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**Research Report**

## Poverty reduction strategy papers in Latin America: The case of Bolivia

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**REPORT**

# **Poverty Reduction Strategy Papers in Latin America: The Case of Bolivia**

**Michael Krakowski**

HWWA-Report

**230**

Hamburgisches Welt-Wirtschafts-Archiv (HWWA)  
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# **Poverty Reduction Strategy Papers in Latin America: The Case of Bolivia**

**Michael Krakowski**

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## **1. Introduction**

The international development debate has undergone significant changes during the last decade. The so-called Washington consensus, often described as a focus on macroeconomic adjustment and stabilization policies, has been extended to include a new approach of institution building. Although most developing economies in fact did quite well in terms of macroeconomic stabilization, progress on poverty reduction was judged to be disappointing. The Eighties left a legacy of high levels of indebtedness, and throughout the Nineties one international initiative after another tried to resolve or at least alleviate this problem. When developing countries and international financial institutions agreed on economic policy reforms in the context of loan agreements, it was often felt that the governments lacked real commitment, which was explained by their lack of “ownership.” One of the new instruments to have emerged from the international policy debate is the Poverty Reduction Strategy Paper. This new instrument pursues three objectives: (1) Poverty Reduction Strategy Papers must be drawn up by the governments concerned in a participatory process, intended to assure national consensus and ownership. (2) It is hoped that the explicit focus on poverty reduction will improve results in this area. (3) And if the international community accepts a country’s PRSP, a high percentage of outstanding debt will be written off by bilateral and multilateral donors within the HIPC (highly indebted poor countries) initiative.

The international community is watching this new approach closely. Many conferences and assessments by the international financial institutions, the bilateral donors and civil society organizations mirror this interest. Of the 26 countries (Albania, Benin, Bolivia, Burkina Faso, Cambodia, Ethiopia, Gambia, Ghana, Guinea, Honduras, Kyrgyz Republic, Malawi, Mali, Mauritania, Mozambique, Nicaragua, Niger, Rwanda, Senegal, Sri Lanka, Tajikistan, Tanzania, Uganda, Vietnam, Yemen, Zambia) that have

completed their first full PRSPs,<sup>1</sup> three are highly indebted Latin American countries. Bolivia completed its strategy in March 2001, and the joint staff of the World Bank and International Monetary Fund proposed the acceptance of the strategy to their boards in May 2001.

This study aims to provide a preliminary appreciation of Bolivia's PRSP. It is too early as yet to evaluate the results of the strategy. Instead, the study analyzes past policies and the past performance of Bolivia's economy in order to detect the shortcomings which ought to be addressed by a PRSP. Then Bolivia's PRSP is evaluated in the light of this analysis. This leads on to some points of criticism which may be taken into account by international donors in their respective country strategies for Bolivia.

This study focuses on poverty reduction, and policies are assessed according to their appropriateness to that purpose. It seems that sustainable poverty reduction without economic growth is not feasible; a large and still growing number of empirical studies supports this hypothesis. However, similar growth rates in different countries have reduced poverty to differing degrees, i.e. the poverty reduction elasticity of per capita growth is far from uniform. Poverty will be measured in this paper by a poverty headcount index, i.e. the proportion of the population living below a particular poverty line. Different definitions of the poverty line and scarce data of varying quality render international comparisons difficult. Nevertheless, the available evidence indicates marked differences in the poverty reduction elasticity of economic growth.

If this elasticity is high, growth is quite often described as "pro-poor." "Pro-poor growth" will be defined in this context as a growth process in which growth of per capita income among the poor exceeds growth of per capita income for the non-poor. If

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<sup>1</sup> As of March 2003.

income were uniformly distributed among the population below the poverty line, poverty reduction elasticity would be  $-1$  if income also increased by the same percentage throughout the population. As this is not generally the case, pro-poor growth is consistent with different poverty reduction elasticities. In countries with higher average GDP per capita, more of the poor might be expected to live close to the poverty line, making the “poverty gap” smaller, and the elasticity of poverty reduction accordingly higher. At least in Latin America this is not the case.<sup>2</sup>

This highlights the importance of income distribution. Distribution is often measured by the Gini coefficient, which mirrors overall income distribution. In the context of poverty reduction strategies this cannot be considered an appropriate measure for two reasons. First, changes in distribution which affect only the higher quintiles of income distribution do not affect the extent of poverty. Second, the international community is interested in the eradication of poverty, as laid down in the millennium goals (Organization for Economic Cooperation and Development 2001, p. 12) but not in income distribution in itself. Individual societies may have different norms and values regarding the distributions that are acceptable or unacceptable. This study therefore concentrates on income distribution within the poor sections of society, and on the share of total income earned by the poor.

Government welfare expenditure may play an important role in rendering growth more pro-poor. However, not only the scale of redistribution due to state activities is of importance, but also the quality of policy design and implementation. In general terms, there is a consensus on important aspects of design, for example favoring basic education in rural areas over higher education in the urban centers or basic health services over sophisticated hospitals. Optimal institutional design may nevertheless

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<sup>2</sup> The correlation coefficient between poverty reduction elasticity of per capita growth and average GDP

depend on local experience and therefore be path-dependent. It is extremely difficult to judge this point or the quality of implementation without exhaustive field studies.

In order to evaluate policy outcomes, the study will compare progress in Bolivia to that in other countries. Given the high cultural and historical diversity among developing countries, prime consideration is given to the Latin American context. Bolivia is classified as a lower middle income country by the World Bank. The other two Latin American Highly Indebted Poor Countries with PRSPs (Honduras and Nicaragua), are low income countries. Thus Latin American low and lower middle income countries are often used as a peer group for comparisons in this study.<sup>3</sup>

## **2. The Bolivian Economy**

### **2.1. Economic Structure**

Bolivia is one of the poorest countries in the western hemisphere. Only Nicaragua and Haiti have lower GDP per capita. Bolivia is endowed with some important natural resources. Extraction of oil and gas and also of ores (zinc, gold, silver, copper) amounted to 7% of GDP in 1999. The weight of these sectors increased at the beginning of the Nineties and is currently roughly constant. Manufacturing is less important than in other Latin American lower middle income countries (see Table 1). Indeed, its share of GDP decreased during the Nineties. One third of manufacturing is accounted for by food and beverages, whereas chemical products and clothing amount to 5% each. Agriculture is also less important than in other Latin American lower middle income countries, and saw its share of GDP diminish in the same period. Besides subsistence farming, growing and processing soybeans is a prominent feature in the sector.

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in the Nineties for 12 Latin American countries with available data is  $-0.09$ . See also appendix chart 1.

<sup>3</sup> Cuba and the smaller Caribbean islands are excluded in this context.

Financial services is the sector which expanded most during the Nineties; it reached 16% of GDP in 1999, a high value compared with other developing countries. Transport and communications also grew in relative importance. The weighting of the government sector increased in current prices but decreased in real terms, showing the rising relative cost of labor in government. The construction and the energy and water industries expanded moderately, whereas wholesaling and retailing contracted.

Table 1: Bolivia: Economic Structure and Comparison with Lower Middle Income and Latin American Countries

	Gross domestic product 1999 (at current factor prices) Bolivia	Gross domestic product 1999 (at current factor prices) Lower Middle Income Countries	Gross domestic product 1999 (at current factor prices) Latin America and Caribbean
Agriculture, hunting, forestry and fishing	14.36%	14%	8%
Industry	30.66%	39%	30%
Mining, quarrying and petroleum	6.77%		
Manufacturing	16.73%	28%	21%
Electricity, gas and water	3.11%		
Construction	4.04%		
Services	54.99%	46%	62%
Wholesaling and retailing	7.80%		
Transport, storage and communications	13.58%		
Finance	15.64%		
Public administration	13.71%		
Other services	4.25%		

Source: Instituto Nacional de Estadística de Bolivia (2002), World Bank (2001)

## 2.2. Structure of Foreign Trade

The structure of Bolivian foreign trade mirrors the weight of mining in GDP. Gas, zinc, gold, silver, copper and petroleum are the main export products. The dominant agricultural export products are soybeans and processed soya. Within the manufacturing sector, exports of clothing and handicrafts have increased in recent years.

As gas is transported by pipeline, the principal clients are the neighboring countries, mainly Brazil and Argentina. These two countries also buy most of Bolivia's petroleum exports. Exports of liquefied gas are planned for the future to the north American markets. More than half of Bolivian exports go to neighboring countries; exports to industrialized countries are relatively small (See Annex Table 1).

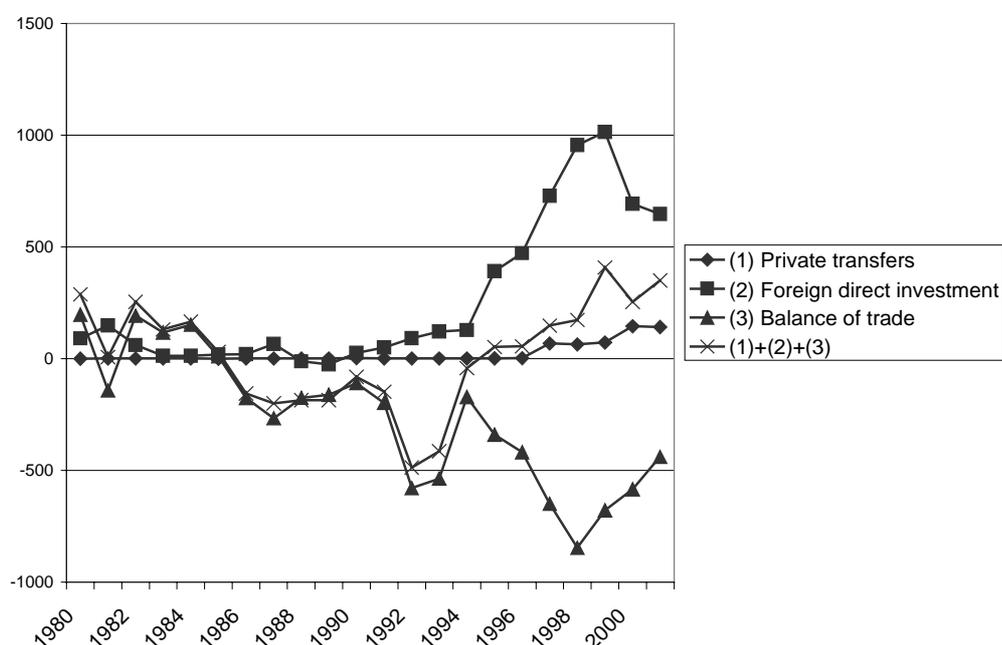
Exports of goods and services expanded in proportion to GDP after the introduction of new economic policies in the mid-Eighties but stalled in the early Nineties; by 1999 they had fallen to their lowest level since 1960.<sup>4</sup> Imports nevertheless increased rather steadily until 1998, but decreased afterwards reflecting the economic slowdown. The trade deficit expanded substantially and reached 12% of GDP before narrowing again due to both lower imports and slightly increased exports, gas exports being particularly strong.

Privatization of state-owned enterprises during the Nineties induced high inflows of foreign direct investment, which helped balance the trade deficit. Lately investment in gas pipelines to Brazil has been an important source of foreign investment. Nevertheless, privatization is a nonrecurring event and these inflows have diminished in recent years. On the other hand, as private transfers started to become more important, a new means of financing the trade deficit emerged. Foreign companies now invest mainly in petroleum and gas extraction, refining and transport. Thus the dominant position of minerals and mining in the Bolivian economy similarly applies to FDI (See Annex Chart 4).

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<sup>4</sup>As Schweickert notes: *Export expansion has been undermined by terms-of-trade shocks as well as a strong currency due to disinflation and privatization triggering strong inflows of foreign direct investment* (Schweickert 2001, p. 35)

Chart 1 Bolivia: Balance of Payments 1980–2001 (USD millions)



Source of data: World Bank (2001), Banco Central de Bolivia (2002a)

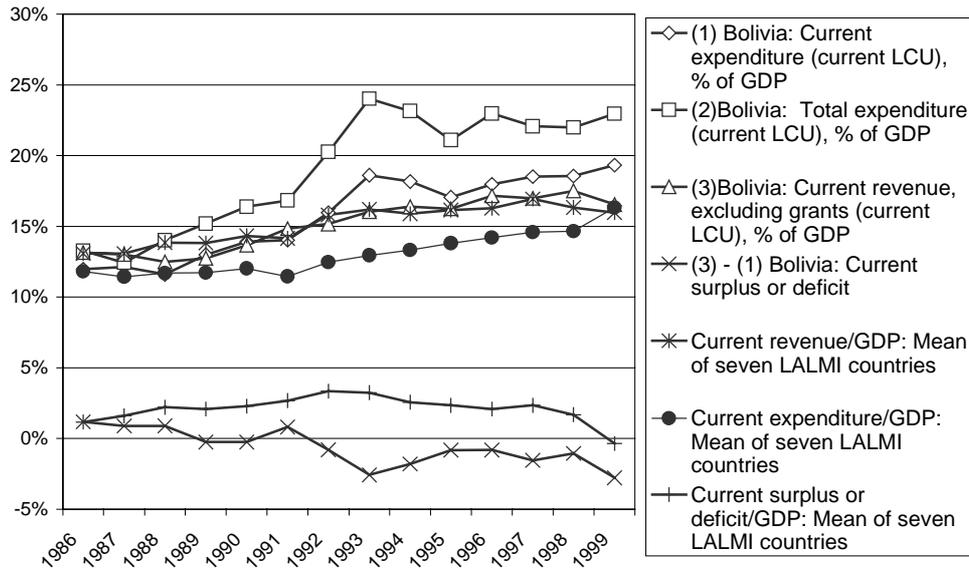
### 2.3. Budget

Central government expenditure as a proportion of GDP in Bolivia increased rapidly during the second half of the Eighties and the early Nineties. After dipping until 1995 it then stabilized at around 23%. Tax revenue as a percentage of GDP also expanded, but after 1992 it did not keep pace with expenditure. After narrowing in 1994 and 1995, the deficit expanded again until 1999, and reached nearly 3% of GDP. This trend continued in 2000 and 2001 (Banco Central de Bolivia, 2002).

