RE-312

COUNTRY PROGRAM EVALUATION URUGUAY (1991-2004)

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ABBREVIATIONS

AEBU	Asociación de Empleados Bancarios del Uruguay [Uruguayan Association of Bank Employees]
AFAP	Administradora de fondos de ahorro provisional [pension fund manager]
ANCAP	Empresa Nacional de Combustibles [National Fuel Company]
ANEP	Administración Nacional de Educación Pública [National Public Education Administration]
ANTEL	Empresa Estatal de Telecomunicaciones [Uruguayan public telecommunications company]
ASSE	Administración Nacional de Servicios de Estado [State Health Services Administration]
BCU	Banco Central del Uruguay [Central Bank of Uruguay]
BHU	Banco Hipotecario del Uruguay [Mortgage Bank of Uruguay]
BPS	Banco de Previsión Social [Social Security Bank]
BROU	Banco de la República Oriental del Uruguay [Bank of the Oriental Republic of Uruguay]
BT	Bachillerato Técnico [Technical School Diploma]
CARU	Comisión Administradora del Río Uruguay [Río Uruguay Administration Commission]
CEPRE	Comité Ejecutivo para la Reforma del Estado [Executive Committee on State Reform]
CETP	Consejo de Educación Técnico-Profesional [Board of Technical/Vocational Education]
CINVE	Centro de Investigaciones Económicos [Economic Research Center]
CODICEN	Consejo Directivo Central de la Enseñanza Pública [Central Executive Board of Public Education]
CONACYT	Consejo Nacional de Innovación, Ciencia y Tecnología [National Innovation, Science and Technology Council]
DGI	Dirección General Impositiva [Directorate General of Taxation]
DINACYT	Dirección Nacional de Ciencia y Tecnología [National Science, Technology and Innovation Directorate]
DNA	Dirección Nacional de Aduanas [National Customs Directorate]
ECH	Encuesta Continua de Hogares [Continuous Household Survey]
FAS	Fortalecimiento de áreas sociales [strengthening of social areas]
FESB	Fondo de Estabilización del Sistema Bancario [Fund to Stabilize the Banking System
FNR	Fondo Nacional de Recursos [National Resource Fund]
GDP	Gross domestic product
IAMC	Instituciones de asistencia medica colectiva [mutual healthcare institutions]
IMF	International Monetary Fund
INCOME	Impuesto a la Compra de Moneda Extranjera [Tax on Foreign Exchange Purchases]
INE	Informe Nacional de Estadísticas [National Statistics Report]
INIA	Instituto Nacional de Investigaciones Agropecuarias [National Agricultural Research Institute]
LM	Logical framework
MECAEP	Mejoramiento de la Calidad de la Educación Primaria [Improvement in the Quality of Primary Education]
MEF	Ministerio de Economía y Finanzas [Ministry of Economic Affairs and Finance]

MEMFOD	Mejoramiento de la Educación Media y Formación Docente (current name) [Modernization of Secondary Education and Teacher Training]
MESyFOD	Mejoramiento de la Educación Secundaria y Formación Docente (previous name) [Modernization of Secondary Education and Teacher Training]
MGAP	Ministerio de Ganadería Agricultura y Pesca [Ministry of Livestock, Agriculture and Fishing]
MIR	Metodología de impacto regulatorio [regulatory impact methodology]
MSP	Ministerio Público de Salud [Ministry of Public Health]
NBC	Nuevo Banco Comercial [New Commercial Bank]
ONSC	Oficina Nacional de Servicio Civil [National Civil Service Office]
OPP	Oficina de Planeamiento y Presupuesto [Planning and Budget Office]
OPYPA	Oficina de Programación y Políticas Agropecuarios [Office of Agricultural Programs and Policies]
OVE	Office of Evaluation and Oversight
PCR	Project completion report
PCU	Program coordinating unit
PIAI	Programa de integración de Asentamientos Irregulars [Program for the Integration of Squatter Settlements]
PISA	Programme for international student assessment
PLASV	País libre de aftosa sin vacunación [foot-and-mouth disease free country where vaccination is not practiced]
PPMR	Project performance monitoring report
PREDEG	Programa de Reconversión de la Granja [Farm Reconversion and Development Program]
PRENADER	Programa Recursos Naturales y Desarrollo del Riego [Program for the Development of Natural Resources and Irrigation]
PRI	Private Sector Department of the IDB
PRIS	Programa de Inversión Social [Social Investment Program]
R&D	Research and development
RICYT	Red Iberoamericana de Indicadores de Ciencia y Tecnología [Ibero-American Network on Science and Technology Indicators]
RUCAF	Registro Único de Cobertura de la Asistencia Formal [Master Registry of Formal Health Assistance Coverage]
SCOT	Supervisión de las Condiciones Objetivas de Trabajo [Objective Employment Conditions Oversight]
SEG	Sistema de Ejecución del Gasto [Public Expenditure System]
SEV	Sistema de Evaluación de la Gestión por Resultados [Performance-based Management Assessment System]
SIG	Sistema Interno de Gestión Pública Internal [Public Management System]
SIIF	Sistema Integral de Información Financiera [Integrated Financial Information System]
UNDP	United Nations Development Programme
UTE	Usinas de Transmisión del Estado [State-owned Power Company]
WB	World Bank

PREFACE

This evaluation is composed of five chapters that evaluate the outcomes of the Bank's program in Uruguay for the period 1991-2004 from different standpoints. The first chapter presents developments in the country in the period evaluated and goes on to examine the main challenges for its long-term economic and social development. The second chapter studies how the strategies prepared by the Bank during the period responded to those changing needs. Chapter three explains how the strategies were converted into operations approved by the Bank and summarizes how they performed in execution. Chapter four evaluates whether the portfolio achieved the expected development results, corroborating the information provided by the Bank through empirical evidence and data. Last, the fifth chapter reflects on the extent to which the Bank's support has had an impact or built up capacity in terms of the country's long-term development challenges, and offers recommendations.

EXECUTIVE SUMMARY

Uruguay enjoyed an extraordinary level of prosperity in the mid-twentieth century, foreshadowing for its citizens a model of social wellbeing marked by heavy government involvement in the provision of jobs, economic services, social security benefits, and stability guarantees. The most significant period of growth in the economy since that time was during most of the 1990s, but the gradual loss of jobs, rising poverty from 1995 onward, the economic recession starting in 1999, and the 2002 crisis led to palpable disillusionment with the policies promoted by the different governments.

