonds by short-term securities.

tensions through two funding programs: i) the Long-Term Refinancing Operations (LTRO) Program, aimed at injecting liquidity through three-year loans to the banking system with a total value of approximately €1 billion; and ii) the Outright Monetary Transactions program (OMT), devoted to the purchase of sovereign debt of countries with financial problems (program subject to the formal request for financial aid from these countries). Similarly, the People's Bank of China cut its benchmark rate to 6% and, in the case of large banks, reduced legal reserve requirements to 20%. Another tool employed by the Chinese monetary authority was to reduce the rate for repo operations to low levels.

With regard to Latin America, some economies such as Mexico and Peru chose to maintain their policy rates constant. However, in most cases rates followed downward trends, and in Colombia and Brazil they were reduced several times. Furthermore, the latter economy linked the savings interest rate with the SELIC interbank rate in order to prevent migration of investments from government securities to financial system assets.

Regarding the Bolivian economy, during 2012 it showed a favorable performance reaching a growth rate of Gross Domestic Product (GDP) of 5.2% by the end of the year. This dynamics was explained mainly by financial services and hydrocarbons. From the expenditure approach, domestic demand continued underpinning growth. Nonetheless, it is worth mentioning the positive contribution of net external demand to GDP growth after five years of continuous negative impacts.

The good performance of the economy as well as higher tax revenues originated a fiscal surplus equivalent to 1.8% of GDP (surplus obtained for the seventh consecutive year). Actually, tax revenues, hydrocarbons sales, customs revenues and sales of other public companies reported an annual increase of 16.4% higher than growth of public expenses (14.1%). These expenses aimed to improve country's road infrastructure, increase investment in strategic sectors, as well as to promote social protection programs for the most vulnerable population sectors. It must be noted that fiscal results of 2012 implied a decrease of domestic financing to the public sector of Bs7,631 MM.

In 2012 external accounts also showed positive results. Indeed, exports and gross foreign direct investment reached record levels ($us11,233 MM and $us1,505 MM, respectively). These results as well as a remittances flow of $us1,094 MM explained the global surplus achieved in the Balance of Payments. In terms of its accounts, the largest surplus corresponded to the Current Account (7.8% of GDP) while the surplus in the Capital and Financial Account was of 2% of GDP. In line with this behavior, Net Foreign Exchange Reserves (NFER) amounted to $us13,927 MM by the end of 2012 with an increase of $us1,908 MM (15.9%) compared to the previous year.

Due to net redemptions of Treasury (TGN for its acronym in Spanish) and Central Bank of Bolivia (BCB for its acronym in Spanish) securities, domestic public debt was reduced by 7.4% (Bs2,552 MM equivalent to $us372 MM). The solvency indicator of medium– and long-term external public debt reached 15.4% of GDP in 2012, far below both the maximum limits recommended by international organizations and the ratios observed in other countries.

Consistent with the evolution of its fundamentals, monetary issue had an annual growth rate of 14.3% (16.3% in 2011). On the source side, the expansion of the monetary base was produced by higher revenues from exports and the consequent increase in the NFER. The growth rate of money supply in local currency was above the one recorded in total monetary aggregates, aspect that reflected higher confidence of the population in national currency.

The good economic performance, together with financial policies implemented by the BCB in coordination with the Ministry of Economy and Public Finance and the Supervisory Authority of the Financial System (MEFP and ASFI respectively for their acronyms in Spanish) promoted growth of the Financial System as well as deepened its de-dollarization process. Indeed, deposits of financial intermediaries grew by Bs16,560 million (22.5%), while loans increased by Bs11,738 million (19.5%). It is noteworthy that the absolute growth achieved in loans and deposits in 2012, constituted the highest in the economic history of the country. Besides, regarding the de-dollarization process, local currency reached a ratio of 72% of total deposits (8pp higher than in 2011) and 80% of total credits (10.5 pp greater).

Moreover, concerning the evolution of the Consumer Price Index (CPI) inflation reached a rate of 4.5% at the end of 2012, inside the ranges announced by the BCB in its Monetary Policy Report of January and July 2012 and slightly below the central forecast of both reports (5%).