If current revenue in Bolivia is compared to other Latin American lower middle income countries, the results for tax pressure are similar. Nevertheless, Bolivia's expenditure as a proportion of GDP is higher than in its peer group, thus leading to a higher current deficit (or smaller current surplus). In Bolivia as well as in a group of seven other Latin

American lower middle income countries, the share of central government expenditure in total GDP increased substantially over the period under review.

Chart 2 Bolivia and Seven Latin American Lower Middle Income Countries: Central Government Revenue and Expenditure (1986–1999)



Source: World Bank (2001)

## 2.4. Population and Employment

Bolivia still has strong population growth, but at a decelerating rate. Thus the dependency ratio, i.e. the relative number of dependents that the population in working age is required to support, is falling. This benign situation presents an opportunity to improve education and introduce pension schemes — an opportunity which ought to be grasped.<sup>5</sup> GDP per capita growth resumed after the mid-Eighties, but part of this growth may be explained by the improving age profile of the population. In 1999 GDP per capita declined by nearly 2%, in 2000 it remained unchanged and in 2001 it declined again (Banco Central de Bolivia 2002a, p. 11).

<sup>5</sup> In Bolivia proceeds from privatization were used to build up pension funds.

Bolivian statistics provide employment figures only for urban areas. Official statistics indicate a decline in urban unemployment during the first half of the Nineties, and a significant deterioration in later years as the economy contracted (PRSP, p. 38., CEPAL 2001, p. 105). Overall growth was supported by trends in the age composition of the population and increasing employment until 1995.

Table 2 Bolivia: Urban Employment by Sector 1989 and 1997

	1989	1997
Employment in the public sector	24%	11%
Employment in the enterprise sector	25%	28%
Employment in the semi-entrepreneurial sector	10%	15%
Self employment	33%	42%
Domestic service	8%	4%

Source: Bolivia PRSP p. 39

Patterns of urban employment changed dramatically between 1989 and 1997. The change was dominated by the process of privatization, which cut the proportion of public-sector employees by more than half. Employment in the semi-entrepreneurial sector and self employment were the main winners in this process, reflecting the growing importance of micro and small enterprises in Bolivia.

## 2.5. Poverty and Distribution

Poverty data for Bolivia are quite poor. Time series are available only for the major urban centers, starting in 1986. According to the poverty headcount index, urban poverty increased until the end of the eighties — possibly due to tight stabilization policies in these years — and started to decline at the beginning of the nineties. Extreme poverty followed the same pattern. Poverty and extreme poverty in the rural areas are much higher than in the urban centers. Between 1997 and 1999, the only two years for which data are available, rural poverty actually increased.<sup>6</sup>

<sup>6</sup> Poverty lines were calculated on the basis of the construction of the basic food baskets and the estimation of nonfood needs valued at the prices prevailing in each area. The poverty Headcount Index assesses the percentage of the population whose income is below the poverty line. Extreme poverty is the percentage of the population whose income is below the cost of a basic food basket.

Table 3 Bolivia: Headcount Index of Poverty and Extreme Poverty in Major Cities, 1986–1997 (per cent)

Year	Poverty	Extreme Poverty
1986	52	22
1989	54	23
1989	59	30
1990	58	29
1993	52	24
1997	51	21

Source: Bolivia PRSP, p. 36.

Table 4 Bolivia: Headcount Index of Poverty and Extreme Poverty (per cent)

Year	Total		Urban		Rural	
	Poverty	Extreme poverty	Poverty	Extreme poverty	Poverty	Extreme poverty
1989			53.1	23.3		
1994			51.6	19.8		
1997	62.1	37.2	52.3	22.6	78.5	61.5
1999	60.6	36.5	48.7	19.8	80.7	64.7
2000	60.6	36.5				
2001	61.2	37.3				

Source of data: CEPAL (2002), pp. 4, 217.

An analysis of unsatisfied basic needs corroborates the substantial gap between rural and urban quality of life, which increased further between 1992 and 2001. The main improvements that have occurred are in education and access to water and sanitation.

Compared to other Latin American countries with similar income levels, rural poverty is higher in Bolivia and urban poverty is lower. This underlines the insufficient participation of rural Bolivia in the growth process, the more so as poverty in these areas has actually increased in the last few years. The decline of poverty in urban areas in the Nineties was related to an overall increase in per capita income. If progress in Bolivia is compared with that of other Latin American countries, the elasticity of poverty reduction with respect to growth in per capita income is found to be at the lower end of the range (see Chart 6).

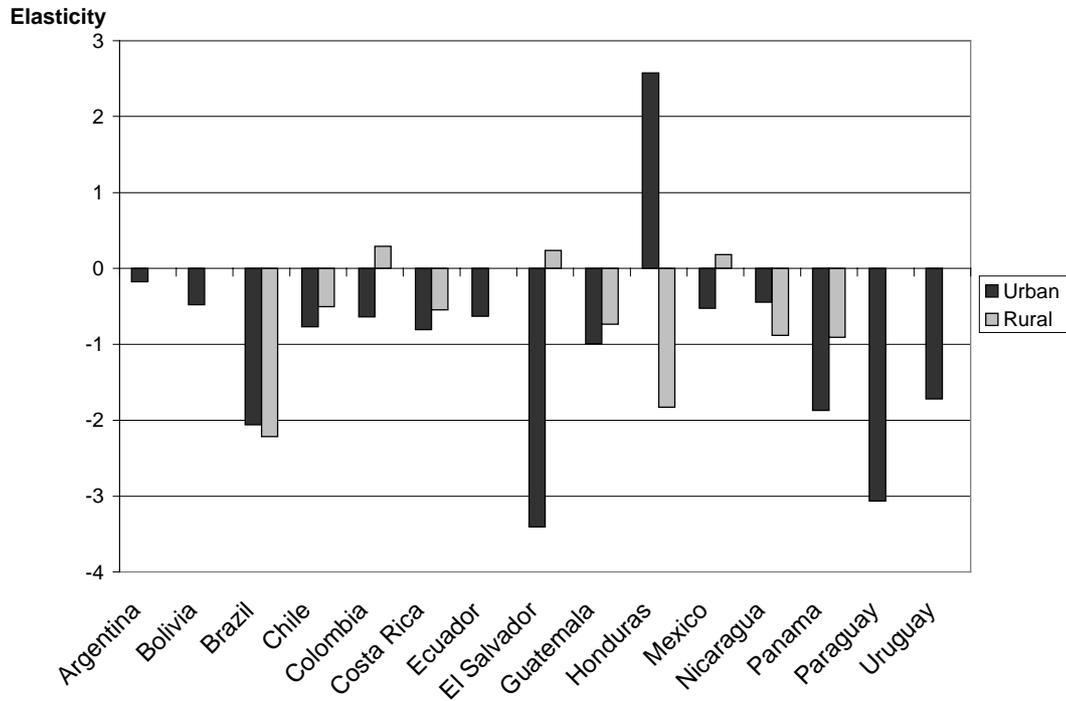
Table 5 Bolivia: Unsatisfied Basic Needs

	Urban		Rural	
	1992	2001	1992	2001
Quality of construction	22.5%	15.6%	83.5%	75.7%
Available space for living	76.3%	68.9%	85.1%	76.3%
Water and sanitation	60%	44.3%	97.6%	78.9%
Energy supply	21.2%	14.1%	93.8%	91.2%
Education	53.9%	36.5%	90.1%	70.9%
Health	44.2%	31%	66.6%	54.5%

Source: Instituto Nacional de Estadística (2001)

One of the reasons for this disappointing performance seems to be a lack of continuity in economic performance, be this due to policy shifts or to external policy shocks. Chart 4 illustrates the relationship between per capita income and poverty in Latin American countries (available data between 1990 and 1999). Whereas some countries like Panama, Costa Rica or Uruguay managed a relatively stable economic performance during the period under observation and increased per capita GDP and decreased poverty steadily, others like Honduras, Paraguay, Mexico or Bolivia suffered substantial backlashes in their process of poverty reduction. One of the most promising short-term policy recommendations for successful poverty reduction is a policy that is able to avoid such backlashes.

Chart 3 Latin America: Elasticity of the Proportion of Poor Relative to Per Capita GDP  
(constant 1995 USD)



Source of data: CEPAL (2001)

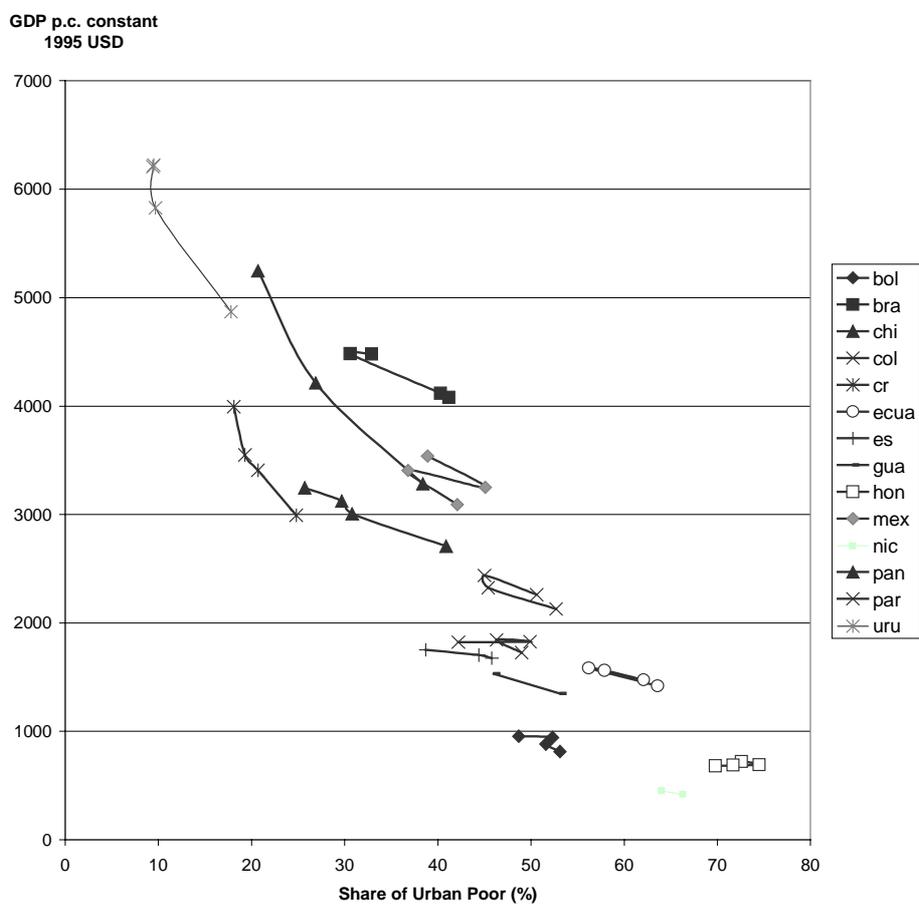
Poverty may also decrease if the distribution of income improves, allowing poorer households a greater share in national income. The share of the 40% poorest households in Bolivia's total income was the lowest of all the Latin American countries for which CEPAL reports data (in 1999).<sup>7</sup> Based on a social accounting matrix analysis using 1997 figures, Thiele and Piazzolo report that:

- *Smallholders and urban informals together account for about two thirds of the total labor force, but for less than a quarter of total income;*
- *the richest household group (employers) receives slightly more than ten times the income of the poorest household group (smallholders);*

<sup>7</sup> The outcome does not appear as bad if one considers the Gini coefficient instead of the income share of the poorest 40%. But as the Gini reflects overall income distribution, not only that of the poorest, it is a less helpful indicator if poverty reduction is the main objective (See CEPAL, 2001, p p. 69-72).