In this context, the country papers for 1991, 1997, and 2000 defined a predominant role for the Bank compared to other international lending agencies, in support of some of the main priorities of the successive governments. In a framework of sweeping change in the social and economic structures, the country strategies did not lead to actions and policies that took a long-term view of the implications of those structural changes. In particular, the Bank's strategic contributions, based on its working experience with other countries, could have provided significant value added with respect to the adaptation of the social security model to a more polarized society, the scope of State reforms in a context of fundamental political restrictions, or the vulnerabilities associated with the move toward a more open economy.

These strategies gave rise to a large portfolio of operations, marked by a relatively large fast-disbursing component, equivalent to nearly 50% of the total value. The individual operations were both designed and executed in partnership with the national authorities, who felt a sense of ownership of them. The loans generally performed well in terms of disbursements, except those affected by the 2002 crisis, and also demonstrated the country's capacity for fiduciary administration. However, to execute operations, recourse was systematically made to setting up outside agencies (which is evidence of structural restrictions on the operation of the public sector in key technical functions). The contribution of these outside agencies to building up or institutionalizing the capacity of the beneficiaries has been limited.

The programs in the area of social development and equity supported the priorities of the different governments in a setting of institutional reform and growing attention to vulnerable groups. However, their effectiveness suffered as a result of a partial comprehension of the implications of poverty growth and its influence on a programmatic response that divorced measures to address emerging poverty from measures to reform social welfare structures. On the one hand, the program supported reforms of the traditional social policy institutions designed for a more equalitarian society, with a limited approach to adapting them to a social structure that was gradually changing or to the rise of structural poverty. On the other, a series of programs were carried out to address the symptoms of poverty, based on interventions of a temporary nature, as if those symptoms were a transitory phenomenon, which meant that the results were also limited in scope. Today, developing a structure to provide a comprehensive response to poverty, both economically and socially, has become one of the main items on the new government's political agenda.

The programs in the field of modernization of the State linked the Bank to the main reforms undertaken by the authorities, first from the standpoint of economic reform and demonopolization of public companies and, in the second half of the 1990s, with stress on the administrative reform of the public sector. Although some of them had a considerable fiscal cost, the conditionalities of the Bank's loans were useful for spurring progress by the different ministries involved or by the legislative branch. However, the scope of the reforms that were supported was constrained mainly by the scant political room to maneuver of minority governments and by constitutional prohibitions. As a result, except in the case of social security, such progress as was obtained—for instance the cutback in the size of the central government or the introduction of management by results—was unable to decisively channel processes for long-term improvements.

The programs in the area of economic openness and competitiveness were directed to promoting production in a series of traditional export sectors at a time when exports were being concentrated in neighboring markets, and to improving the investment climate through the development of financial markets. Although the programs to boost production were generally effective for the sectors concerned, the programs to develop capital markets and bank supervision did not anticipate the fragility of the banking system or cushion the impact of the 2002 crisis on it. Given the increased trade exposure to the Argentine and Brazilian markets until 1998, it would have been desirable to support greater diversification of export markets toward the global economy, which would also have lessened Uruguay's economic, commercial, and financial vulnerability to the behavior of its neighbors.

Last, the Bank's contribution to macroeconomic stability and fiscal sustainability translated during the 1990s into growing amounts of financing to support the conversion of the foreign debt under the Brady Plan. Except for some difficulties in the middle of the decade, the fast-disbursing component of the loans behaved beneficially and tended to address government demands for liquidity in periods of fiscal adjustment. However, Uruguay's current high level of debt with the Bank and the repayments programmed for the next two and a half years represent a situation that is historically anomalous in relations between the Bank and the country, with repercussions for the government's fiscal headroom in the medium and long terms. This situation can largely be explained by the relative stringency of the terms and conditions of the 2002 financial emergency loan.

Based on these findings, this report proposes the following recommendations for the most effective possible partnership to address the country's main development challenges in the coming years.

Recommendation 1. The analysis of the country's external debt position indicates that today the Bank is a factor in its macroeconomic stability and fiscal sustainability. Keeping this in mind, the Bank should establish a schedule for flows in the coming years that helps to resolve the country's critical financial situation and is attuned to the macroeconomic balances and the need for long-term fiscal savings.

Recommendation 2. This evaluation notes that performance was generally better in those areas where the Bank found a niche with strategic long-term relevance, where it could concentrate its operations over time. Continuing in this direction, the Bank should establish a future program that is geared to the objectives of the national development agenda—in some cases for more than one administration's term of office—focusing its efforts on the areas where it can have the greatest impact, particularly:

a. Promoting economic growth as the main variable around which the recovery program revolves, by providing more support for improvement in the investment climate and revisiting actions to improve the efficiency of the economic services provided by public companies, among other measures; and

b. Adapting the structure of the social welfare system to the new long-term challenges related to poverty and a more unequal social structure, and improving the system's quality.

Recommendation 3. The processes of formulating country strategies and technical-cooperation programs have resulted in a buildup of know-how and capacity, although at discrete points in time. To continue these efforts, the Bank's programming should be backed up by a program of studies and ongoing institutional development. In particular, support should be provided for the government to identify the best opportunities for: (i) strengthening or redefining the social security model; (ii) developing management for results in the public administration; and (iii) performing cost-benefit analyses of interventions during the design stage to determine, in particular, the returns from investment, sector, or emergency loans compared to the cost of the debt.

Recommendation 4. Analysis of the outcome and conditionality tables of the sector programs indicates that the latter frequently served as reference points and incentives for coordination of the different stakeholders involved. In the current context of fiscal constraints, the Bank should support the establishment of a programmatic results framework that would permit:

a. The establishment of financing relations with the ministries responsible for execution, based on periodic accountability and results-based performance, from a position of partnership with the finance authorities; and

b. Maintenance of flexible financing relations with the Bank that are compatible with periods when there is a need for liquidity, associating disbursements with progress in national programs rather than specific projects, and that are a more effective way of addressing emergency situations that might arise.

Recommendation 5. The analysis of the program points to the country's existing capacity for efficient and flexible portfolio design and administration, based on a programmatic approach. Keeping this in mind, the financing modalities used in future should make the most of the possibilities provided by the New Lending Framework, such as: (i) discretion to use national capacity in designing programs and local administrative systems; (ii) combination of sector, investment, and technical-cooperation programs for a single purpose; (iii) disbursement against results rather than for payment of inputs or compliance with procedures; and (iv) a single programmatic approach of the existing portfolio to the future, including the possibility of restructuring it.

