



Money and Banking Conference  
Central Bank of Republic of Argentina

# **Monetary Policy in Bolivia**

## **Lessons from the Latest Economic Crisis**

**Gabriel Loza Tellería**  
President of the Central Bank of Bolivia

**Buenos Aires, September 2010**

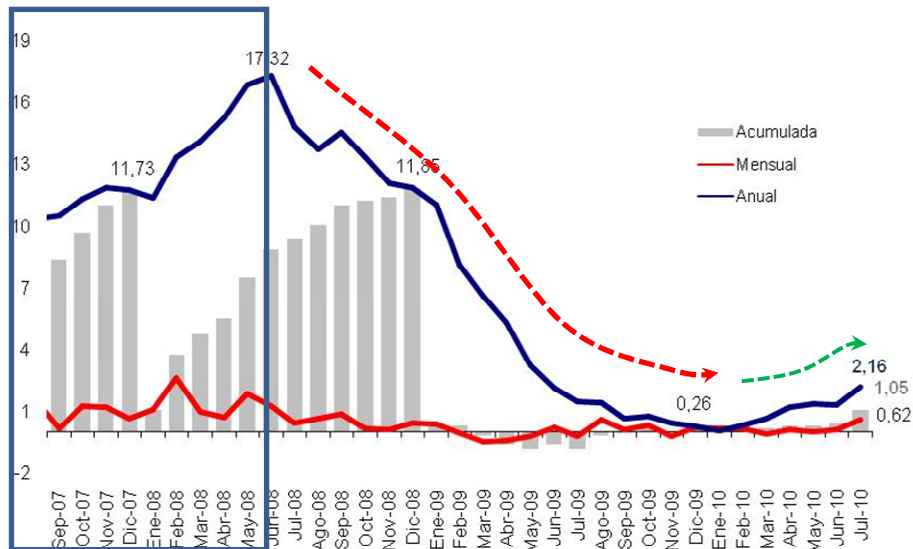
# Dealing with the Structural Crisis of Capitalism

- Bolivia is a small open economy characterized by partial dollarization, low trade and financial integration to global markets.
- Exports are highly concentrated on commodities. Therefore, Bolivian transmission mechanisms of external shocks are particular.
- Direct mechanisms come through international prices, specially commodities, and remittance flows.
- Indirect mechanisms include exchange rate as well as interest rates volatility of major economies and neighbor countries.

# External Shocks and Bolivian economy: Inflation upturn and Financial crisis

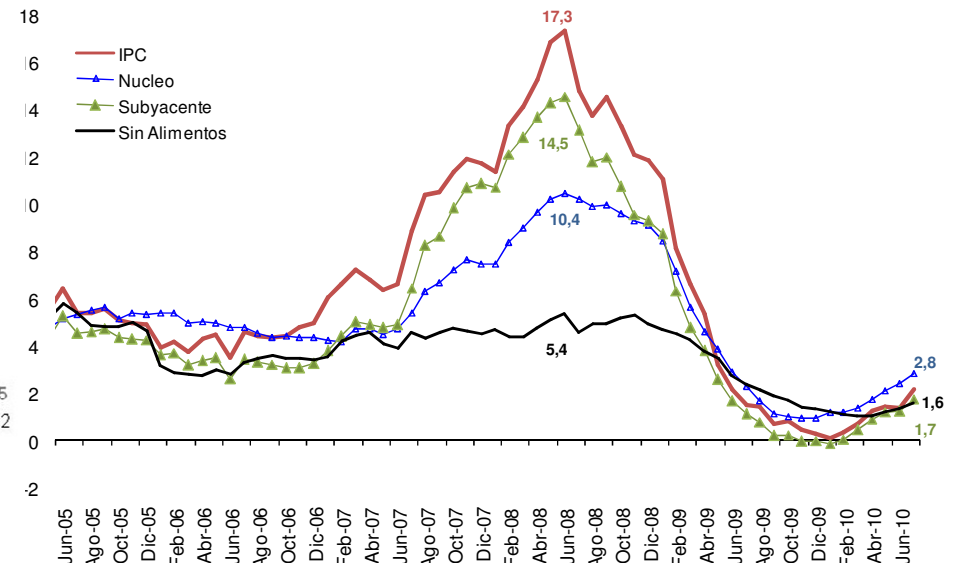
- Bolivian economy has experienced two major events: the abrupt increase in food and fuel prices between 2007 and 2008; and the effects of global economic crisis.

Inflation Rate : Monthly , interannual and cumulative (%)



Source: National Institute of Statistics

Core Inflation Measures (oya, %)