- *disparities in the distribution of wealth are even somewhat wider, with employer's net assets exceeding those of smallholders by a factor of 15;*
- *the poor household groups are characterized by low savings, low investment, and a low participation in the financial system. (Thiele, Piazzolo 2002, p. 41)*

Chart 4 Latin America: Share of Urban Poor and Per Capita GDP, 1990–1999 (constant 1995 USD)



Source of data: CEPAL (2001), World Bank (2001)

Available data indicate that the share of total income going to the 40% poorest households was still diminishing in the Nineties. Clearly any economic policy which seriously aims to reduce poverty must reverse this trend.<sup>8</sup>

Income is just one indicator of poverty. If other dimensions of exclusion are taken into account, we note that

- 14% of the population cannot read or write, with illiteracy rates reaching 34% in rural areas
- more than 20% of the population do not have access to safe water
- life expectancy at birth is only 62 years
- infant mortality is 59 per 1,000 live births
- enrollment in primary schools is 93%.

Reasons for high rural poverty mentioned in Bolivia's PRSP include (Bolivia PRSP pp. 41-42)

- Low agricultural productivity due to insufficient production infrastructure, low quality of seeds and inputs, limited investment, and an unskilled labor force
- small land holdings
- uncertainty and inefficient land use due to unclear ownership rights
- water shortage due to the lack of physical infrastructure and unclear ownership rights
- high transport costs
- asymmetrical information about prices and quantities in agriculture, creating high margins for intermediaries.

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<sup>8</sup> *Between growth and inequality, no significant statistical relationship can be identified for Bolivia.* Thiele (2001), p. 26.

## 2.6. Bolivia's Structural Economic Advantages or Disadvantages

A country's structural economic advantages or disadvantages result mainly from geography, size, availability of natural resources and the long-term international framework which interacts with these factors.

### 2.6.1. Geography

Bolivia is located in the center of South America and is a landlocked country. Roughly half of the country lies in the Andes. La Paz has the highest elevation of all the world's capital cities. The other half of the country comprises tropical lowlands. Transportation of its products onto international markets is difficult and costly. Bolivia's natural trading partners are therefore its South American neighbors. The main agricultural products, determined by the country's geographical location, are soybeans and coca. Coca production has traditionally been an important source of revenue in the rural areas. To what extent this is still the case is not quite clear. Government campaigns to diminish coca production have had limited success. Not having any coast or beaches, Bolivia is not a typical tourist country.

### 2.6.2. Size

Bolivia's economy is quite small. Because of the limited home market, few industrial enterprises have been able to reach a minimum optimal scale of production by selling their products into this market alone. If economic policy protects domestic producers by applying import duties, thus allowing them to operate at a profit, consumers subsidize this production and pay high prices, and producers in the downstream parts of the value chain have to pay higher prices for semi-manufactured goods. Apart from certain limited investment opportunities in the food and beverages sector, Bolivia will not be able to attract investment in industry unless there is access to other regional and

international markets. Thus the opening up of these markets is of paramount importance for Bolivia.

### 2.6.3. Natural Resources

Bolivia is endowed with important natural resources, namely tin, zinc, copper, gold and silver; in the Seventies, oil and gas were also discovered. As oil production has diminished in the meantime, gas is now the most important export product. More than 40% of Bolivian exports are natural resources such as metals, oil and gas.

### 2.7. Bolivia's Place in the Process of Globalization

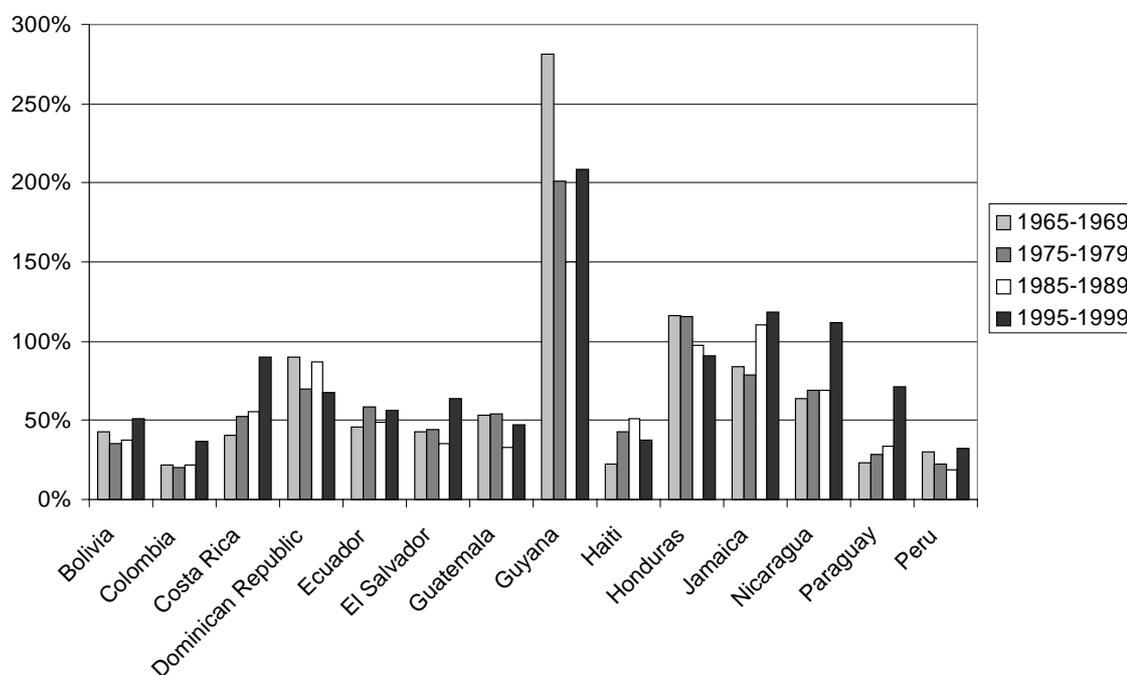
Globalization is a process of *growing integration of economies and societies around the world as a result of flows of goods and services, capital, people, and ideas*. (Dollar 2002, p. 1) The key issue for purposes of poverty reduction is whether the degree of globalization of a particular economy is positively linked to growth and/or the distribution of income. The prevailing opinion nowadays is that a positive link does exist between globalization and growth,<sup>9</sup> whereas none can be identified between globalization and distribution.

Dollar compares his measure of globalization (increase in trade) with the development of overall per capita growth and finds a positive relationship. Correlation between overall per capita growth and per capita growth of poor people's incomes is also significant — on average, a one-to-one relationship is detected — but there is substantial variation around that average relationship. What these results effectively tell us is that changes in the distribution of income are not systematically associated with the growth rate (or globalization) itself ( Dollar 2001, p. 33).

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<sup>9</sup> Frankel and Rohmer (1999) identify a positive influence of trade on income. As Levine and Renelt note, this may be due to a positive correlation between the quality of institutions and trade, and good institutions foster growth ( Levine, Renelt, 1992). Proponents of a positive linkage between trade and

Chart 5 Latin American Lower Middle Income Countries: Trade as a Percentage of GDP 1965–1999 (1995, constant USD)



Source of Data: World Bank (2001)

If a country participates increasingly in the process of globalization, better technology, more knowledge and higher levels of competition can be expected to result. The symbiosis between factors of production improves, and total factor productivity may increase. This process triggers higher growth in the economy.<sup>10</sup> Not only the productive sectors benefit from globalization: It also appears that the quality of national institutions is positively affected. This makes sense in as far as knowledge and competition with

growth are Dollar, Kraay (2001) and World Bank (2002). For a critical view on this relationship, see Rodrik (2000) and Rodríguez, Rodrik (2000).

<sup>10</sup> As Robles notes in the Central American context: *Statistically, there is a strong positive relationship between openness and TFP growth in all countries.* (Robles 2000, p. 47). This result nevertheless is not generally valid. As Grossman and Helpman note: *Does trade promote innovation in our model of the small economy? The answer is, 'It depends.'* When trade causes resources to be released from the manufacturing sectors, which then find their way into research labs, the rate of innovation rises. But when the sectors that expand in response to trading opportunities compete with the research labs for factor inputs, international integration may retard growth. (Grossman, Helpman, 1991, p. 152). The empirical literature deals with the question of which of the two effects generally occurs.

foreign institutions would be expected to help improve the design of institutions and the implementation of policies.

Trade, international capital flows and migration may be considered the key dimensions of globalization. Trade as a percentage of GDP increased in Bolivia during the Nineties. Nevertheless, compared with other Latin American lower and lower middle income countries its level remained modest and its increase was lower than the average (Chart 8). Bolivia, then, is not one of Dollar and Kraay's "new globalizers."<sup>11</sup>

A quite different picture emerges from the analysis of FDI. The strong increase in FDI into Bolivia during the process of privatization was already mentioned. Net inflows as a share of GDP reached very high levels in Bolivia if compared to other Latin American countries (World Bank, 2001)). Their dynamics were less impressive, but Bolivia continued to experience high relative growth in FDI during the Nineties. It was mentioned earlier that FDI inflows in Bolivia started to decrease in 2000 and that, having been triggered by privatization, they are likely to decrease further in the future. There are no migration data available for Bolivia, but the increase in worker remittances offers evidence of increased emigration in the Nineties.

Bolivia's trade is still dominated by exports of natural resources and one cash crop, whereas industrial products are imported. The future of this trade pattern seems limited, as does the positive impact of globalization via trade. FDI has increased rapidly, but again the positive effects in the case of investment in the exploitation and transport of natural resources seem limited: They are not coupled with any increase in competitive pressure within the domestic economy, and offer scant technology transfer to other sectors of the economy. In the case of finance and telecommunications, FDI may

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<sup>11</sup> Dollar and Kraay use the increase of trade to GDP as indicator for globalization of an economy (Dollar, Kraay 2000, pp. 36, 37).

increase overall economic performance, as these are important input sectors for the economy as a whole.

## 2.8. Governance

Bolivia has the reputation of being a country that followed in the past the advice of the international financial institutions closely and has a relatively good governance track record. This is one of the reasons for early acceptance of the completion point within the HIPC framework by these institutions. Bolivia was not required to fulfill the one year time span of successful implementation of the PRS stipulated in the enhanced HIPC initiative before obtaining debt relief. In order to appreciate if governance in Bolivia really is better than in other Latin American countries different aspects of governance in Bolivia are compared with other Latin American countries. The focus is on Spanish and Portuguese speaking major countries, thus eliminating countries of a different cultural heritage.

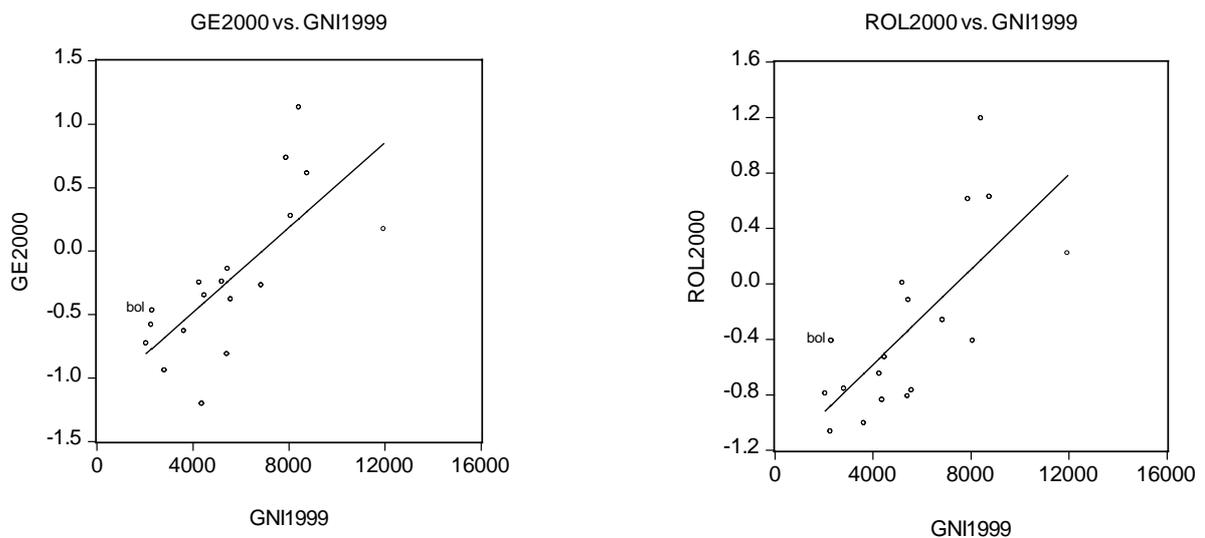
For this analysis the Kaufmann-Kraay-Zoido-Lobatón dataset is used. They provide data for 160 countries on „Voice and Accountability“, „Political Stability“, „Government Effectiveness“, „Regulatory Quality“, and „Rule of Law“, derived from several surveys and aggregated using an unobserved components model (Kaufmann, Kraay, Zoido-Lobatón 1999). Because a higher living standard often is associated with better governance, Bolivia’s performance will be classified as better as the average of Latin America, if the indicator lies above the line of a simple regression between gross national income per capita on a purchasing power parity basis and the indicator.<sup>12</sup>