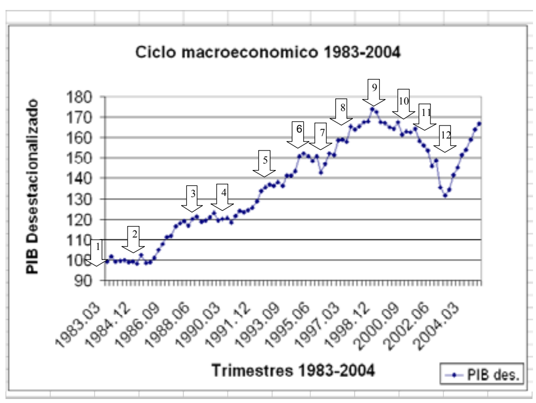
I. Country Context and Main Development Challenges

A. Context

1.1 Uruguay enjoyed an epoch of prosperity and well-being in the mid-twentieth century, when economic growth and growth in employment led to a middle class boom and foreshadowed a model of social wellbeing marked by heavy government involvement in the provision of jobs, economic services, social security benefits, and stability guarantees. The most significant period of growth in the economy since that time was during most of the 1990s, but the gradual loss of jobs, rising poverty from 1995 onward, the economic recession starting in 1999, and the 2002 crisis led to palpable disillusionment with the policies promoted by the different governments.[1]

1.2 The figure below presents some of the events that took place during those years which were relevant for the behavior of the economy.

Figure I.1
Macroeconomic cycle 1983-2004



Main events

1. Crisis in the financial system and bank bailout (1982)
2. Restoration of democracy (1985)
3. Referendum on adjusting social security liabilities (1989)
4. Signature MERCOSUR (1991)
5. Referendum on privatization of ANTEL (1992)
6. Entry into force of MERCOSUR (1995)
7. Law reforming the social security system (1996)
8. Investment grade classification of the sovereign debt (1997)
9. Devaluation of the real in Brazil (1999)
10. New outbreak of foot-and-mouth disease (2001)
11. Argentine financial crisis (2001)
12. Uruguayan financial crisis (2002)

1.3 **Period 1990-1994**. Five years after democracy was restored in 1985, president Lacalle's administration inherited a highly inflationary economy, marked by tight fiscal constraints stemming from the debt taken on to resolve the financial crisis of 1982, which was compounded by the fiscal cost of reforming the way in which pension liabilities were adjusted, approved in the 1989 referendum.[2] In harmony with the Washington Consensus model of macroeconomic stabilization established at the time, the government undertook a plan to restructure its foreign debt with international private banks, which was supported by the multilateral lending agencies, and a monetary stabilization plan based on maintaining the exchange rate within given preannounced bands, that would come to define exchange policy for almost the entire decade.[3] In keeping with these developments, a process of reform of the State and the economy was launched in this stage, with stress on eliminating monopolies, restructuring commercial banks, and developing financial markets.

Progress in eliminating monopolies lost impetus at the end of 1992 on account of a referendum in which Uruguayans voted against the privatization of the basic telephone services of the public telecommunications company (ANTEL), whose impact was decisive in terms of the scope and orientation of subsequent reforms.

1.4 In line with a policy based on a model of entering into the global economy through MERCOSUR, tariff barriers were rapidly dismantled, which hastened the disappearance of import-substitution industries and their replacement by service industries.[4] The change in the profile of production produced a shake-up in the structure of employment demand, adding between 1.5 and 2 points to the historic floor of structural unemployment which, coupled with the behavior of wages, led to a gradual worsening in income distribution. The reduction of 4.5% in real public sector wages between the third quarter of 1989 and the same period in 1994 and stagnation in private sector wages, which grew by 2.7% while pensions increased by 41%, produced an income redistribution to the detriment of work and the benefit of liabilities. The poor results in restoring wellbeing led to citizen dissatisfaction, which resulted in a change in government in the 1994 presidential elections, in a context of weaker political support for the traditional parties.[5]

1.5 **Period 1995-1999**. In this period, which was marked by a favorable regional context after a quick exit from the "tequila crisis," the second administration of President Sanguinetti returned to policies of competitive growth with stability, continuing the process of reform of the State, motivated by the lack of long-term sustainability in certain public spending items and the need to reform public institutions.[6] From the platform of a government coalition between the traditional parties, several necessary reforms were undertaken in social security, education, and the central administration.[7]

1.6 During this period, the economy made progress toward renewed stability, which translated into cumulative annual growth in per capita GDP of 2.8% a year and into curbing inflation, which fell to a single digit in the final years of the period. Macroeconomic stability and the fall in relative debt levels allowed the country to achieve investment grade for its sovereign debt in 1997. In combination with high liquidity in the markets and favorable rates in dollars, the reduction in country risk led to a significant increase in the net flow of international capital.[8] At the same time, there was significant growth in deposits in the banking system by nonresidents from the region, and there was a large expansion of domestic consumer and investment credit in dollars, particularly in the housing sector.[9] However, growth in the volume of financial business was not accompanied by significant improvements in development of the sector, which continued to operate with high market concentration in a small number of public banks with high portfolio exposure and limitations on the supervision exercised by the Central Bank.[10]

1.7 The entry into effect of MERCOSUR in 1995 accelerated a strong regionalization of trade relations until by 1998, MERCOSUR accounted for more than half of all the country's exports (33.8% to Brazil and 18.5% to Argentina), while current account income rose owing to strong tourism flows, particularly from Argentina. The government lowered the barriers to free trade and continued to support competitive modernization of agriculture, permitting its export volumes to grow. New agricultural investors and companies appeared and the process escalated later when the registration requirement for shares held by land owners was removed, thereby attracting international investors.

1.8 Growth in the economy did not bring improvement in social indicators. On the contrary, during this period they experienced a downturn which was the beginning of a prolonged negative trend. The unemployment rate continued at 10% of the economically active population (EAP) until the end of the government's term, which is higher than the historical level. After falling from 1985 to 1994, the number of people living below the poverty line began to rise in 1995. Inequality had begun to sharpen steadily, moving from a Gini index of 41.6 in 1995 to almost 44 in 1999. Due to the high geographic concentration of the low-income population, pockets of poverty and marginalized settlements, mainly in urban areas, began to appear in this period. Citizen discontent over social cohesion and job security was a factor that explained a new change in the governing party in 2000.