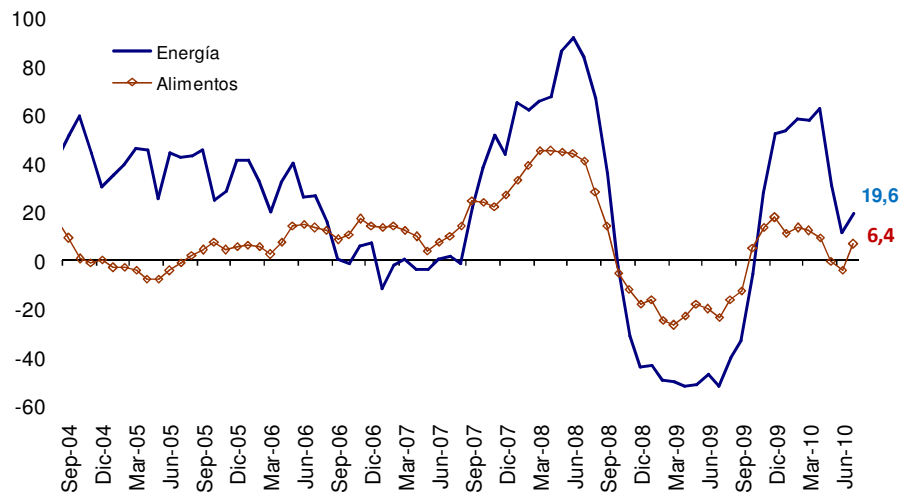


Source: National Institute of Statistics

# Countercyclical policies

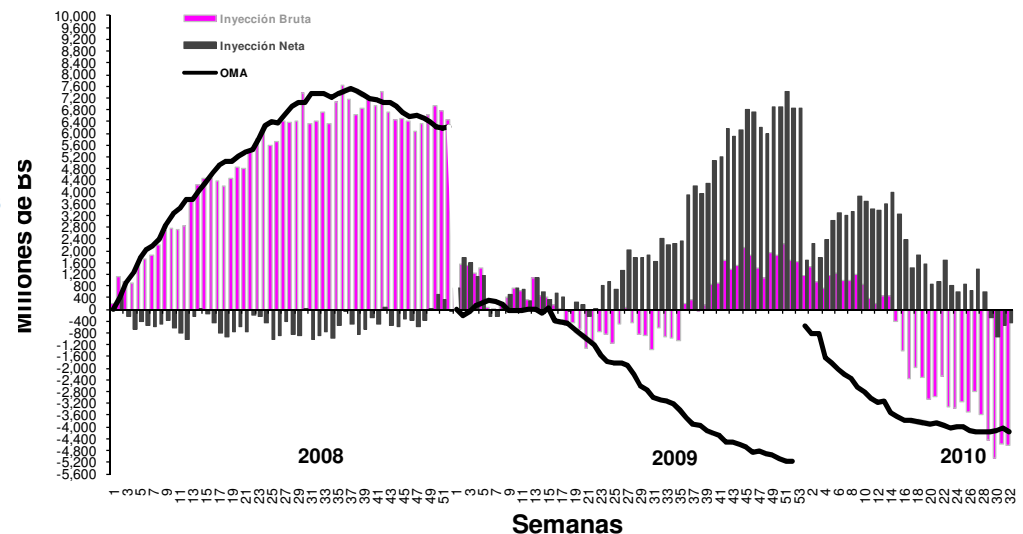
- First external shock: Monetary policy was contractive; and the exchange rate policy was characterized by mini revaluations and accumulation of international reserves.
- Second external shock: Monetary policy was expansionary and exchange rate stability attenuated external volatility transmission.

International prices of oil and food  
(oya, %)



Source: Worl Bank

Gross and net liquidity inflow  
(Millions of bs. accumulated in the year)

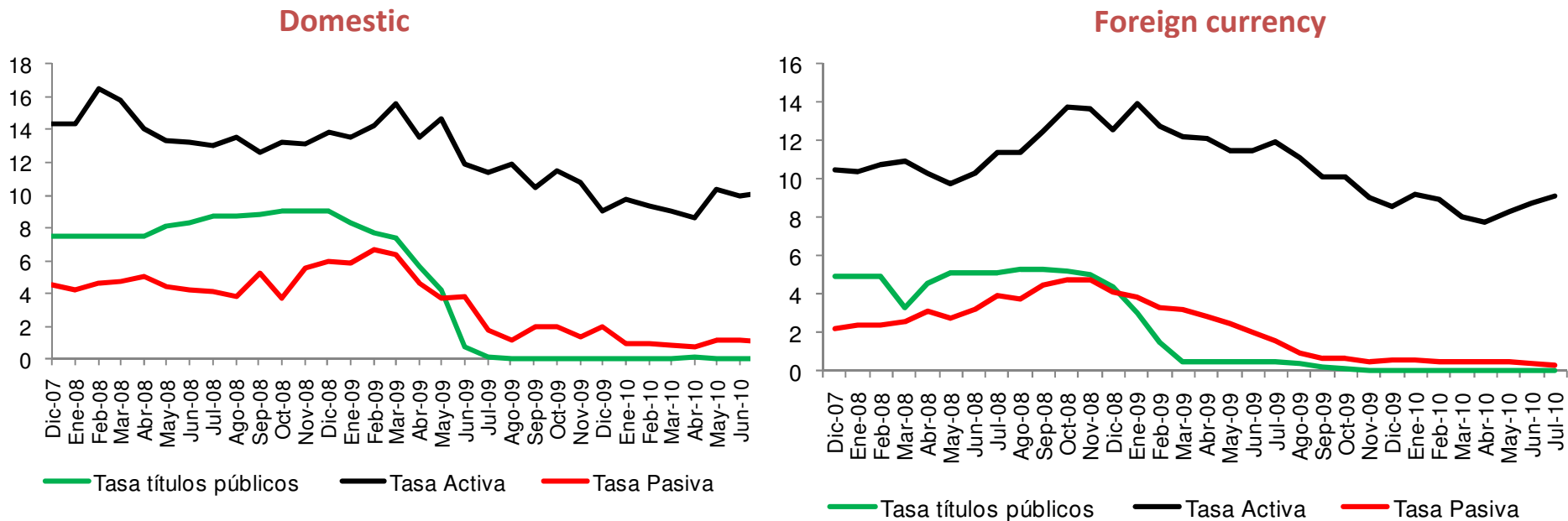


Sources Central Bank of Bolivia

# Countercyclical monetary policy

- Expansionary monetary policy: net treasury bills maturity induced a substantial decline of money market rates, partially transmitted to the interbank and financial market rates.

