

INFLATIONARY MEMORY, RISK AND CREDIBILITY IN THE INTEREST RATES DETERMINATION IN A SMALL ECONOMY: BOLIVIAN POST-HIPERINFLATIONARY EXPERIENCE

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ABSTRACT

In this paper I manage the inflationary memory as a determinant of the interest rates in Bolivia in the 1985 - 1994 period. The Bolivian' hyperinflationary process ended in august, 1985 through an orthodox program called NPE (Nueva Política Económica - New Economic Policy). The inflation rate decreased rapidly after the NPE's implementation and the GDP did grow up slowly but a positive rate since 1987.

The real interest rate remains high and this is a governmental preoccupation. Many hypotheses were formulated about it and many of them managed the risk and the credibility problem as the main determinants of the difference between the domestic and external interest rates, despite the domestic market structure.

The way to evaluate the risk and the credibility is intimately related with the inflationary memory. The inflation was the main financial problem during the hyperinflation and a current long inflationary memory reflects a low level of credibility. Additionally, a major instability in the current inflation rate is a risk factor in the financial return. Here, the recursive variance of inflation (VARINF) reflects the risk and it's initialization period reflects the credibility level related to the inflation rate. With VARINF, many traditional hypothesis (like PPP) have an empirical support in the lung run relationships.