1.9 **Period 2000-2004**. Starting in 2000, the plans to maintain the reform program met with restrictions imposed by the government's parliamentary minority, the weakness of the coalitions, and the opposing interests of sector pressure groups. As a result, the reforms whose first steps had been taken—administrative reform, social security reform, improvements in regulations—came virtually to a standstill. Some attempted reforms were reversed through referendums, such as the liberalization of the fuel market or the water supply, or were revoked, as in the case of telecommunications.

1.10 The Russian crisis in 1997 and the Asian crisis in 1998 and their impact on the devaluation of the Brazilian real in 1999 were the prelude on financial markets to a series of negative shocks to Uruguay's trade balance, such as deterioration in the terms of trade, the new outbreak of foot-and-mouth disease in early 2001, and the Argentine and Brazilian crises. With the Argentine crisis, there was a temporary increase in foreign deposits from that country, in a setting of limited supervision and control over the private banks' risk exposure.[11] When international risk rating agencies withdrew their investment grade rating, the voluntary financial markets were virtually shut down, and the country was forced to finance itself through international reserves and with loans from the multilateral lending agencies. When suspicion arose that the deposits of nonresidents in the commercial banks that had been taken over by the Central Bank might not receive equal treatment, and doubt was cast on the validity of the government's implicit guarantee of the safety of deposits in the public banks, a run on the banks unleashed the most serious financial crisis in the country's modern history.[12]

1.11 The 2002 crisis exposed the shortcomings in bank supervision of offshore funds and in control of the positions of the public and private banks in terms of risk. The political system responded to the financial crisis with institutional accountability, respecting ownership rights and the legal rules of the game, and maintaining the independence of the Central Bank. In the context of the negotiations with the IMF, in August 2002 it was decided to establish a fund to stabilize the banking system for about US$1.5 billion, wholly financed by multilateral institutions, to provide the liquidity needed to maintain the system's banks.[13]

1.12 The impact of the 2002 crisis on the country's main economic and social indictors was considerable. GDP declined by 11% in real terms and there was dramatic shrinkage of credit and private investment.[14] The combined effect of the devaluation and the extensive external financial assistance from the multilateral agencies exacerbated the debt-to-GDP ratio, which soared to over 100%.[15] In 2003, the economy entered a strong recovery stage and today the levels of wealth prior to the crisis have been recouped, in a setting of favorable external circumstances.

Figure I.2
The financial crisis and the recovery

	Sept. 98 level (pre Russian crisis)	March 01 level (pre Argentine financial crisis)
Drop	-24.35%	-19.79%
Recovery	26.65%	26.85%
Gap closed (Dec. 2004)	96%	102%
Average 2005/Average 2004 (est.)		6%
Average 2004/Average 2003		12.36%
Average 2003/Average 2002		1.85%

1.13 The repercussions of the economic and financial crisis on the social indicators were considerable. The period between September 1998 and December 2004 saw a loss of wealth attributable to the crisis of more than 20%. The unemployment rate continued to climb until it had reached an annual maximum of 17% at the end of 2002 and a quarterly maximum of 19.5% of the economically active population, accompanied by a sharp reduction in real wages. The percentage of people living below the poverty line doubled in 1999 and grew to 30.9% in 2003 and 31.2% in 2004, while extreme poverty affected 4% of the population, putting the responsiveness of the existing social and institutional safety net to the test. Despite the recent economic recovery, the social impact of the crisis has not been reversed, which poses the challenge of restoring opportunities for the most disadvantaged groups in a context of significant budget restrictions.

B. Determining factors for the country's long-term economic and social development

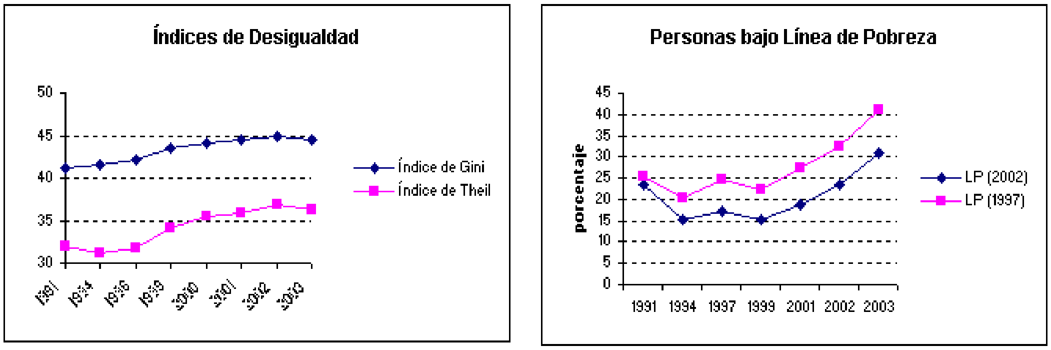
1.14 As noted in the preceding section, in the last five decades Uruguay has experienced volatile macroeconomic conditions, with economic policies that have ranged from tariff protection and heavy State intervention in the economy, to trade and financial liberalization, in some cases unilateral. In that period, Uruguay moved from being one of the most developed economies in terms of per capita income and social welfare in the middle of the twentieth century to an economy that is struggling today to stay within the group of middle-income countries.[16]

1.15 This long-term economic and social performance was caused by a series of restrictions and structural vulnerabilities that determined future capacity to pursue the objective of growth with equity. The following specific discussion of these economic, social, and political factors enables a strategic long-term perspective to be established for the analysis of the strategies proposed and, ultimately, for an evaluation of the capacity developed by the country with Bank support over the last 15 years.