Monetary policy and financial interest rates (%)

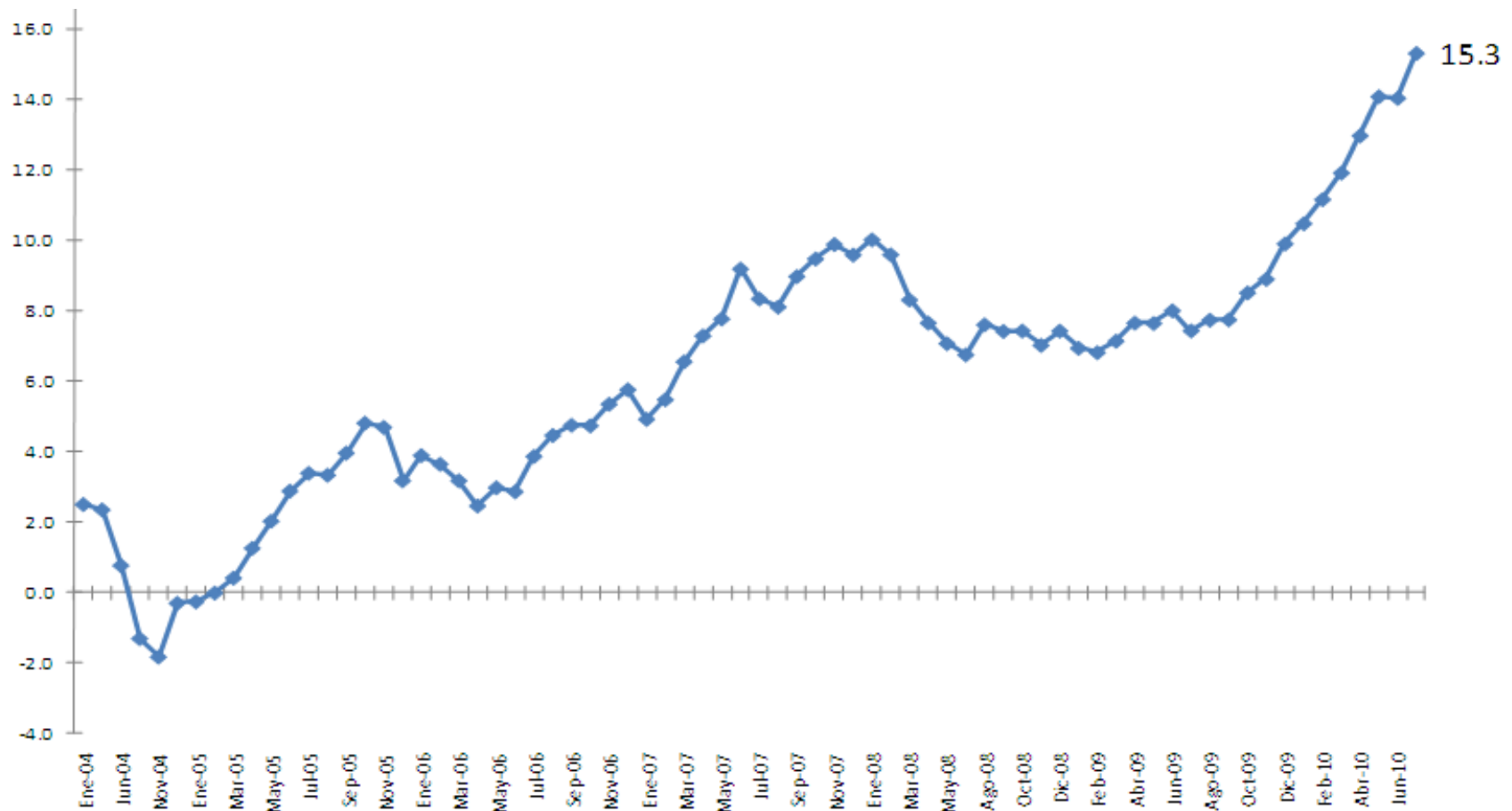


Source: Central Bank of Bolivia

# Countercyclical monetary policy

- This behavior contributed to a higher domestic credit to private sector growth, mainly in domestic currency, which implied lower dollarization.