Inflation in 2012 was explained mainly by the following factors: i) price adjustments in some services, especially those related to property rentals and housekeepers remunerations; ii) low variability of food prices, due to a good performance of the agricultural sector; iii) reduced external inflationary pressures because of the deterioration of global economy; and iv) little volatility and low figures of inflation expectations, which reflect public's confidence in the policies executed by the BCB and the Executive Branch of Government to control inflation.

Measures implemented by National Government (aimed at supporting productive activities and to ensure market supply), a prudent fiscal policy, and the suitable liquidity regulation carried out by the BCB were decisive for the positive outcomes obtained in terms of prices.

As in past years, in 2012 policies of the BCB have been characterized by its prudence and countercyclical orientation, being implemented in coordination with the Executive Branch. On the one hand, monetary policy maintained a careful balance between the objectives of preserving low and stable inflation and to contribute to economic growth. To this purpose, during the first half of the year the Monetary Authority made net sales of securities to regulate liquidity in the Financial System. From the second half of 2012, the orientation of monetary policy became gradually expansionary, reducing the supply of securities and keeping policy rates low. This approach aimed to counter the effects of the crisis in the Eurozone, the slow U.S. recovery and the slowdown in some sectors of neighboring economies, all of which took place in a phase of reduced domestic inflationary pressures.

Moreover, with the purpose of promoting the use of Bolivian currency both BCB and TGN continued prioritizing local currency operations while offering their securities. These orientation was applied as well in the process of direct sales of bonds to the public implemented by both entities (BCB Direct Bonds, BCB "Christmas holiday season" Bonds and Treasury Direct Bonds).In the same vein, amendments to reserve requirements were made, aimed at deepening the currency differentiation of reserve requirements, providing an additional boost to Bolivianization process. Note that this process was also stimulated by promotional campaigns for the use of the national currency (informative brochures, dramatization contests for students, among others disseminated by BCB).

With respect to exchange rate policy, in 2012 the exchange rate remained stable. This orientation responded to an external environment with reduced inflationary pressures and financial instability. Exchange rate stability allowed anchoring expectations and contributed to the process of Bolivianization. In addition, exchange rate policy implemented, allowed the real exchange rate to remain consistent with its fundamentals.

According to the portfolio diversification of international reserves, investments in Chinese Renminbi (CNH) were included in the Global Portfolio since May. Similarly, risk was diversified through investment in inflation-indexed U.S. Treasury bonds (TIPS) for a value of $us500 MM. Finally, the Gold Portfolio remained unchanged its stock of 42.3 tons, with an increase of $us167 MM under the gold price valuation.

As a result of these policies, reserve portfolios in 2012 reported a return of $us134 MM, of which $us120 MM accounted for monetary reserves and $us14 MM to income of gold reserves.

In 2012, the BCB was a net seller of foreign currency to financial system, especially in the fourth quarter. It is noteworthy that exchange operations in the financial system were performed within the limits set by the regulations.

In line with what has been undertaken in recent years, the BCB continued to implement additional measures in order to contribute to economic growth and social development. Indeed, in order to contribute to the development of the Department of La Paz, the BCB approved the specific regulations for the granting of credit to TGN for construction, deployment and management of cableway La Paz - El Alto.

Similarly, within the framework of energy security policy and to finance investment projects in the hydrocarbon sector, the BCB continued providing concessional loans to Bolivian Fiscal Oil Fields (YPFB for its acronym in Spanish). In this sense, the end of 2012 the BCB disbursed to YPFB a total of Bs2,691 MM. Additionally, the BCB also continued to support Strategic National Public Enterprises (EPNE for its acronym in Spanish). Three new contracts were signed with the National Electricity Company; disbursements were completed to the Mining Corporation of Bolivia (COMIBOL for its acronym in Spanish) for the project “Implementation of Pilot Plant in Bolivia Lithium Batteries Phase III” and began disbursements to Sugar Company San Buenaventura (EASBA for its acronym in Spanish) to finance productive investment projects.

In what refers to the economic outlook in the external context, a gradual recovery of global growth is expected during 2013. However, the projected economic recovery would be much more moderate than the one estimated previously, due to the uncertainty still prevailing in some developed economies.