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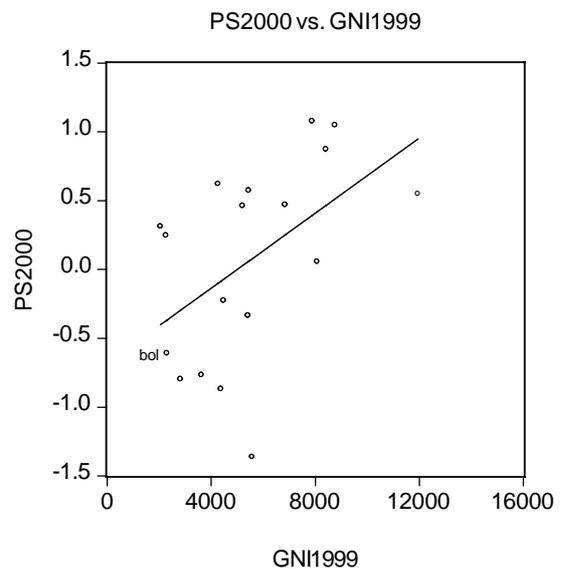
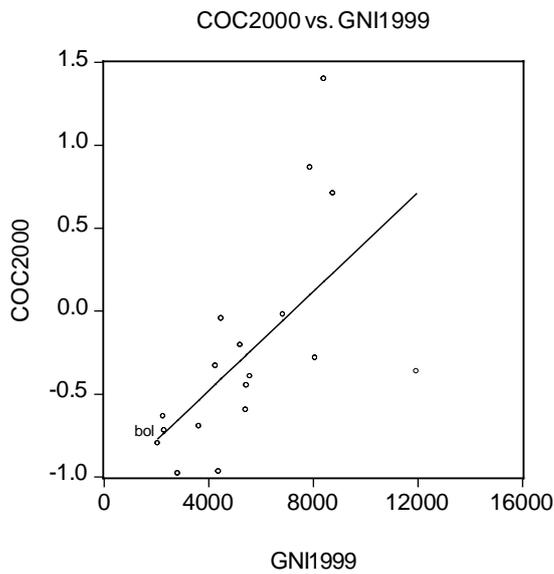
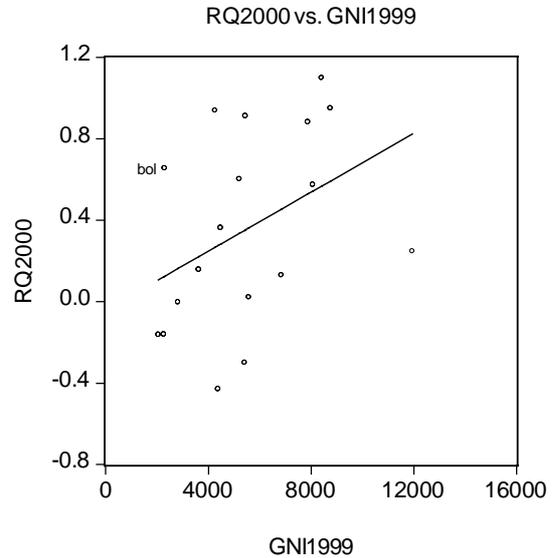
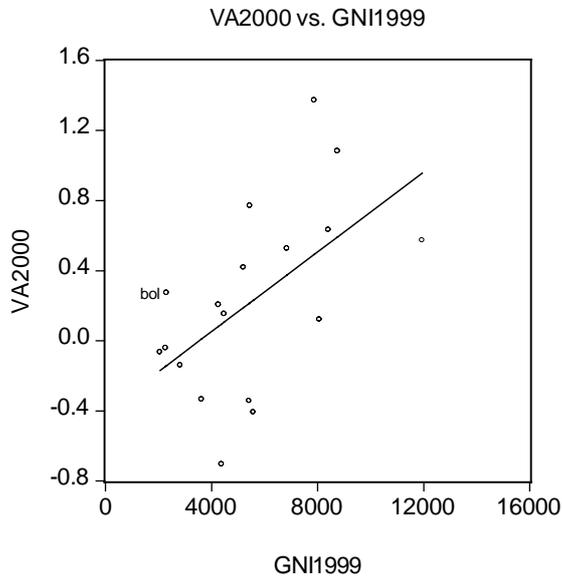
<sup>12</sup> One of the findings of Kaufmann and Kraay using this dataset is that governance seems to influence per capita income positively, but per capita income governance negatively. They provide some kind of intuitive explanation for this surprising result, but certainly more analysis is warranted. See Daniel Kaufmann and Aart Kraay: Growth without Governance,

Using the 2000/1 dataset, Bolivia fares better than the Latin America average with respect to most of the indicators, corruption is similar to the rest of the continent and political stability is judged to be lower (chart 6). The aforementioned social unrest due to coca eradication and privatization probably is responsible for this outcome. On the whole this analysis seems to corroborate the conventional view of – relatively - good governance in Bolivia. But in the past the relative position of Bolivia has even been better, as a matter of fact all of Bolivia’s governance indicators deteriorated sharply between 1997/8 and 2000/1, the two dates for which the dataset provides data (chart 7)<sup>13</sup>.

Chart 6 Governance Indicators: Relative Position of Bolivia in Latin America



<sup>13</sup> This hold also, if differences in gross national product per capita are taken into account.

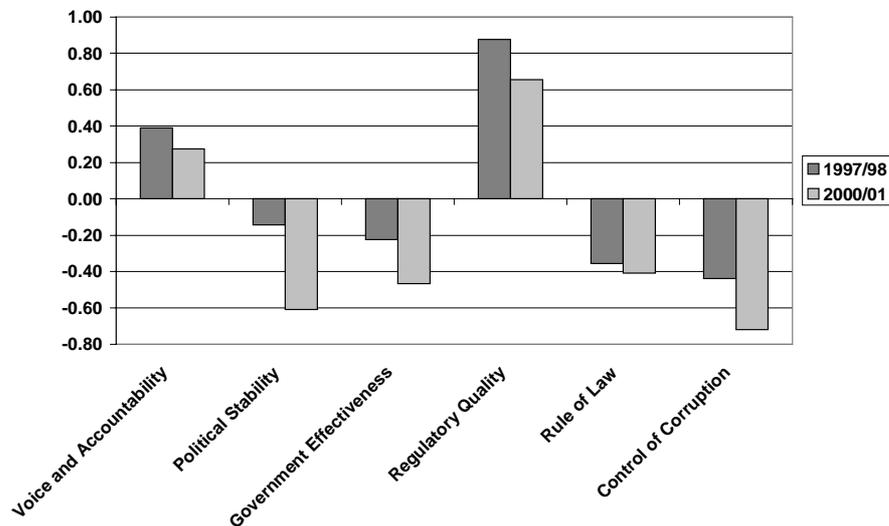


Voice and Accountability: VA, Political Stability: PS, Government Effectiveness: GE, Regulatory Quality: RQ, Rule of Law: ROL, gross national income per capita on a purchasing power parity basis: GNI, Source of Data: Kaufmann, Kraay, Zoido-Lobaton, (2002), World Bank (2001)

Elaboration of the Bolivian PRSP thus happened during a period of deteriorating governance indicators; and the political situation in Bolivia seems to have worsened even more during the last months. Social and political unrest due to announced tax increases led to 33 dead and 173 wounded in February 2003 (La Prensa, 2003). The budget deficit was reduced less and new debt was higher than planned as a consequence, thus increasing the risk of fast accumulation of new debt and an again unsustainable degree of indebtedness even after receiving debt relief according to the

HIPC initiative. This is an example that a good track record of the past is not necessarily an indicator for future performance.

Chart 7 Bolivia: Indicators of governance, 1997/98 and 2000/01



Source of Data: Kaufmann, Kraay, Zoido-Lobaton, (2002), World Bank (2001)

### 3. Past Policies

#### 3.1. Macroeconomic and Stabilization Policies

After 1985 Bolivia introduced major structural reforms and institutional changes in order to promote stability and economic recovery. The government and authorities took action to liberalize markets for goods and factors, open the economy to foreign trade, and liberalize the financial system:

- The fiscal measures reduced expenditure and increased tax revenue to narrow the deficit. A tax reform was applied, under which the number of taxes was reduced, collection mechanisms simplified, the tax base broadened, and special regimes established which favored small-scale rural property ownership and small taxpayers.
- Market liberalization began with government deregulation of domestic prices. On the labor market side, flexibility was enhanced by deregulating hiring and by consolidating special bonuses into the basic wage.

- Tariff dispersion was eliminated, quasi-tariff barriers were reduced, and a system of customs duties featuring low, uniform rates was adopted, thus opening the economy to foreign trade and reducing the production costs of tradables. To promote exports, and particularly nontraditional ones, mixed institutions were established to support the export sector. Measures such as the drawback certificate were introduced to enhance producers' competitiveness.
- A single exchange rate using the crawling peg mechanism was established and foreign exchange was allocated through auctions.
- Free movement of capital was established and interest rates were liberalized. The central bank was reorganized to give it autonomy in the management of monetary and exchange-rate policy, and a Superintendency of Banks was established. A Law on Popular Ownership and Credit was promulgated to enhance microcredit activities. Sectoral provisions such as the Mining Code, Hydrocarbons Law, and the Laws on Forestry and the Environment were approved.
- The Laws on Privatization and Capitalization made it possible for businesses in the energy, hydrocarbons, communications, and transportation sectors to attract foreign capital. The Law on Popular Ownership and Credit promoted this process and had social and redistributive effects, giving the employees a stake in their enterprises through pension funds and the collection of life annuities.

### 3.2. Financial Sector

In 1987 a financial sector reform took place in Bolivia in order to improve regulation, supervision and support for the banking sector. In 1993 a General Banking Law was approved by Congress, in 1995 a new Central Bank Law, in 1998 a Law on Securities Markets in order to develop the local securities exchange as well as a Law on Property and Popular Credit to increase microcredit and improve conditions for microbusinesses. In 2001 the supervisory role of the Central Bank was strengthened (Ley de Fortalecimiento de la Normativa y Supervisión Financiera).

In the early Nineties the state withdrew from commercial banking activities (Jemio, 2001 p. 167). Five private and three state-owned banks had to be liquidated in the Eighties (Loubière, 2000 p.138) and two more banks were liquidated by the Superintendency of Banks in 1994, mainly because of fraudulent operations carried out by the shareholders. In 1997 and 1999 the Superintendency intervened with regard to two more banks. Because no guarantee fund for the public's deposits existed, the government guaranteed these deposits for reasons of economic and social stability. After 1994 — probably in part due to the banking failures — the process of monetary intermediation in Bolivia slowed down. Nevertheless M2 as a percentage of GDP reached one of the highest levels in Latin America.<sup>14</sup> There are currently twelve banks established in Bolivia, three of which are of foreign origin. The degree of dollarization of deposits is high: 95.0% of fixed term deposits, 95.6% of savings deposits and 80.7% of current deposits are held in US dollars (End of March 2002, Banco Central de Bolivia 2002b)

### 3.3. Institutional Changes

Institutional changes focused on government reform including decentralization, and strengthening the judicial system.

- Under the Law on Popular Participation, resources were transferred to the municipalities, which were delegated the responsibility to provide and administer basic services. Each year 20% of sharable tax revenue is transferred to each municipality according to a formula commensurate with its population. The law also established monitoring mechanisms acknowledging the significance of grassroots territorial organizations. The Law on Administrative Decentralization delegated technical and administrative functions to the departmental prefectures.

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<sup>14</sup> In 1999 M2 as percent of GDP in Bolivia was surpassed only by Panama, Nicaragua and Chile (among principal Latin American Countries ( World Bank 2001).

- Despite the progress made in decentralization, municipal governments still lack capacity for public management and the participatory mechanisms that were established have been insufficient to ensure full participation for both urban and rural municipalities.
- A Constitutional Court, the Judicature Council — an administrative and disciplinary body of the Judicial Branch — and the Office of the Ombudsman were created, to enhance reliability and independence of judicial process and to guarantee citizens their rights and liberties. A new Criminal Procedures Code and Civil Procedures Code were also promulgated.
- Customs Reform, Civil Service Program, Civil Service Staff Regulations, and institutionalization of the Internal Revenue Service were all carried out to improve transparency in public administration.