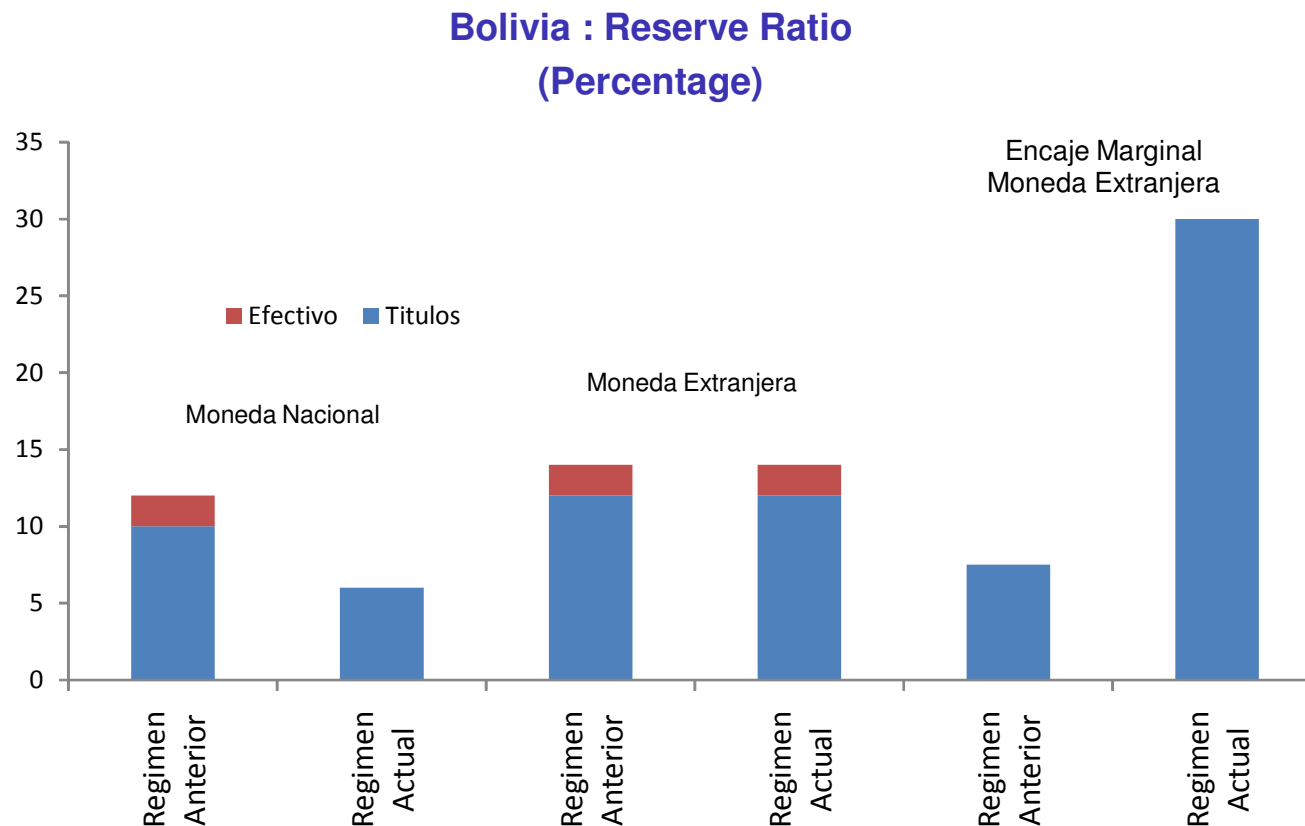
Domestic Credit to Private Sector Growth  
(oya, %)



Source: Central Bank of Bolivia

# Reserve requirement policy

- Bolivian reserve requirement policy was different from conventional policies, even in dollarized countries. Foreign currency requirement was increased to discourage dollarization, while domestic rate was reduced to promote credit growth.

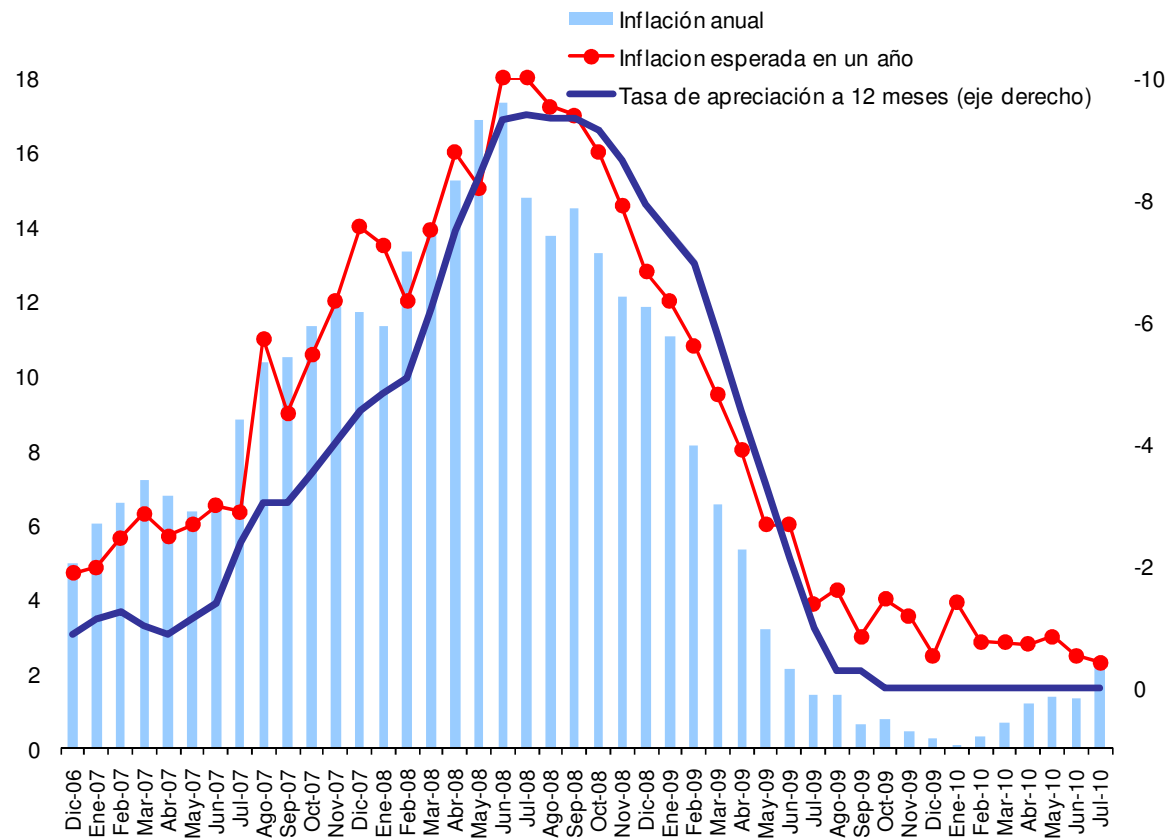


Source: Central Bank of Bolivia

# Exchange rate stability

- Bolivian exchange rate policy was unconventional as well. Zero rate of crawl policy anchored foreign exchange market outlook. Furthermore, it has been consistent with price stability achieved since September 2009.