1. Social development and equity

1.16 The model that identified Uruguay as one of the Latin American countries with low levels of inequality and less poverty began to fade in the last decade, and today the signs of structural poverty are growing. Inequality began to sharpen gradually in 1991, rising from a Gini index of 41 in that year to 44.5 in 2003. The unemployment rate climbed from 9.9% of the EAP in 1991 to 10.3% in 1995, and to a peak of 19.5% in the third quarter of 2002, falling back to 12.1% in the first quarter of 2005. This unemployment level includes a large percentage of unemployed who are unlikely to be able to rejoin the workforce.[17] In 1995, the percentage of poor individuals and households soared during the recession to unprecedented levels of 30.9% in 2003 and 32.1% in 2004, with a considerable percentage of this figure represented by structural or long-term poverty according to recent Bank estimates. Extreme poverty worsened during the crisis, rising from 1.5% in 2000 to 2.8% in 2003, and 4% in 2004. The factors that explain the worsening of poverty and the increase in inequality are the sharp reduction in formal sector employment, the increase in unstable jobs with no social security coverage, and the fall in real wages.[18] Persistent poverty and inequality levels despite the economic growth in the last few years, along with the recent rise in structural poverty, confirm that a considerable challenge exists in adapting social policy.

Figure 1.3



1.17 In parallel, the evolution and projections for the demographic pyramid in Uruguay show a gradual aging of the population that causes a long-term imbalance between the economically inactive and active populations. This trend can be attributed to the steady decline in the birth rate, the drop in the mortality rate, and alarming figures for emigration, particularly by young people. Official estimates indicate that close to 122,000 Uruguayans left the country between 1996 and 2004 owing to the economic crisis, a high percentage of them professionals and university graduates.[19]

1.18 Getting social policies to respond to the rise in structural poverty and marginality poses a considerable challenge, particularly considering the present fiscal restrictions. The current authorities have placed this issue front and center on their political agenda. Social spending is highly skewed towards a ministerial structure designed for an integrated society (social security, health care, and education) which absorbs 89% of public spending. The country does not have a social welfare structure targeted to the poorest groups, as yet. As a result, today, one third of poor households do not receive any benefits, and the figure rises to more than half if retirement and pension payments are excluded.[20] In a context of severe fiscal restrictions, the significant increase in the number of people who demand social assistance casts doubt on the responsiveness and fiscal sustainability of the model on which social welfare policy was traditionally based.[21] The spending reallocation demanded by these trends probably goes beyond simply optimizing the way in which the existing model operates and greatly exceeds the scale of improvements that could have been considered in the past.

2. Reform of the State

1.19 Historical experience with the reform of State institutions in Uruguay indicates that it is a gradual and long-term process that is determined mainly by constitutional prohibitions.[22] On this account and because of the process by which it was established, even after several reforms Uruguay's public sector continues to be large with multiple layers.[23] From the organizational standpoint, although attempts have been made to define spheres of operating responsibility, unnecessary duplication of functions persists and, in some cases, there is an imbalance between the functions of an agency and the number of qualified professionals on its staff. The capacity of public servants has remained at levels below the Latin American average, particularly because of the aging of employees and the low, rigid, and inequitable wage structure, marked by insufficient incentives.[24]

1.20 The reforms undertaken to cut costs and boost public sector capacity, particularly in education, health care, and the central administration, were concentrated in the second half of the last decade and later tailed off owing to the difficulties in garnering consensus, fiscal restrictions and, later, the need to manage the crisis. The reform decisions were, from the outset, subject to the feasibility consideration that they might be submitted to a referendum, which limited their scope and depth.[25]

1.21 During the first half of the 1990s, a series of initiatives were taken to liberalize the public monopolies. They lost impetus because of the outcome of the referendum on privatization of the public telecommunications company (ANTEL) in 1992, whose impact was a determining factor for the scope of the economic reforms. With some exceptions, such as the electricity generating markets, port services, railway freight transport, and cellular telephony, this referendum meant abandoning the road to privatization that leads to opening up markets or private capital participation and the creation of regulatory agencies. In 2003, a new referendum rejected opening up the national fuel company (ANCAP) to private capital, reconfirming strong public opposition.

3. Economic openness and competitive development

1.22 Since 1990, a strategy based on a model of entry into the global economy through MERCOSUR has taken root, which has helped to spur the economy as a prelude to a process of liberalization on a larger scale. In those years, however, this model of openness led to a position of financial and commercial vulnerability and a new profile for the country's productive specialization. The influence of neighboring countries on the behavior of Uruguay's economy has been particularly visible as they followed and abandoned their respective stabilization plans, including of course the most recent financial crises.[26] As a consequence, Uruguay's economic cycle became more closely correlated with the behavior of the Argentine economy, with the correlation growing between 1991 and 2003 from 0.2 to 0.6.[27]

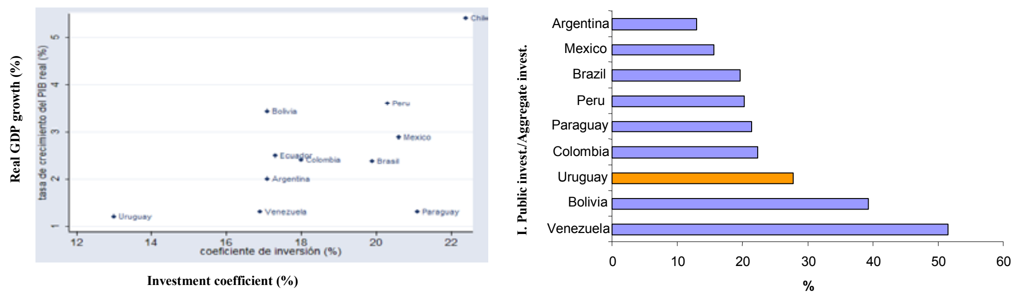
1.23 As for trade, experience over the period makes greater diversification of export markets in the world economy desirable. This would also have the effect of cushioning the country's vulnerability to the behavior of the neighboring markets. During the 1990s, the process of joining MERCOSUR adapted, while significantly exposing, Uruguay's products to the nature of the demand on its regional market, which subsequently diminished after 1999 on account of the crisis in the Argentine and Brazilian markets. These aspects of regional dependency are compounded by the volatility of international prices for agricultural products, which are the country's main export.[28] The deliberate acceleration of the tariff reduction timetable, which eliminated tariffs for Argentina and Brazil, and the promotion of the lowest possible common tariff left large sectors of the economy exposed at a time when the exchange rate was appreciating. This contributed to the long-term transformation of the profile of the country's productive specialization during the 1990s into an economy fundamentally based on services, which grew from 50% to 65% of GDP, in tandem with a transition in the entrepreneurial fabric to smaller companies.[29] These rapid changes led to growth in frictional and structural unemployment, hand-in-hand with expansion of the informal economy.