#### 3.4. Social Policies

In the late Eighties economic stabilization was the priority public-policy objective during structural adjustment, and, with few exceptions, this did not involve any social policy agenda (Bolivia PRSP, p. 24). However, in the early Nineties it was found that low human capital levels had constituted the major obstacle to economic growth, which highlighted the concern and need for placing social and poverty reduction issues on the agenda. In the mid-Nineties, policies were developed in a human development context, with emphasis on the themes of citizenship and participation. The focus was placed on the close relationship between capacity and market access, access to justice, and the role of institutions, resulting in the decision to pursue the decentralization strategy referred to earlier.

### 3.4.1. Overall Social Expenditure

The share of current expenditure earmarked for the social sectors rose from 12.3% of GDP in 1994/95 to 16.1% in 1998/99 (see Table 6) and social expenditure as a proportion of total expenditure rose from 49.4% to 56.5%. These proportions are higher than the average in other Latin American countries.<sup>15</sup> Within the social expenditure category, health spending declined in relative terms while that on education increased during the period under review.

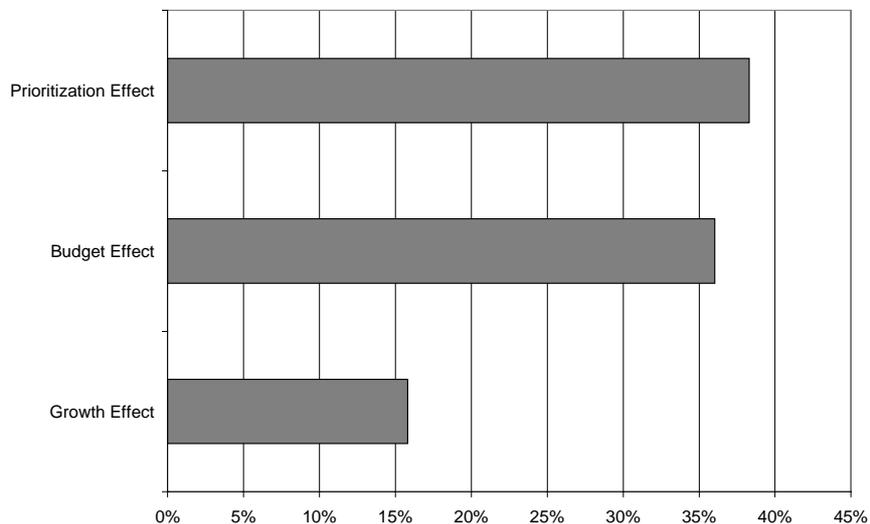
Table 6: Bolivia: Social Expenditure

	1994/1995	1996/1997	1998/1999
Social Expenditure as Proportion of GDP	12.4	14.6	16.1
Social Expenditure as Proportion of Total Public Exp.	49.4	54.9	56.5

Source: CEPAL (2001) p. 139, 140.

Chart 8

Bolivia: Factors in Social Expenditure Trends, 1994/95-98/99



Source of data: CEPAL (2001), World Bank (2001)

An analysis of social expenditure between 1994/1995 and 1998/1999 reveals that social expenditure per capita in real terms increased mainly because of political prioritization,

<sup>15</sup> CEPAL figures are used here. National figures give lower shares. See Bolivia PRSP, p. 32.

followed by the influence of increased spending by the government as a share of GDP.<sup>16</sup> Only a small part of the increase in per capita social expenditure can be explained by overall growth. It seems that Bolivian governments attributed a high political priority to social spending, which was both high and growing on a per capita basis. The already high level of overall expenditure in Bolivia naturally places severe restraints on this kind of policy.

#### 3.4.2. Education

Education reform led to enhanced coverage and quality of education, particularly at the primary level. It involved greater community participation in education, and incorporated the cross-cultural concept and bilingual techniques. Despite considerable progress, low quality levels are still observed, owing in large measure to inadequate teachers' pay. Nevertheless, the proportion of the rural population without access to education decreased by 21.31% between 1992 and 2001, which is the highest improvement of all unsatisfied needs in rural areas. Access to education in urban areas increased by 32.28% (see Table 5).

#### 3.4.3. Health and Childcare

During the Eighties, *ad hoc* actions were undertaken to promote health among the poor population, particularly in the form of child immunization programs. At the end of the Eighties, priority in this area focused on mother-and-child health, laying the groundwork for health system reform. In 1996, National Maternity and Child Insurance (SNMN) was established, offering a package of services designed to protect mothers and children. In 1999, basic health insurance was introduced which expanded the benefits offered by the SNMN package.

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<sup>16</sup> The method of decomposition used here is described in CEPAL, 2001, p.122.

Comprehensive care for children was established on the basis of three programs that began during the early Nineties: the comprehensive childcare program, comprehensive child development centers, and the national program of care for children younger than 6. These programs have now been incorporated into the Program of Care for Boys and Girls Younger than 6, which aims to coordinate the supply of initial education, nutrition, health, and protection.

Shortage of human resources, high staff turnover and inadequate training remain a serious problem in the health sector. Administrative personnel have no interface with medical staff, indicative of inefficient human resource allocation and the low numbers of medical personnel. Insufficient training of administrative personnel leads to institutional management constraints, limiting the impact of health programs. Nevertheless, noticeable progress in basic health services was made (1992–2001: 28.86% in urban and 18.17% in rural areas, see Table 5).

#### 3.4.4. Housing and Basic Sanitation

The major problems in the housing sector are poorly defined property rights, the absence of a reliable real estate registry, lack of transparency in the recording of market values for real estate transactions, unskilled human resources, insufficient information systems, and institutional weaknesses in the municipalities, which lead to low quality of construction. Little progress was achieved in this area: Quality of construction and available living space in the rural area improved by 9.34% and 10.34%, respectively, between 1992 and 2001 (see Table 5).

In the area of water and basic sanitation, the Rural Basic Sanitation Program was the key instrument in providing these amenities to rural communities, with assistance from the Social Investment Fund and municipalities. Water and sanitation projects included training and participation of beneficiaries. The mechanisms have yet to be consolidated

to cover financing and implementation of these projects to enhance levels of coverage. Water and sanitation improved considerably between 1992 and 2001, by 26.17% in the urban and by 19.16% in the rural areas (see Table 5).

#### 3.4.5. Social Emergency and Investment Funds

In 1986, the Emergency Social Fund was established to alleviate the effects of stabilization policies. This fund generated temporary employment and made it possible to create social infrastructures, thus alleviating the consequences of strict stabilization policies for the poorer parts of the population. Social investment funds began to operate in the early Nineties. The funds enhanced disbursement capacity, achieved nationwide coverage, acquired technical expertise, and established eligibility criteria with municipal governments. However, operating costs proved to be high, and the funds executed projects that were not always coordinated with the sectors. In some cases projects were rather poorly managed (Bolivia PRSP, p. 29). and relations with beneficiaries were sometimes difficult (Witt, 1998, p. 304). The funds are currently undergoing restructuring in order to improve management efficiency, reduce financing periods, lower administrative costs, and improve institutional performance.

### 4. Assessment of Past Policies

Bolivia is often described as the Latin American country which was most fastidious in applying the recommendations of the international financial institutions.<sup>17</sup> Its decentralization process is widely reputed on the continent as one of the most far-reaching policy experiments. Bolivia experimented with governmental reform, many elements of which were taken into mainstream policy recommendations, but others — such as the creation of super ministries — were abandoned after a number of years. The

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<sup>17</sup> *In the course of its cooperation with the IMF and World Bank, Bolivia was very early to implement structural and institutional reforms, and as such came to be regarded by the international financial institutions as a model reforming country.* Translated citation from Walther, Hentschel (2002), p. 95.

overall applause which Bolivia has received for its economic and social policies<sup>18</sup> stands in stark contrast to the actual results achieved to date. In 1999, the share of national income going to the poorest 40% of the population in Bolivia was the lowest anywhere in Latin America, and indeed lower than in countries with lower per capita GDP such as Nicaragua and Honduras. Moreover, the available statistical evidence indicates a continuing decline in that share. The absolute elasticity of urban poverty reduction was around 0.5 in the Nineties, still quite low, but Bolivia performed slightly better than Nicaragua in this respect. There were significant disparities in regional economic growth in the Nineties, relatively high growth in the Departments of Santa Cruz, Cochabamba, and Tarija, which experienced average annual economic growth levels of 5.7%, in contrast to poorer regions such as Chuquisaca, Potosí, and Beni, for which growth levels were below an annual rate of 2.5%. Poverty in the rural areas remains high.<sup>19</sup>

The economic growth of the Nineties was based primarily on the capital-intensive sectors, such as electricity, transportation, and financial services, which achieved annual growth rates in excess of 4.5%, compared with the more moderate rates in other, more labor-intensive sectors such as manufacturing (3.8%) and traditional agriculture (2.5%) (Bolivia PRSP, p. 21). This process was supported by the privatization of the industries involved (or “capitalization,” as it is called in Bolivia). The composition of growth thus was not favorable for poverty reduction and a different future composition may trigger faster poverty reduction than observed in the past.

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<sup>18</sup> For example: *The Bolivian poverty reduction policy since 1986 can be regarded as the most ambitious and far reaching in Latin America* (Gleich, 1998, p. 66).

<sup>19</sup> Andersen reports that ubication of households is one of the determining factors of children’s education, thus perpetuating the gap between rural and urban areas. (Andersen, 2001, p. 10. He also finds that overall social mobility in Bolivia is low compared to that of other Latin American countries.

The analysis of trends in social expenditure within the budget suggests a high policy priority attached to this type of spending (see Chart 9). Great efforts were undertaken to improve education, access to water and sanitation, and access to health services for the poor. These efforts were not sufficient to balance the negative effects of the growth pattern on distribution. The poverty-reduction elasticity of economic growth remained modest. The efforts of the past were not sufficient to increase per capita growth for the poor beyond the national average, so pro-poor growth was not achieved.

Economic policies introduced after 1985 led to macroeconomic stability in Bolivia. The widening of the budget deficit in the last three years may be attributed in part to a worsening international economic climate and internal social unrest. Nevertheless, efforts must be undertaken to reverse this tendency. The stabilization of the economy and an appropriate regulatory framework attracted substantial inflows of foreign investment in the process of privatization. Because a large part of these inflows was contingent to privatization, high levels of FDI cannot be taken for granted in the future. Even if worker remittances have increased in recent years, the trade deficit has reached unsustainable levels. Economic policy has not achieved the necessary diversification of export products. The export performance of the Bolivian economy is still based on the extraction of primary resources and on soya, making it highly vulnerable to external price or demand shocks. Economic growth thus still depends on external developments, and growth in the rural areas remains low.

The analysis of past performance hints at a lack of continuity in economic policies. And the social unrest which prevailed in Bolivia during most of 2000 and 2001 (Glaser, 2001, pp. 60–62), and started again in 2003 is an indicator that Bolivian institutions have a limited capacity to resolve conflicts. Both the performance of the Bolivian economy and political developments highlight an unsatisfactory situation: The gap

between living conditions in the rural and urban areas remains large and little progress has been achieved in this respect. Moreover, the coca eradication policy is not supported by the majority of the rural masses. Policies in the past seem not to have benefited from a large national consensus.

The conceptual advances in the fight against poverty were not always matched by actions ensuring effective results in poverty reduction. The municipalities suffered from institutional weaknesses and limitations in the social control of resources became evident; however, these weaknesses may be attributable to the fact that the process of decentralization was still in the initial stages. Nevertheless popular participation and administrative decentralization contributed to a redistribution of resources to the regions and promoted the participation of civil society in resource allocation. Evidently, though, this process was not sufficient to overcome widespread feelings of exclusion especially by the rural poor, so that social unrest erupted.<sup>20</sup>

## **5. Bolivia's PRSP**

### **5.1. The Process**

The first "National Dialogue" in 1997 had the purpose of developing a plan for the use of debt relief provided under the initial HIPC Initiative. The Dialogue produced the "Proposals Against Poverty" strategy. The strategy was never fully implemented and the associated participatory process did not become institutionalized as civil society groups grew frustrated that government had failed to deliver on its promises (International Development Association and International Monetary Fund, 2002, p. 27).

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<sup>20</sup> *What seems to oppose the pronounced wish for popular participation in Bolivia is the lack of interest in changing the role of the political parties. The political parties are still the major power holders in the Bolivian society* (Andersson, 1999, pp. 12/13).

In January 2000 the government submitted an “Interim PRSP” to the International Financial Institutions, which had been elaborated by a small group of experts. The government instituted a second National Dialogue in April 2000 to develop the full poverty reduction strategy. The first discussions took place in municipal round tables and not until these were concluded was debate moved up to the departmental (regional) and national levels. Alongside the National Dialogue a number of independent initiatives promoted popular participation, such as the Jubilee Forum, the Liaison Committee, and other social organizations. These initiatives focused on the implementation of some kind of mechanism of social control in order to supervise the distribution of funds resulting from the extended HIPC initiative.<sup>21</sup>

The strategy vests primary responsibility for poverty reduction activities in the municipalities, which must assume responsibility for education and health services, and will be involved in the creation of the economic infrastructure and the promotion of the local economy. Resources under HIPC II are planned to be transferred automatically to the municipalities.