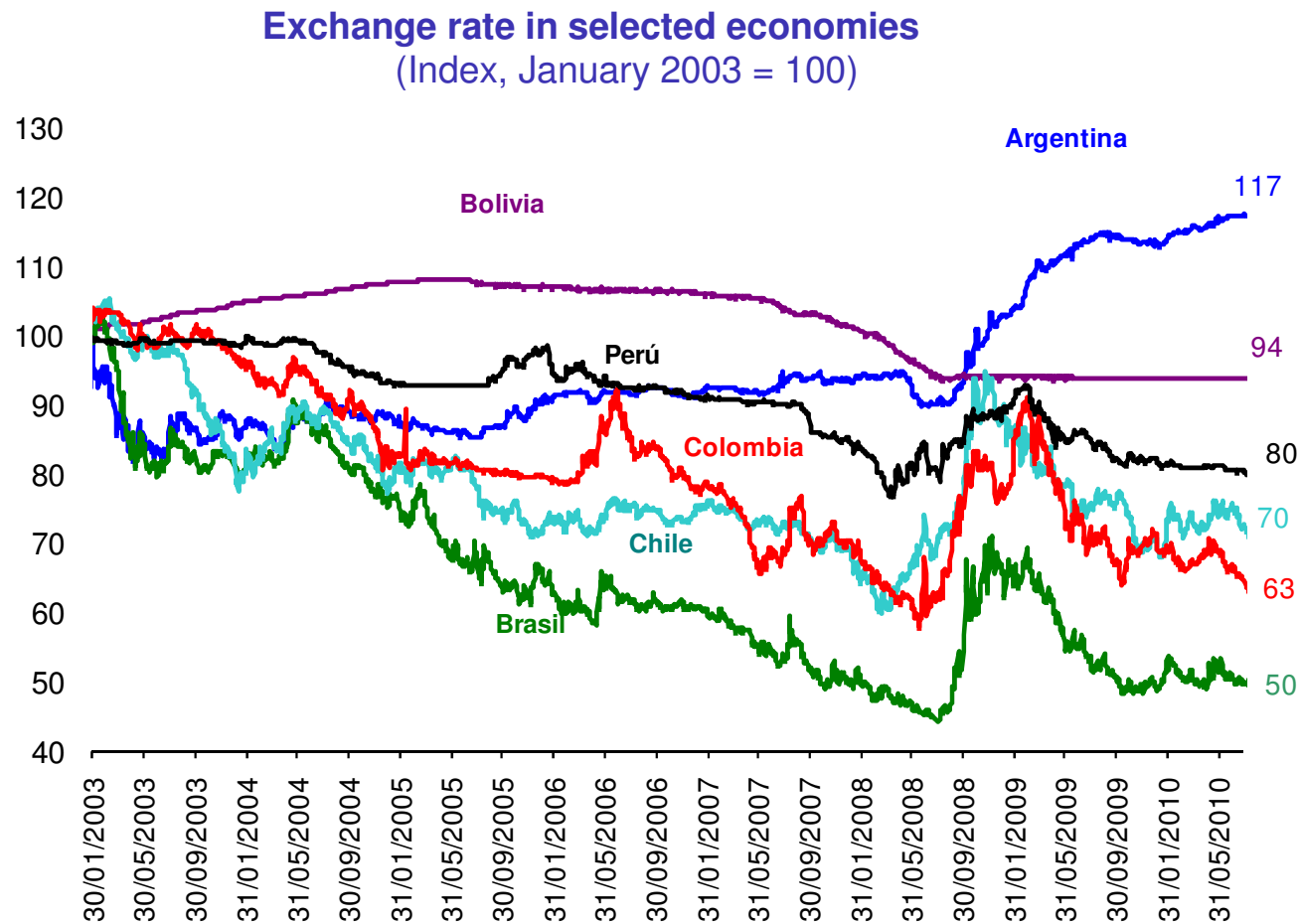
Nominal appreciation, observed and expected inflation  
(oya, %)



Source: Central Bank of Bolivia

# Exchange rate stability

- Bolivian case is a clear example of low exchange rate volatility during the crisis, while other currencies showed sudden movements.