Regarding internal perspectives, official projections for 2013 indicate GDP growth of around 5.5%. On the activity side, underlying dynamics includes a correction factor that in the previous year have determined a contraction of Mining. Furthermore, from the perspective of expenditure, domestic demand would continue to underpin growth. Meanwhile, regarding the future course of inflation, it is expected to be around 4.8% at the end of 2013 (in a range between 3.8% and 6.3%), while in 2014 inflation would be around 4%. The projections outlined are part of the Decision Agreement of Execution Fiscal-Financial Program 2013 signed on January 28, 2013 between the Ministry of Economics and Public Finance and the Central Bank of Bolivia.

In terms of institutional management, adjustments and additions were made to the regulations issued by the Board of Directors of BCB, consistent with the institutional and social changes experienced by the country. Among them highlighted the approval of loans to EPNE and the New Regulations for International Reserves Management enabling investment in new instruments. There were also approved regulations regarding NIR for buying gold in the domestic market, as well as for the granting of a loan to the Fund for the Industrial Revolution and Production (FINPRO for its acronym in Spanish). It was also provided the sale of U.S. dollars through one-stop window of BCB, making access to this currency easier by the public. Finally, it is worth noting the approval of the Institutional Strategic Program 2013-2017 of the BCB, which determines the medium-term guidelines for the institution operations.

With regard to the payment system, various actions on operational and regulatory aspects by BCB are highlighted, all intended to facilitate the transfer of funds and availability of cash for different sectors of the economy. Indeed, in 2012 the BCB held workshops in several cities of the country to promote the incorporation of non-banking institutions and approved the addition of 2 new participants. It also expanded the number of operation days for the clearing house electronic order and established a flat rate for all system operations. Likewise international remittance transfers were regulated and there was continuity in the Integrated Settlement Payments Project. The value processed by Payment Systems during the year was Bs635,869MM, more than three times the value of GDP, a figure that reflects the growing importance of this system in resource mobilization.

Regarding the management of monetary material, the bigger Bolivianization and money emission resulted in a growing demand for such material. To promptly meet these requirements, as well as ensure the replacement of damaged units, were distributed 130 MM pieces of notes through the Financial System (equivalent to Bs7,631 MM) and 117 million pieces of coins (Bs132 MM); at the same time, were removed from circulation 76.6 MM pieces to improve the average quality of the banknotes.

Moreover, in terms of their institutional affiliation, in 2012 the BCB strengthened its relationship with other organizations from the public and private sectors at national and international levels. Examples of this were the signing of agreements with the Chamber of Representatives in order to improve access to information, and the National Institute of Statistics (INE for its acronym in Spanish) to support the implementation of the National Census of Population and Housing. In addition, the BCB arranged with the Ministry of Education the implementation of the Economic-Financial Education Program in the Plurinational Educational System curricula.

As part of the Institutional Transparency and Social Control, the Monetary Authority maintained a constant relationship with social organizations. In 2012, the priority topics in discussion were: Credits to EPNE, NIR Management and Bolivianization Benefits, performing public hearings in various places of the country for the purpose. In the same vein, with the purpose of informing compatriots living outside the country on the actions and role exercised by the BCB in recent years, it participated in the Inter-Ministerial Fair “Communicating the change without borders” held in December 2012 in Barcelona, Spain.

Simultaneously, the BCB gave continuity to the promotion and dissemination of knowledge activities. In July, with the participation of national and international speakers, held the Sixth Monetary Conference under the theme “Stability and Economic Growth.” Subsequently, in August held the Fifth Meeting of Bolivian Economists in the city of Santa Cruz, whose main theme was “Economic Growth and Development from the Regions.” Similarly, continued with the organization of school competitions linked to economic issues, performing the Fifth School Essay Contest and the Second School Dramatization Tournament, involving students from all around the country. In the same way, encouragement of research continued through the Fourteenth National Research Award and Academic Seminars conducted by the BCB. Finally, the Monetary Authority participated in the Fourth edition of the Credit Fair in November.

Financial statements of the BCB were audited by PricewaterhouseCoopers and represent fairly well all significant aspects as the financial condition, operation results and cash flows of the BCB to December 31st, 2012.

Finally, it should be noted that the BCB reaffirms its commitment to appropriately use available policy instruments, in order to fulfill its constitutional mandate of preserving the domestic purchasing power of the currency to contribute to economic and social development of the country.