A questionnaire had been developed for the official process (Dialogo Nacional) in order to obtain some prioritization of problems on the local level. A similar questionnaire was developed for the departmental level, focusing mainly on political and institutional aspects. During the discussions a popular version of the poverty analysis was provided. Discussions at the local level included representatives from the

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<sup>21</sup> *Despite the strengths of the National Dialogue, the process has not been without weaknesses. There were criticisms that the voices of the most vulnerable (e.g., women and indigenous groups) were neglected, and that the agenda for debate was too rigidly defined. There was also significant dissatisfaction among some civil society groups who believed that debate was hijacked by local elites. (International Development Association and International Monetary Fund, 2002, p. 27). Public participation in the National Dialogue was drowned out by other factors: the social conflicts and protests against the policy of privatization in the water sector, the government’s campaign to eradicate coca cultivation, and demands for increased pay in the public sector (unofficial translation of: Walther, Hentschel, 2002, p. 111). As in other countries, the Bolivian PRSP was not discussed by parliament.*

local government, the so-called „Comites de Vigilancia“ (committees for social control) and NGOs. At the end of the process a national round table was organized and agreements were concluded in the areas of education, health, rural property rights, sanitation, production and infrastructure. The character of these meetings nevertheless did not lead to clear prioritization of planned actions.

A technical unit within the ministry of finance analyzed and disentangled the outcome of this process and wrote a first version of the PRSP. This version was submitted to discussion within the government, which led to a second version. Intense discussions between the government and the international donor community resulted in substantial changes in the strategy. At this stage in the process the government did not seek new discussions with civil society because of time restrictions.

In March the PRSP was presented to civil society during a meeting called „El Gobierno Escucha“ ( the government listens) and on March 27 the final version of the Bolivian PRSP was presented to the international donor community. In May the IMF and the World Bank accepted the strategy and granted debt reduction within the framework of the enhanced HIPC initiative (HIPC II) (The International Monetary Fund and the International Development Association, 2001).

Later in 2001 the national assembly approved a law of the national dialogue („Ley del Dialogo Nacional“), which regulates the distribution of the funds obtained by HIPC II:

- The „Fondo Solidario Municipal para la Educación Escolar y Salud Públicas“ was established in order to finance additional personnel in the areas health and education. During the first year 5 Mio. USD were earmarked for this fund, in later years 27 Mio. USD.

- The remaining funds are deposited in a special account at the central bank. 20 per cent of these funds are used for improvements in education, 10 per cent for improvements in the health sector and 70 per cent for investments in infrastructure at the local level.
- The funds earmarked for infrastructure are distributed according to poverty indicators, the poorer municipalities receive more funds per inhabitant than the richer ones. These funds may be used for co-financing projects with funds stemming from the ordinary national budget.
- The development funds are reorganized and money is allocated through the same poverty adjusted formula.

During the process of elaboration of the strategy social unrest occurred, triggered by coca eradication and privatization of sanitation in some municipalities. These policies had started before the PRS-process. Therefore the government considered the participatory process within the PRSP framework as a useful means for alleviating the tension in the country, even if the process started as a result of the enhanced HIPC initiative.

## 5.2. The Policies

The Bolivian PRSP has four strategic components: (a) expand employment and income-earning opportunities; (b) develop productive capacity; (c) increase security and protection; and (d) promote participation and social integration. The poverty reduction strategy includes cross-cutting actions targeting a sustainable environment, gender equality and equality among ethnic groups, and institution building to promote a backdrop of transparency, legal security, and full exercise of democracy. Within this framework, priority actions are identified to support rural development, the development of micro-enterprises and small enterprises, technical assistance, and road infrastructure, as well as (primary) education, primary health care, basic sanitation, and

comprehensive attention to youth. In addition, an institutional framework is developed for combating corruption.

#### 5.2.1. Expand Employment and Income-Earning Opportunities

This policy area includes promoting rural development, supporting micro and small enterprises, developing microfinance, and improving road infrastructure.

Support for rural development seeks to increase the scale and productivity of production through better road infrastructure, improved risk coverage, increased electrification, and more microcredit. Intermediate indicators in this policy area include volume of production, land cultivated, participation of rural credit in the credit portfolios of microfinance institutions, electricity supply coverage, quantity and quality indicators of road infrastructure, and percentage of municipalities with access to financial services. Developing and strengthening small and microbusiness as well as supporting technological assistance are considered to be primarily dependent on an appropriate regulatory environment, so no quantitative indicators were developed in this case.

#### Actions include:

- Rehabilitation of rural roads by local micro and small enterprises.
- Construction and maintenance of irrigation and micro-irrigation systems.
- Construction of basic agricultural infrastructure.
- Provision and maintenance of electrical power networks.
- Provision of rural telecommunications services.
- Concluding the regularization of rural land ownership.
- Identification and selection of agro-food and agro-export sequences through agricultural and rural development plans.
- Design and implementation of programs to promote rural tourism.
- Opening of foreign market opportunities.
- Revision and adaptation of regulatory framework to cater for the characteristics of micro and small enterprises.
- Expansion of productive, commercial and services infrastructure.
- Provision of technical assistance services, training in business management, information, and marketing.
- Coordination of incentives for artisanal production through programs for craftsmen and small industry.
- Development of markets for entrepreneurial and microfinance services.
- Consolidating an information services network.

- Voucher program for training in business techniques
- Promoting the strengthening of financial institutions serving urban and rural micro and small enterprises.
- Consolidating research systems and rural technological innovation.
- Development of Internet access.
- Establishment of agreements between universities, private entities and agricultural producers to link productive sector needs with academic institutions' output.
- Dissemination of agricultural information.
- Implementation of business development services in micro and small enterprises.

### 5.2.2. Developing people's capabilities

Education, health and habitability (sanitation and housing) are the areas addressed here.

Indicators include quantity and quality measures of education and different standard indicators of health and access to sanitation.

Planned actions include:

- Transfer to the municipal governments of responsibility for administering, supervising, and controlling human resources in the schools, as well as the corresponding funds.
- Strengthening of the educational information system.
- Development of an educational quality measurement system
- Promoting creation of an autonomous educational accreditation body.
- Strengthening and diversifying technical institutes, and linking them to productive activities.
- Implementation of a new administrative system for teaching staff, incorporating a teacher incentive program.
- Training for officials of departmental and municipal governments in planning, evaluation, information, administration, and control systems.
- Increasing human resources.
- Expansion and consolidation of basic health insurance.
- Gradual implementation of universal health insurance.
- Development and implementation of the Health with Identity program and incorporation of traditional medicine.
- Development of health services network.
- Institutional strengthening of the health sector by implementing training and technical assistance programs in the municipalities.
- Construction of drinking water and sanitary sewerage systems in peripheral urban and rural areas.
- Construction of waste water and solid waste treatment plants.
- Development of technical assistance programs on preinvestment and investment feasibility studies for small municipalities.
- Leadership of women in the implementation and appraisal of sanitary education projects.
- Construction and improvement of low-cost dwellings in rural municipalities.
- Modernization of the system for the urban and rural registry of property rights and cadastre.
- Design of new regulations on real property rights, cadastre, rentals, expropriations, Law on Preferential Purchase Rights for municipalities.
- Self-construction programs for low-cost housing.
- Incentives for the incorporation of private social development.
- Institutions for the financing of housing in rural areas.

### 5.2.3. Increase Security and Protection

The topics of protecting the elderly and young, vulnerability, and legal protection of land tenure are considered in this context. Indicators include qualitative indicators associated with progress in programs for the elderly and childcare programs, the creation of a fund for natural disasters and the establishment of an emergency jobs program. Legal security of land tenure is measured by the number of hectares with titles cleared.

Actions include:

- Effect the transfer of funds to people over 65 years of age.
- Expand health programs for the elderly.
- Improve and expand programs caring for children and adolescents.
- Implementation of the national plan for seniors and establishment of the institutional network for seniors' organizations.
- Regulation of NGOs in the execution of food security programs.
- Implementation of the Law on Risk Reduction and Disaster Response.
- Development of emergency employment programs.
- Programs to protect workers with professional risks, dangerous occupations, or rare skills.
- Modernization of urban cadastre.
- Concerted preparation with civil society of a regulation establishing the principles of access rights to and use of water resources and the institutional framework for its management and control.
- Districting and delimitation of native community lands.
- Strengthening of the Agrarian Superintendency.
- Participation of the Military Geographic Institute in regularizing land tenure.
- Creation of the National Water Authority and the Water Superintendency.
- Simplification and modernization of administrative and judicial procedures and of records of real estate transactions.

### 5.2.4. Increase Participation and Social Integration

This policy area seeks to increase popular participation in decision-making with a special focus on ethnic minorities. The plan is that the National Dialogue should be conducted every three years as a demonstration of the State's commitment to participatory policies.

Actions include:

- Implementation and improvement of strengthening and technical assistance programs for municipal governments.
- Conducting dissemination campaigns on the scope and results of popular participation and administrative decentralization.

- Formation of consultative committees in each municipality.
- Streamlining and ordering of supply and demand in technical assistance, and training for municipalities.
- Training system for popular participation.
- Strengthening of Ombudsman's office.
- Increased access to the educational system for indigenous peoples and their continued attendance at school
- Periodic dissemination of information with indicators desegregated by ethnicity.

#### 5.2.5. Cross-cutting Issues

Cross-cutting issues are the participation of ethnic minorities, gender, and sustainable environment. Indicators include the number of culturally oriented micro-enterprises in operation, the percentage of indigenous population covered by basic services, percentage of micro and small enterprises headed by women, access of rural women to education and technical training, access of women to basic health insurance, completion of design of national water resources plan, and the increase in income levels due to sustainable wildlife management programs.

Actions include:

- Development of programs that promote women's access to productive resources, credit, ownership and clear title to land.
- Revision of labor legislation and the Civil Service Statute.
- Support for productive skills of micro and small enterprises, with emphasis on those led by women.
- Development of technological, market, and chain-of-production information systems, facilitating access for women.
- Development of programs promoting renewal of the traditional skills of women.
- Improvement of the identification card process and civil registry, with emphasis on registering women.
- Incorporation of the gender and cross-cultural approaches at all levels of the educational system.
- Implementation of campaigns to prevent and eradicate gender-based violence.
- Development of municipal programs to strengthen the Ombudsman's offices for children and women.
- Promotion of plans and programs oriented toward facilitating the entrepreneurial and self-management organization of indigenous and native peoples. Development and implementation of initiatives to consolidate culturally based indigenous and native micro-enterprises.
- Management of native community lands and small farmer communities.
- Linking programs and projects to the special traits of small farmer communities and indigenous and native peoples.
- Design of national water resources, basins, and flood control plan.
- Development of incentives programs to promote environmentally beneficial technological change in mining and industry.
- Development of environmental regulations for industry.
- Institutionalization of environmental management in prefectures and municipalities.
- Design and implementation of programs for the participation of civil society in managing environmental quality.
- Fees charged in protected areas to benefit local communities.

- Approval and implementation of the biodiversity strategy.
- Establishment of biological corridors and buffer zones.
- Development of programs for integration of forests, industries, and markets.
- Promotion of sustainable forest management.
- Approval and implementation of forest management plans.

### 5.3. Monitoring and Evaluation

The plans and programs subject to evaluation are: Master Transport Plan, Educational Reform, Basic Health Insurance and the Comprehensive Childcare Program. Evaluation is carried out by the Social and Economic Policy Analysis Unit in close coordination with the National Statistics Institute. Monitoring consists of: (i) the identification of social and institutional actors; (ii) the establishment of goals and indicators; (iii) the definition of technical criteria for achieving intermediate goals; (iv) the compilation and analysis of information; (v) the preparation of periodic reports; (vi) the dissemination of results; and (vii) a feedback and decision-making process.

### 5.4. Anticipated Macroeconomic and Poverty Reduction Results

The projected macroeconomic performance of Bolivia is quite optimistic: Real GDP is targeted to grow by more than 5 per cent per annum starting in 2003. Growth in the economy is based on the following factors: (i) macroeconomic policy and regulations on attracting investment and the sectoral regulatory system; (ii) the contribution of Bolivia's PRS in more labor-intensive and traditional small-scale sectors; and (iii) the dynamic performance of the modern sectors of the economy.

Besides stressing the continuity of the general macroeconomic policies which ought to generate confidence for the private sector, the PRSP stresses the necessity of a simpler tax code, and the completion of the sectoral laws and the sectoral regulatory systems.