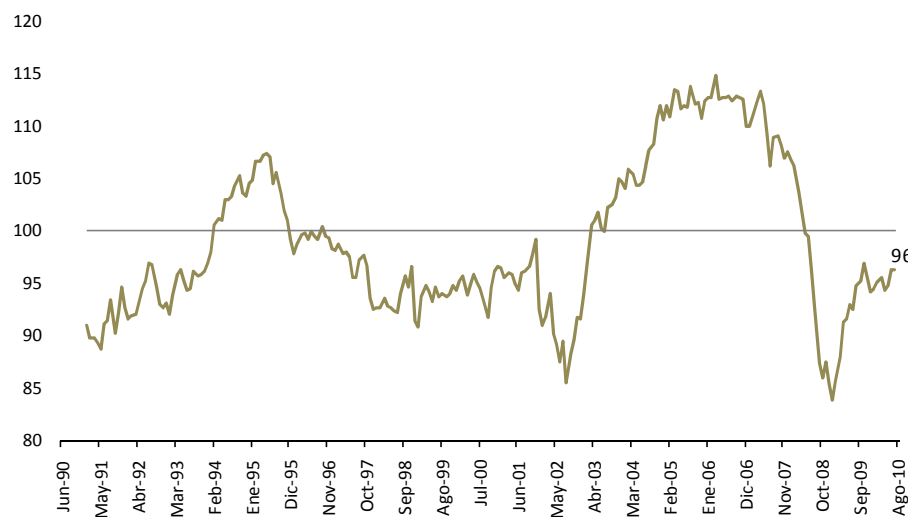


Sources: *Bloomberg* - Central Bank of Bolivia

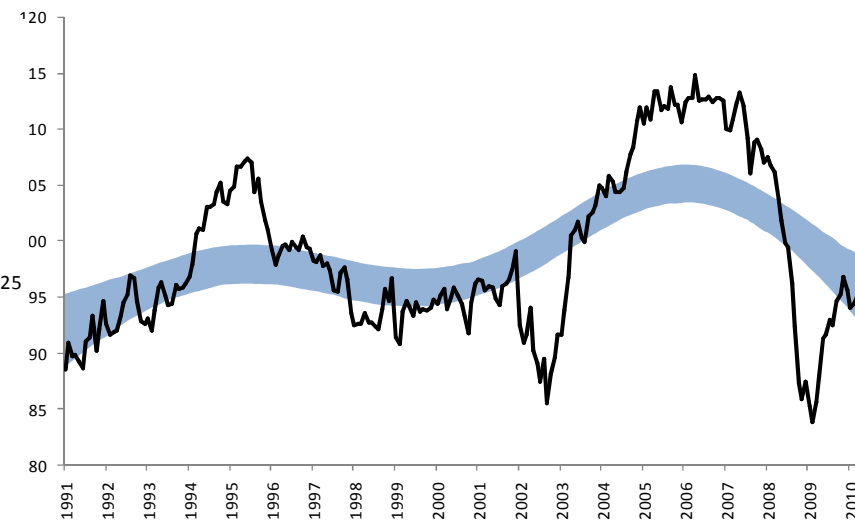
# Exchange rate stability

- Exchange rate policy preserved purchasing power of the local currency without persistent misalignments.