1.24 The development of long-term credit and capital markets continues to be a bottleneck for raising the chronically low levels of investment that determines economic growth. The average investment coefficient in the country over the last decade was 13%, which is considerably lower than in several other Latin American countries with a similar level of economic and social development and has repercussions for the real economic growth rate. Over the same period, a substantial part of the country's aggregate investment (27.7%) was provided by the government, which is a relatively higher percentage than in most of the comparison countries.

Figure 1.4

Investment coefficient and GDP growth rate in Uruguay compared to other Latin American countries – Average 1990-2002

Percentage of public investment out of aggregate investment in Uruguay compared to other Latin American countries – Average 1990-2002



Source: ECLAC Statistical Yearbook, cited in a recent study commissioned by the Bank: "Sostenabilidad Fiscal y de la Deuda en Uruguay [Fiscal sustainability and debt in Uruguay]," FIEL, August 2004.

4. Macroeconomic and fiscal sustainability

1.25 Fiscal and macroeconomic sustainability in Uruguay are closely linked to the public sector's gross debt and, in particular, to the levels of its foreign debt. Since 1990 and as a consequence of the financial crisis in the early 1980s and the customary bailout of the banking sector, the Uruguayan government embarked on a strategy of conversion of the private foreign debt to multilateral debt under the Brady Plan. After presenting relatively healthy levels throughout the decade, the domestic and foreign debt levels in the country today as a consequence of the 2002 crisis have exceeded the peak initially reached as a consequence of the earlier crisis.[30] The expansion of the 2002 debt, based on a medium-term loan portfolio, was out of step with the nature of the problem, since it was not a transitory crisis or one with a short macroeconomic recovery cycle, and led to a significant concentration of debt falling due within short maturities. The debt repayment demands will require a primary surplus in the order of 4% of GDP in the coming years according to the government's plans, to the detriment of fiscal headroom to cover the public investments necessary for economic growth and to reduce inequity in income distribution and poverty.

1.26 The historical evolution of public finances has behaved in a markedly procyclical fashion, both from the spending side and from the income side, which has stood in the way of generating fiscal savings to relaunch the economy or protect social spending in times of stagnation or recession. In a context of public spending that is highly resistant to reduction, the revenue structure based mainly on indirect taxes experienced several consecutive rises in tax rates in the 1990s, climbing to very high levels of tax pressure. The need to optimize potential revenue by broadening the tax base in a context of high tax evasion and failure by the administration to press claims has not yet been tackled through structural measures related to strengthening the tax administration or to reforming the tax system.[31]

II. THE BANK'S PROGRAMMING

2.1 This evaluation covers three multiyear programming exercises by the Bank, approved in 1991, 1997, and 2000, which correspond with a certain time lag to the five-year planning periods used by the administrations of Presidents Lacalle, Sanguinetti, and Batlle. During this period, there was a transition in strategy from the earlier model that involved decades of financing for investment projects, particularly infrastructure, to a portfolio with a strong sector component in a setting of the structural reforms undertaken by the different governments.

2.2 In general, the strategies involved areas of intervention that were in line with national policy guidelines and, in most cases, were priorities for the national authorities. While in 1991 the strategy promoted a market liberalization policy, freer trade, and economic reform reflecting the Washington Consensus, in 1997 and 2000 programming turned toward support for government administrative reform initiatives. One of the advantages of this approach to the country is that the Bank's program developed with a strong sense of ownership by the national authorities. However, under this approach, the country papers did not promote policy actions in key strategic areas, most particularly in relation to the model of welfare and social solidarity demanded by the citizenry, by establishing conditions for its viability, or attenuating the risks and vulnerabilities on the economic plane.

2.3 Although the definition of the strategic areas for intervention demonstrates a position that is appropriate for the national political scenario, indicators for outcomes and strategic goals for the Bank's portfolio are spelled out only in the 2000 country paper, but were generic and difficult to ascribe. The objectives of the interventions that the Bank supports are not defined in terms of an objective image of their outcomes, much less quantification or qualification of the expected goals, which makes it difficult to evaluate the linkage of the outcomes of the projects to the effectiveness of the strategic outcomes for the portfolio. The relative lack of precision of the strategic objectives and the prominence of fast-disbursing loans in the programming limit in some cases the ability to ascribe outcomes to specific Bank programming.

2.4 Owing to the association between the Bank's programming and the five-year planning exercises, the predictive capacity of the pipelines of projects included in the country papers was considerable, although it tended to extend beyond the three years of the projected pipeline to the actual five years, also on account of the relative rigidity of the country's five-year budgeting processes. As the following table shows, owing to the extensive reprogramming associated with the 2002 financial crisis, the most recent country paper was less anticipatory than the earlier ones and involved a greater degree of improvisation.[32]

Table 2.1
Degree of anticipation of the programming

Programming cycle	Anticipation rate		Improvisation rate	
	Amount	Number	Amount	Number
1991-1995	77%	74%	26%	30%
1996-1999	88%	75%	9%	14%
2000-2004	69%	75%	57%	36%
Total	80%	74%	35%	26%

2.5 The strategy papers included an analysis of the country's main development challenges over time as the starting point for programming. An analysis focused on the development challenges over time shows that they remained substantially the same, although some showed signs of becoming permanent and more acute. In this framework, the following sections examine whether the strategies set forth programmatic objectives that were relevant and coherent and contained sufficient analysis of the risks compared with the evolution of the challenges and the country's vulnerability, organized on the basis of the programming areas set by the Bank.

A. Social development and equity

2.6 The Bank's programming focused on top priorities for the country's authorities in a framework of institutional reform and attention to vulnerable groups. However, the diagnostic analyses included throughout the programming only treated poverty intermittently, and this key theme was not included among the country's main medium- and long-term challenges.[33] Although the 1991 strategy announces that poverty increased as a result of the restructuring of production, the 1997 and 2000 strategies do not take this up again, and present an analysis centered on the appearance of pockets of poverty but ignore the general trend for it to worsen.[34] Probably as a consequence, attention to poverty was based on a strategic approach that viewed it as an exception during the 1990s and as requiring corrective measures during the crisis, and that did not influence the adaptation of the social welfare structure.[35]

2.7 Despite these trends toward the gradual establishment of a more dualistic society, programming responded by divorcing attention to emerging poverty from the reform of the social welfare structure. As a consequence, the strategies included a series of compensatory proposals that dealt with the symptoms of poverty as if they were temporary phenomena, on the one hand. On the other, they focused on reforms of traditional social policy models that were designed for a more equalitarian society, without making any strategic contribution for their functional adaptation or fiscal feasibility, given the gradual onset of a more polarized society.