The PRSP seeks to strengthen the environment for economic growth, particularly in sectors involving traditional agriculture and small production units and both urban and

rural labor-intensive micro-enterprises. Road infrastructure, technical assistance and technology, development of micro- and small enterprises, development of microfinance and land access and tenure, irrigation and micro-irrigation systems, rural electrification, legal security in land tenure, and technical and technological support in the production, marketing and management of primarily agricultural rural activities are mentioned in this context.

Nevertheless, it is assumed that sectors like modern agriculture with strong ties to agro-industry, extractive industries such as hydrocarbons, natural gas and ores will continue to play a crucial role in the growth of the economy. These sectors are also expected to have an effect on related economic activities such as pipelines, processing of natural resources or road construction. Most importantly, the structural composition of economic growth is not assumed to vary substantially from that of past years, but the gap between the modern and more backward subsectors in manufacturing and agriculture is expected to be narrowed.

Table 7 Bolivia. Projections of Population, GDP and Poverty, 2000-2015

	Average per year 2000-2015 (Factor)	Total, 2000-2015 (Factor)	Percent per annum, 2000- 2015 (per cent)	Total percentage change 2000- 2015 (per cent)
Real GDP growth	1.054	2.194	5.38	119.44
Real GDP per capita growth	1.032	1.597	3.17	59.70
Population growth	1.021	1.374	2.14	37.38
Population growth if growth rate is same as 1994-1999	1.024	1.422	2.37	42.19
Change in poverty headcount index	0.972	0.651	-2.82	-34.94
Elasticity of total poverty reduction relative to growth of real GDP p.c., projected 2000-2015				-0.585
Elasticity of urban poverty reduction relative to growth of real GDP p.c. 1989-1999				-0.477
Elasticity of urban poverty reduction relative to growth of real GDP p.c. 1994-1999				-0.682
Projected Poverty Rate 2015 (Bolivia PRSP)				40.6%
Calculated Poverty Rate 2015 (Assumptions: Ongoing urbanization, rural per capita growth = urban per capita growth, moderately poor uniformly distributed )				38.005%

Source of data: Bolivia PRSP, World Bank (2001), CEPAL (2001)

The Bolivian PRSP projects a fall in the headcount index of poverty from 62.4 percent in the year 2000 to 40.6 percent in the year 2015 (and from 36.2% to 17.3% for extreme poverty).<sup>22</sup> The real GDP and GDP per capita growth projections imply a moderate decrease in population growth. The implicit elasticity of poverty reduction with respect to real GDP per capita growth for the period of projection is somewhat higher than the experienced elasticity for urban poverty reduction for the 1989–1999 period, but somewhat lower than the experienced elasticity for urban poverty reduction for the 1994–1999 period (see Table 7). The projected elasticity of poverty reduction is thus substantially lower than actual elasticities of poverty reduction in Latin American

<sup>22</sup> The Bolivian PRSP points out that this assumed behavior is very close to that seen in other countries that have grown at rates of at least 5.0% per year for long periods, and cites East and Southeast Asian countries as examples. (p. 197). Nevertheless a sensitivity analysis is carried out in order to estimate the impact of smaller growth rates on poverty reduction.

An analysis of the effect of urbanization in Bolivia reveals that 3 percentage points of this reduction may be attributed to urbanization, if the rate of urbanization continues at the same speed in 2000–2015 as in the Nineties.

countries in the Nineties (see Chart 6). If the moderately poor benefited from growth as much as the rest of the population — and their incomes were uniformly distributed — the projected poverty rate in Bolivia in 2015 would be lower than the goal expressed in the Bolivian PRSP, taking the urbanization process into account. Under plausible assumptions, projected growth in Bolivia's PRSP thus does not yield a strong pro-poor outcome.

## **6. Assessment of Bolivia's PRSP**

Bolivia's PRSP provides a comprehensive poverty diagnosis based on available data, and examines the regional and distributional consequences of growth in the past. Limitations of the poverty analysis are due to lack of data on poverty in the rural areas. The Bolivian PRSP describes past policies, but does not analyze in depth the reasons for past failures and successes, and the possible implications for future priority policy areas. The PRSP includes a great diversity of actions which should help reduce poverty and which are in line with past efforts. Most actions are directly linked to human development under the headings of "capacity" and "protection and security." Clear priorities have not been laid down within these policy fields. The disbursement mechanism favors local decisions, thus improving targeting. The quality of implementation therefore depends on the quality of local institutions, which has been weak in the past.

Indicators and goals have been established to monitor progress in implementing the strategy. The institutional responsibilities seem clear. The idea is that providing data on the strategy's progress will strengthen the public's monitoring role within the institutionalized process of national dialogue.

The macroeconomic projections assume high real GDP growth from 2001 to 2015. The identified sources of this growth are the same as in the past, mainly the extraction and processing of natural resources. As growth in the past was based primarily on performance in this capital-intensive sector, it is difficult to see how a more labor-intensive mix of economic activities might be achieved. The Bolivian PRSP stresses the stability and reliability of the regulatory environment in Bolivia and does not propose any major policy reform. Empirically, growth rates as high as those assumed for the future have not been achieved over longer periods in the past. Even if a substantial lag between policy reforms in the past and economic growth effects in the future can realistically be assumed, it seems overly optimistic to rely exclusively on this relationship. The projected narrowing of the budget deficit depends on the assumed growth path. Substantially lower growth may jeopardize fiscal stability and the availability of resources for financing Bolivia's PRSP.<sup>23</sup>

Actions to promote human development may increase productivity and thus growth from the supply side. The opportunities component of the Bolivian PRSP consists of actions to improve infrastructure, land access and tenure, technology assistance and actions to foster micro-enterprises and microfinance. All these actions strengthen the supply side, whereas only the last two focus directly on the provision of employment opportunities.<sup>24</sup> Direct actions that would improve the overall investment climate ought perhaps also to have been included. A more thorough analysis of possible pitfalls within the existing labor market regulatory system would have been helpful. Existing evidence indicates substantial regulatory impediments to employment creation (Lay, Wiebelt, 2002, p. 72).

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<sup>23</sup> Using a Computable General Equilibrium (CGE) model for the Bolivian economy, Jemio and Wiebelt nevertheless predict *that combined debt relief with a fiscal expansion ...is expected to have significant macroeconomic impacts: higher growth rates, lower fiscal and external deficits, and lower unemployment.* (Jemio, Wiebelt, 2002, p. 30).

<sup>24</sup> Only 1.5% of expenditure is earmarked for these two components.

Bolivia's PRSP recognizes the necessity of tackling the high trade deficit (Bolivia PRSP, p. 213). It considers tapping new markets, particularly in the more advanced economies, as *one of the structural solutions to the problem of the sustainability of Bolivia's development process*. (International Monetary Fund and The International Development Association 2001, p. 6) Trade policy of the industrialized countries certainly is a constraining factor for development, but again, it does not seem promising to rely solely on this measure to decrease the trade deficit.

Past experience in Bolivia indicates a lack of implementation capacity on the part of public institutions. The strategy acknowledges these deficiencies and includes actions to improve implementation capacity, especially on the local level. Nevertheless, implementation capacity must be viewed as a possible risk to the success of the strategy.

Bolivia's PRSP is a comprehensive strategy which aims at poverty reduction through human capital formation and improved opportunities particularly for the poor. Nevertheless, the growth projections seem rather optimistic. No actions are considered that would directly foster economic growth. The indirect instruments such as human capital formation will impact on economic growth mainly in the long run and cannot be used as a basis for near-term growth projections. Bolivian authorities assume only a moderate impact of growth on poverty reduction. No bold measures are envisaged to improve income distribution. Also, despite the focus on the rural population, the measures are not considered likely to improve the relative income of the rural population. Thus the strategy seems too optimistic with respect to overall economic growth,<sup>25</sup> and too conservative with respect to poverty reduction.

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<sup>25</sup> To be fair it must be mentioned that the strategy considers different growth scenarios.

The Bolivian PRSP does not include actions intended to improve economic regulatory systems such as labor market regulation or the introduction of a competition law. The strategy expresses its hopes that modern and backward sectors may be interlinked in the process of improving human capital formation, but does not include programs which aim at fostering this process in a more direct way. The strategy thus does not include actions that may change traditional patterns of production and enhance diversification. There is a lack not only of actions seeking to increase output of competitive export products besides mineral extraction, but also of proposals addressing the problem of coca eradication. This is especially surprising since the strategy was elaborated in the context of widespread social unrest triggered in part by prevailing coca eradication policies.

## **7. Implementation of the PRS**

Three progress reports on the implementation of the Bolivian PRS were published until the end of 2002 (CISE, 2002a; CISE 2002b; UDAPE, 2002). After the change of government in 2002, the new authorities declared their willingness to continue the PRS process, but announced amendments of the strategy during a new national dialogue planned for 2003.

Elements of the implementation of the strategy are new laws and regulations, the program of public investment and the mechanism of transfers to the municipalities. Problems occurred in respect to the transfer mechanism: Institutional capacity of the newly structured development funds, which finance investments in infrastructure at the local level, is still low. So is the capacity for implementation of the municipalities. This resulted in a slow flow of funds. As municipalities use their funds stemming from HIPC

to co-finance investments of the development funds, use of HIPC funds also remained slow.<sup>26</sup>

In December 2002 the new government published a critical report on the Bolivian PRS and its implementation (UDAPE, 2002). With respect to the actions planned in the “Expand Employment and Income-Earning Opportunities” chapter of the PRSP, the institutionalization of the administration responsible for roads and the elaboration of rules for subsidization of small producers are highlighted, but also a lack of progress in the design of new policies, especially for agriculture. In the “developing people’s capabilities” pillar of the strategy, progress in financing the education and health system, infrastructure and other measures of the “Ley del Dialogo” are mentioned. With respect to “increasing security and protection”, lack of concrete actions in the strategy is criticized. The same is true for the “increasing participation and social integration” pillar. On the whole this progress report is much more critical than the ones published by the anterior government. Not only the implementation, the PRSP as well was criticized:

- Lack of consistency between actions,
  - lack of actions fostering growth and
  - lack of actions directed at increasing the potential of growth for poverty reduction
- are mentioned in this context.

The progress report adjusts the growth expectations of the PRSP downwards and assumes less progress in poverty reduction until 2015; formal adjustment of the PRSP during the planned new national dialogue (Juli and August 2003) is announced.

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<sup>26</sup>From August 2001 until August 2002 only 48.1% of the funds earmarked for the municipalities actually were used (UDAPE, 2002, p. 31)

## **8. Conclusions**

This study has analyzed past policies and the past performance of Bolivia's economy. The main shortcomings are limited progress in poverty reduction, virtually none at all in narrowing the gap between living conditions in rural and urban areas, an economic structure which is still dominated by products of the minerals and mining sector and one cash crop, very slow progress in diversifying the structure of the economy and export products, and an unsustainable trade deficit. Even the highly reputed system of popular participation in Bolivia appears not to have been as successful as is often assumed: It did not prevent widespread social unrest in 2000, 2001, and again in 2003. The implementation capacity of Bolivian institutions is still low, despite many years of institutional strengthening supported by the international donor community.

Bolivia's PRSP does explicitly tackle some of these points. It promises to step up efforts to narrow the gap between rural areas and urban centers, to focus on directly reaching the poor, more popular participation and more institution building. What makes the strategy rather disappointing is that it seems to promise more of the same, without an exhaustive analysis of the reasons why past policies did not achieve the expected results.

The Bolivian PRSP fails to address policy areas which are directly linked to economic growth. The risk of unstable economic policies is tied up with the future course of Bolivian politics. Recent experience with social unrest in Bolivia highlights the importance of rapid progress. Growth in Bolivia must at last be pro-poor. The actions prescribed in Bolivia's PRSP aim in this direction, but growth cannot be pro-poor unless there is positive growth.

The decision to grant debt relief before the usual one year phase of successful implementation was triggered by the relatively good governance performance record of Bolivia in the past. But elaboration of the Bolivian PRSP already happened during a deterioration of Bolivian governance indicators. There is a risk that new debt will again lead to an unsustainable degree of indebtedness even after having received debt relief according to the HIPC initiative. The PRSC (poverty reduction support credit of the World Bank), PRGF (poverty reduction and growth facility of the IMF) and HIPC initiative are strong instruments linked with the PRS process. These instruments should be used by the international donor community carefully and selectively, otherwise the credibility of the PRS process will be jeopardized.