**Real Exchange Rate, 1991-2010**  
(Index, August 2003 = 100)



**Equilibrium and Observed RER**  
(Index, August 2003 = 100)

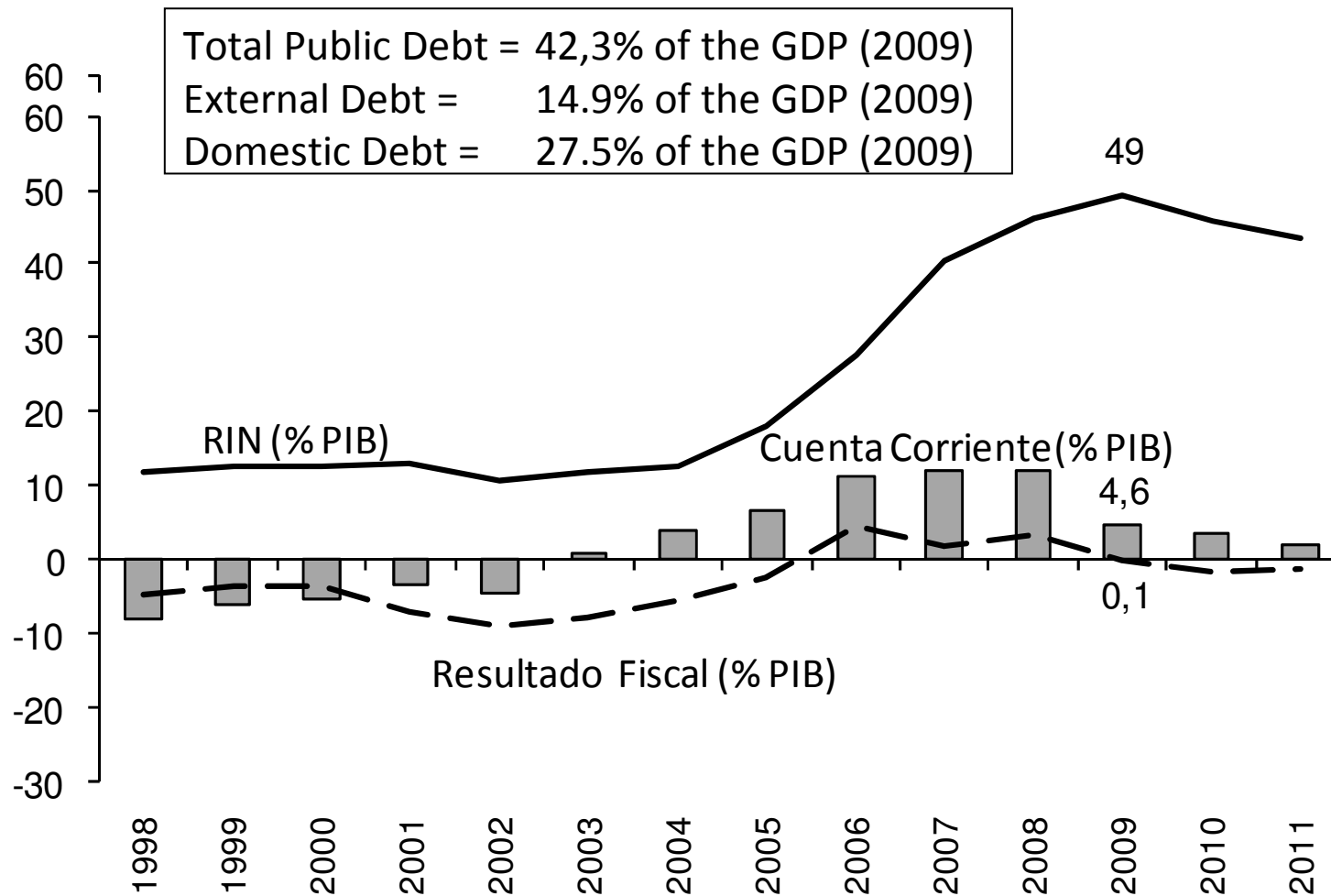


Source: Central Bank of Bolivia

# Low risk indicators

- Sustained increase of international reserves and “twin surpluses” have helped to reduce macroeconomic vulnerability and country risk.

**Bolivia: Risk Indicators**  
(As % of GDP)



# Macro prudential regulation

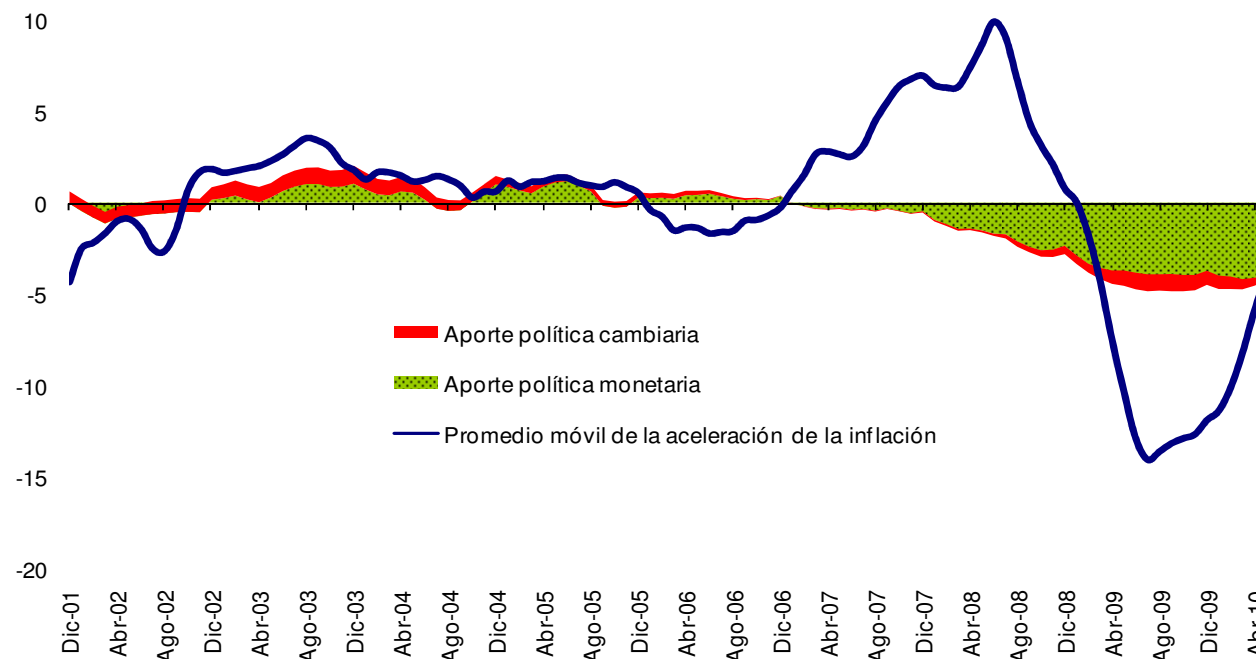
Macro prudential measures were implemented and / or coordinated by the Central Bank, with the Executive Branch and Regulatory Authority of Financial System (ASF):

- Improvement of the formula to calculate a reference rate for financial intermediation (Tre).
- Upper limits to foreign assets of financial institutions.
- Lower loans provision and stimulus for the creation of guarantee funds.
- Implementation of rules for financial institutions to regulate penal interest rates on default circumstances.

# Effects of the central bank policies

- Monetary and exchange rate policies, liquidity regulation, foreign exchange rate revaluation/stability and reserve requirements measures have reduced inflation.