2.8 With regard to reform of social policies, such as education and health care, the Bank's programming maintained a strategic position that was consistent with an analysis that described aspects of inefficiency, regressiveness, and a disproportionate fiscal burden, but largely ignored the behavior of social indicators. Based on that approach, the programming proposed support for organizational reform in each of these fields, but it was intended more to improve the supply than to adapt the institutions to the new characteristics of demand, and there were obvious shortcomings in addressing aspects that were more closely related to long-term institutional development.[36]

2.9 To the detriment of its strategic value, the Bank's programming in this area failed to support the government in establishing a comprehensive vision that would permit it to orchestrate the proposed measures for the reform of social spending with the measures proposed in the programs for reform of the State, which were developed in parallel.[37] As a consequence, some of the crosscutting programs had very tenuous links with the relevant line ministries or developed parallel structures that were not consistent with the objectives of the organizational restructuring. Other programs, such as the reforms in health care or education, were excluded from the 1997 administrative reform strategy, which considered them to be separate programs, although they were subsequently incorporated into the 2000 strategy.[38]

B. Reform of the State

2.10 The Bank's strategies consistently supported the main processes in reform of the State, first with emphasis on economic reform and demonopolization of the public companies and, starting in 1997, supporting the central objective of the authorities which was administrative reform of the public sector, taking opportunities for reducing the structural fiscal deficit as its guide. However, this fiscal focus limited the Bank's strategic contribution to thinking about the scope and timeliness of the reforms in a context of constitutional prohibitions and scant political latitude, which became prime constraining factors for both the administrative reform and the demonopolization of public companies.

2.11 Although the 1991 strategy analyzes administrative reform as one of the most important challenges for the government, the Bank did not decide to play a major role in this field until the second half of the decade.[39] Social security reform was diagnosed in the 1991 country paper as the structural determinant of the chronic fiscal deficit, and reform of the central administration was the first necessary step toward the strategic objective of reform of the State.[40] However, in the context of minority governments exposed to constitutional referendums and marked by a ministerial portfolio divided between political parties, the scope of these reforms had to be adjusted and was frequently constrained by the latitude that could be negotiated politically.

2.12 Programming of the reform progress reproduces a bias toward reform on the spending side that prevailed for the national authorities, with no consistent emphasis on the taxation area which has a large potential influence on the state of public finances. Although the 1991 strategy attaches prime importance to reform of the tax area, it is only taken up again as a central theme in the 2000 strategy and, in practice, structural tax reform that is more consistent with the need to clean up public finances and stimulate private activity is still pending.[41]

2.13 The reform of the public companies was given priority treatment in the 1991 strategy, consistent with the full sway of the Washington Consensus. Once the difficulties of this strategy were uncovered as a result of the constitutional referendum in 1992 on ANTEL, the programming pragmatically abandoned the line of support for the better efficiency of the public companies which, given their importance for the competitiveness of the economy, reappears in 2000, although no operations were approved.[42]

C. Economic openness and competitive development

2.14 The Bank's strategies since the early 1990s consistently supported the model of entering into the international economy through MERCOSUR, which has given rise to a profound transformation of the country's productive structure and its business fabric. However, the Bank's strategies were not able to promote long-term policies to diversify export markets and cushion the economy's long-term vulnerability in relation to its main trading partners or the influences on the labor market of the productive restructuring process. Given the size of the challenge of opening up the economy, the Bank's portfolio was destined to be too narrow. In this particularly demanding context, although the specific operations that were programmed were individually pertinent, the Bank's strategy in the area of competitiveness proposed a portfolio that emphasized certain specific productive sectors, complemented by a set of initiatives that were scantly coordinated with each other for competitive development and conditions that would favor investment.[43]

2.15 Early in 1991 the programming noted the possibility that the entry into force of MERCOSUR could lead to high mortality among companies in some sectors, with economic and social repercussions.[44] However, the selection of the sectors to be supported did not respond deliberately to criteria that make long-term competitive advantages compatible with the need to adapt to the external shock.[45] Despite the influence of the restructuring process on growth in structural unemployment, the Bank's strategies did not support Uruguay in undertaking programs to support productive development in sectors that, in addition to having growth potential, also responded to job creation considerations.[46]

2.16 With regard to the vulnerability of the financial markets, the Bank's strategies echo the complacency over the regulatory framework and bank supervision that existed in the 1990s, based on the approval of a series of rules in line with the Basel standards. The Bank's programming first promoted and later validated a model of bank supervision that permitted legislative changes to be promulgated in law but whose actual operation was limited, which in the end left the system highly vulnerable to the 2002 financial crisis.[47]

D. Macroeconomic stability and fiscal sustainability

2.17 The country papers consistently served as support for continued growth in financing for Uruguay, in accordance with the demands of the national authorities, but they were not systematic in their analysis of financial exposure from the country perspective. In the context of foreign debt conversion linked to the Brady Plan based on repurchasing the country's bonds from foreign commercial banks, in the 1991 country paper, the Bank announced its decision to become the country's main source of external financing in response to government demands.[48] In practice, the Bank has supported and strengthened its position of financial importance as the main external creditor during the three subsequent programming periods, supplementing its disbursements with the unprogrammed financing extended during the 2002 crisis.

2.18 In an atmosphere of close cooperation between the Planning and Budget Office, the Ministry of Economic Affairs, and the Bank, the mix of sector and investment loans envisaged in the strategies gave precedence over time to fast-disbursing loans in periods of high demand for liquidity and fiscal adjustment, consistent with the agreements signed with the IMF. The percentage of sector loans listed in the programming stage was consistently above the 30% of the lending program announced in the 1991 strategy.[49] Actual approvals during the three periods and most particularly on the occasion of the 2002 financial crisis corroborated this programmatic decision, rising to more than 50%, including support during the financial emergency.

2.19 Despite the size of the country's foreign debt, the sustainability scenarios and their monitoring have not been treated systematically from one strategy to the next. Given the starting situation, the 1991 country paper set a gradual reduction in the foreign debt as one of its general strategic objectives which was ultimately reflected in the objectives set forth in the sector portfolio in this cycle.[50] The treatment of the risk of excessive exposure was not dealt with consistently in the 1997 or the 2000 country papers, despite the fact that the weight of the debt on GDP in this last case had risen to levels equivalent to those reported in 1990.[51] The country's debt level has been exacerbated, rising to unprecedented levels after the 2002 crisis.