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## Annex Statistics

Annex Table 1 Bolivia: Exports by Region (2001, percentages)

MERCOSUR	27.84%
Comunidad Andina	27.07%
Chile	2.44%
USA	13.46%
Canada	1.45%
Mexico	0.62%
EU	10.42%
Switzerland	13.01%
Asia	1.46%
Rest of World	2.22%

Source: Banco Central de Bolivia (2002a)

Annex Table 2 Bolivia: Population with Unsatisfied Basic Needs, Census 1976, 1992 and 2001 (Percentages)

Year	1976	1992	2001
BOLIVIA	85.5	70.9	58.6
Chuquisaca	90.5	79.8	70.1
La Paz	83.2	71.1	66.2
Cochabamba	85.1	71.1	55.0
Oruro	84.5	70.2	67.8
Potosí	92.8	80.5	79.7
Tarija	87.0	69.2	50.8
Santa Cruz	79.2	60.5	38.0
Beni	91.4	81.0	76.0
Pando	96.4	83.8	72.4

Source: Instituto Nacional de Estadística. Bolivia: Mapa de Pobreza 2001, La Paz 2001

Annex Table 3 Bolivia: Indicators of Income Distribution

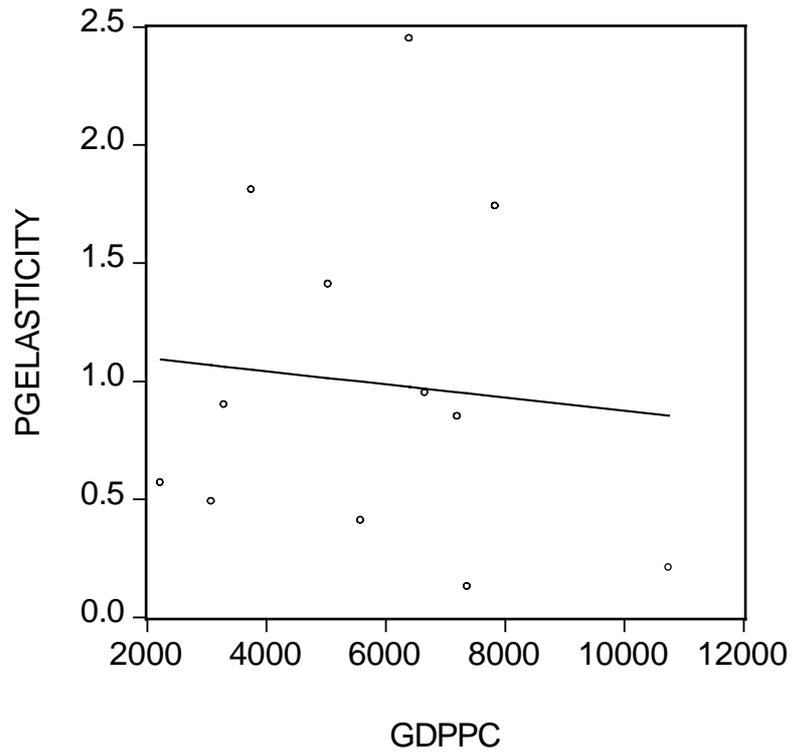
Year	Urban areas			Rural areas		
	Persons with less than average income	Persons with less than 50% of average income	Gini	Persons with less than average income	Persons with less than 50% of average income	Gini
1989 a)	71.9	44.1	0.538			
1997	72.5	43.0	0.531	75.4	53.6	0.637
1999	72.5	40.2	0.504	71.3	52.9	0.640

a). La Paz

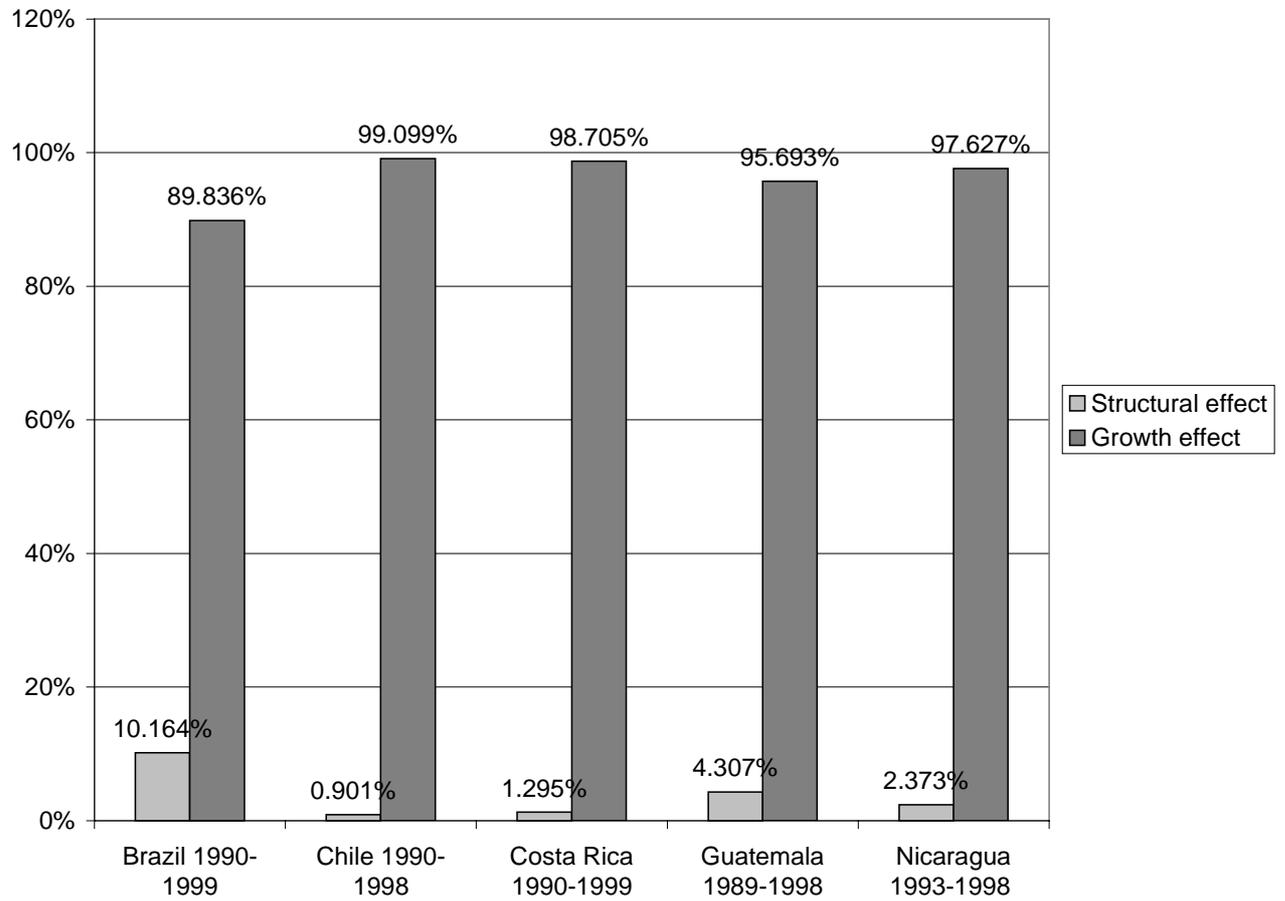
Source: CEPAL(2001)

Annex CHART 1

GDP per capita on a PPP basis and poverty reduction elasticity of growth in the nineties:  
12 Latin American countries

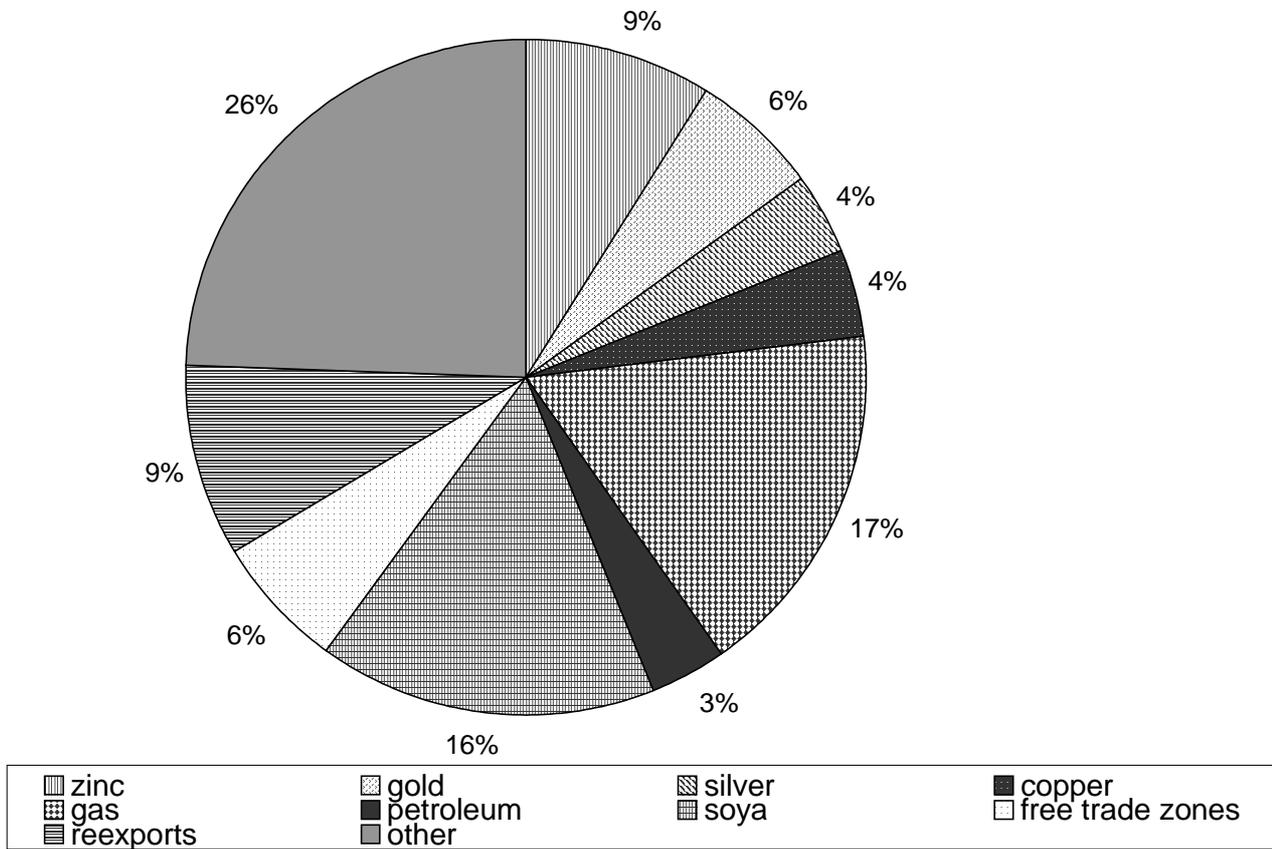


Annex Chart 2 Latin America: Urbanization and Growth as Factors of Poverty Reduction



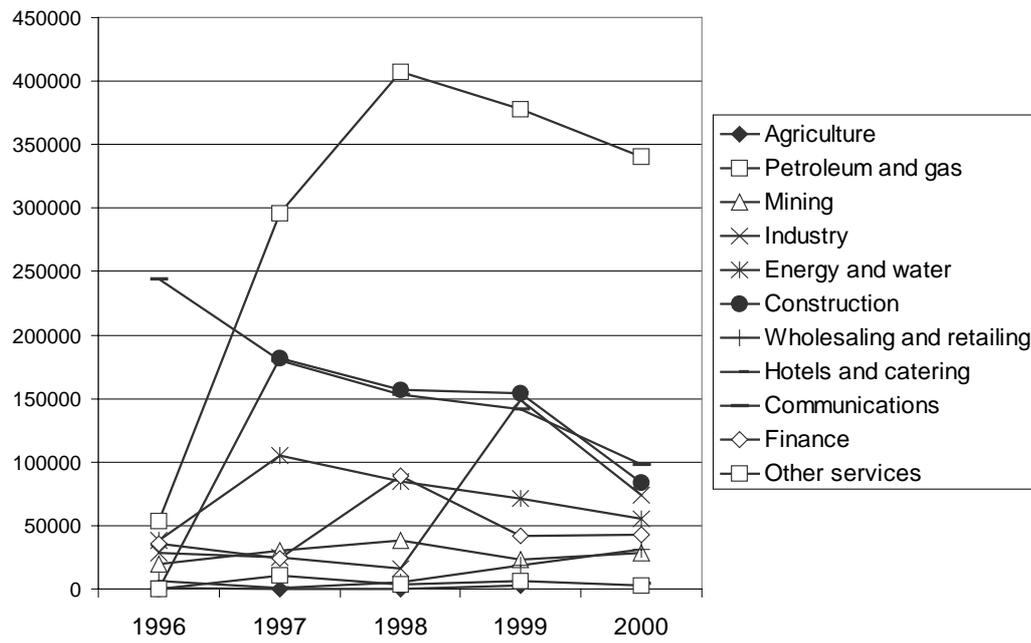
Source of data: CEPAL (2001), World Bank (2001)

Annex Chart 3 Bolivia: Structure of Exports 2001



Source: Banco Central de Bolivia: Memoria Anual 2001, La Paz 2002.

Annex Chart 4 Bolivia: Foreign Direct Investment per Sector 1996–2000 (USD thousands)



Source: Instituto Nacional de Estadística (2002)