**Estimated effect of Central bank policies on inflation  
(Annual change, %)**

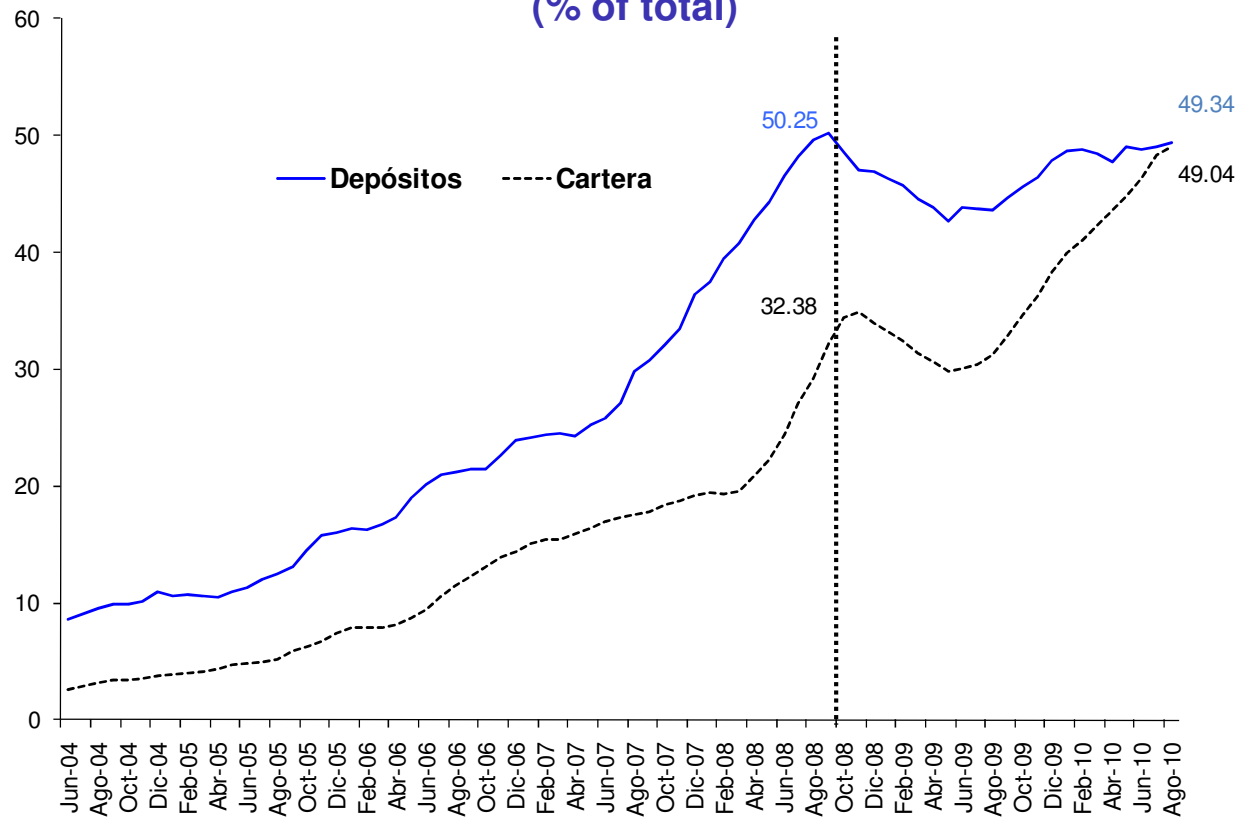


Sources: National Institute of Statistics – Central bank of Bolivia

# Financial “*Bolivianización*”

- With good financial system soundness, “bolivianización” (de-dollarization) has continued, even among the crisis.

Domestic financial intermediation: deposits and loans  
(% of total)



## Bolivian economy's major achievements

- Despite of economic crisis in 2009, Bolivia evidenced the highest growth rate in South America (3,4%), preceded by an exceptional growth in its economic history (6,2% in 2008).
- Despite the economic turbulence, international reserves have continued growing. In fact, Bolivia has the highest level (as a percentage of GDP) of the region.
- Bolivia has recorded a net creditor position since 2008.
- Nationalization of hydrocarbons and fiscal austerity resulted in fiscal surpluses. Similarly, since 2004 there have been current account surpluses. Bolivia was one of the few countries with twin surpluses despite of the global crisis.
- Domestic loans and deposits in the Bolivian financial system have increased. Currently, the “bolivianización” ratio is around 50%.
- Total public debt represents 42.3% of GDP, and public external debt is around 14.9%.

## Reflections and lessons from the crisis

- Price stability should be accompanied by economic growth. Economic progress should also consider GDP`s composition and level. According to the Political Constitution of the Plurinational State of Bolivia, macroeconomic stability is not a goal itself: it is just an instrument that must contribute to the economic and social development.
- Recent economic debates suggested that quantitative inflation targets must be analyzed within the context of new shocks in the global economy. They must allow an proper scope to monetary policy. One objective and one instrument seem to be insufficient, especially in a systemic crisis.

# Reflections and lessons from the crisis

- Besides the explicit aim of price stability, the Central Bank of Bolivia had implicit goals, such as: exchange rate stability, “*bolivianización*” of the economy and financial stability.
- The economic policy implemented in Bolivia before, during and after the crisis has proved to be enough to mitigate adverse effects of global crisis. Moreover, it is adequate for a gradual exit strategy.
- These policies are part of a renewed discussion about current guidelines of macroeconomics and the role of central banks.

## Reflections and lessons from the crisis

- Central banks could include exchange rate stability as a goal. Nevertheless, this policy must be analyzed taking into account specific characteristics of a particular economy. In Bolivia, higher use of domestic currency gave a wider scope for monetary policy. In addition, foreign assets accumulation was an effective mechanism for Bolivian exchange rate policy to deal with external shocks.
- The most valuable lesson for Bolivia from the global crisis is the desirable coordination of monetary and exchange rate policies with fiscal policy. The synchronization of policies and strategies has implied more credibility to maintain low inflation and to preserve macroeconomic stability.



Money and Banking Conference  
Central Bank of Republic of Argentina

# **Monetary Policy in Bolivia**

## **Lessons from the Latest Economic Crisis**

**Gabriel Loza Tellería**  
President of the Central Bank of Bolivia

**Buenos Aires, September 2010**