Can Fiscal Policy Alone Induce Growth? A Simulation Analysis for Bolivia
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NEW FEATURES OF THE BOLIVIAN ECONOMY
The current fiscal situation in Bolivia has a number of novel features:

i) Since 2006, and for the first time in history, the country has recorded fiscal surpluses, due mostly to an export boon and a steady increase in growth rates, at least up until 2009 (reaching 6.1% in 2008).

ii) Social policy almost entirely based on cash transfers to poor households.

iii) Objective of establishing fiscal policy, especially public investment, as the principal tool to promote growth and welfare.

CONSIDERING ALTERNATIVE SCENARIOS
A team of Bolivian researchers has developed a Dynamic Stochastic General Equilibrium (DSGE) model of the Bolivian economy, based on its five main economic sectors – services, manufactures, hydrocarbons, mining and agriculture. The model is used to simulate several fiscal reform scenarios, allowing for changes in sectoral productivity, fiscal balance and the efficiency of public capital provision.

KEY FINDINGS
• The best fiscal policy would combine full trade liberalization with a 3.7% increase of the VAT, resulting in a 3.4% increase in output.

• Whereas an increase in public investment (infrastructure) increases output, the opposite is true for an increase in public current spending.

• All of these results are substantially improved when the efficiency of public capital and sectoral productivity are increased.

CONCLUSIONS
Results of these simulations show that fiscal policy alone cannot substantially increase growth. However, combined with more efficient public capital and productivity boosts, the economy is capable to grow by more than 6% in the short-run and more than 10% in the long-run. In particular, this would allow government to increase transfers to poor households and make them sustainable over time.

POLICY IMPLICATIONS
In order to preserve a favourable fiscal situation and sustain its transfer policies to reduce poverty, the Bolivian government must therefore promote an efficient provision of public capital and generate incentives to enhance productivity.