2.20 As for the risk of financial emergencies, the 2000 country paper had the merit of foreseeing the destabilizing consequences that unanticipated measures and policies originating in the region's economies or the rest of the world could have for the country.[52] However, the program did not reflect a vulnerability scenario, making it less likely that the Board of Executive Directors would discuss possible precautionary measures with more appropriate financing terms.

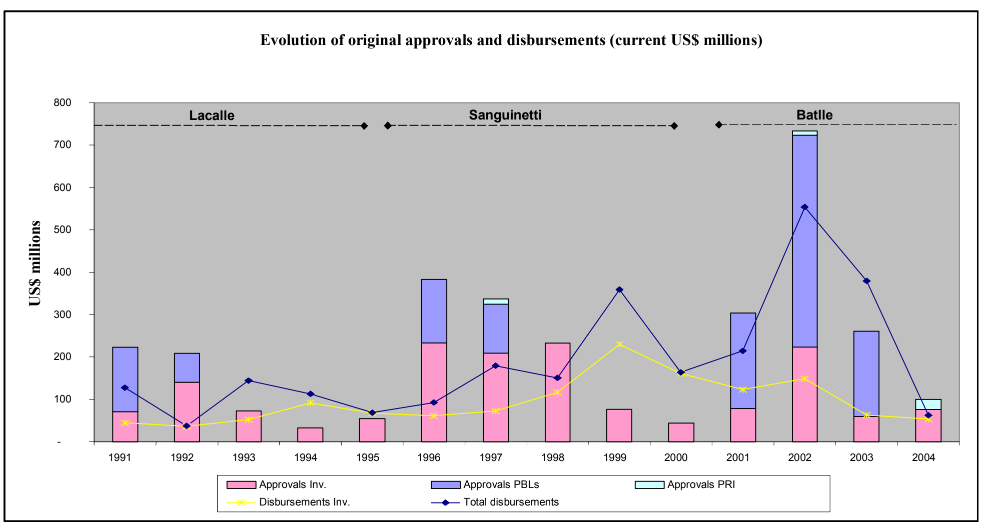
III. EXECUTION OF THE BANK'S PROGRAM IN URUGUAY

3.1 Execution of operations in Uruguay has performed well in comparison with other portfolios in the region. The public institutions responsible for the fiduciary administration of the loans and internal control pose low risk, although project execution has, as a rule, been the responsibility of executing agencies contracted for the purpose. The fiscal restrictions caused by the crisis slowed execution, particularly of the investment program, giving rise to partial cancellations and leaving a balance of projects with scant disbursement capacity.

A. The Bank's portfolio in the period 1991-2004

3.2 **Approvals**. In the period covered by the present evaluation, 44 loan operations were approved for an original total of US$3.061 billion, evenly distributed between investment projects and fast-disbursing loans (52% investment, 47% fast disbursing, and 1% PRI).[53] Uruguay ranks among the three borrowing members countries with the highest proportion of approvals in 1991-2004 covered by fast-disbursing resources, after Colombia and Argentina, which also received sizeable support on the occasion of financial emergencies.

Figure 3.1

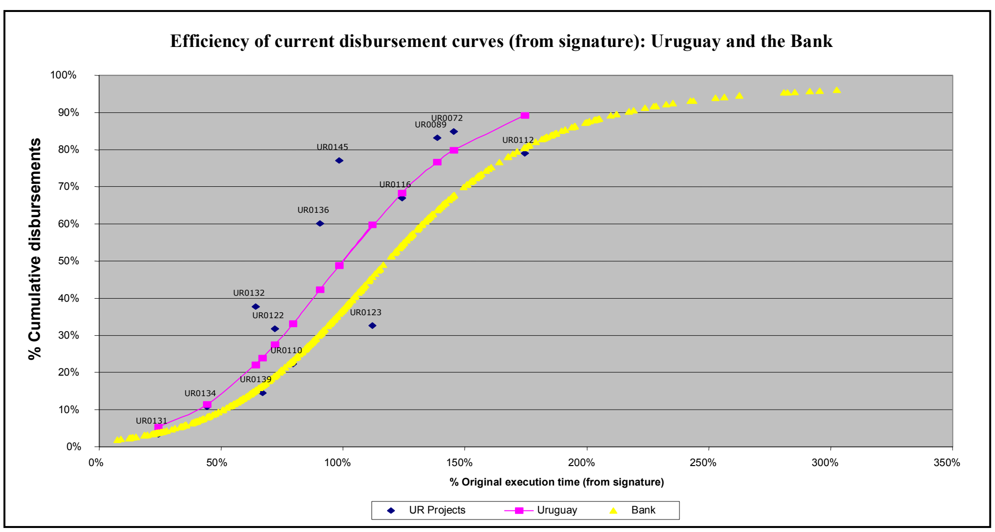


3.3 The current amount of total approvals in the period is just 3% lower than the original, which reflects a low level of cancellations compared to other countries. However, 82% of the amounts cancelled were in 2002 and 2003, as a result of the portfolio restructuring agreed on by the country and the Bank on account of the financial crisis and, later, the currency devaluation.[54] Figure 3.1 shows the annual evolution of approvals by type of loan.

3.4 Total approvals have grown during the programming cycles from US$591 million in the first cycle (14 projects) to US$1.44 billion in the third (16 projects). The marked growth in the last cycle studied is explained by the approval of four fast-disbursing loans for US$925 million, 55% of which were concentrated in the 2002 crisis. An analysis limited to the investment loans shows different behavior, with a peak in the second cycle and similar levels in the first and third.

3.5 **Disbursements**. Total disbursements, like approvals, show a clear increase across cycles, reaching unprecedented levels in 2002. The disbursements of sector loans generally show beneficial sensitivity to periods of high demand for liquidity during fiscal adjustments, except in the mid-1990s. Although disbursements of investment loans tended to increase until 1999, after that year they declined somewhat and in 2004 fell to one of the lowest levels in the entire period analyzed. The result has been an aging of this portfolio, which is reflected in the increase since 2002 in the number of average years of life of projects from approval to disbursement.[55] The policy of curbing spending, particularly investment spending, that the government mostly began to follow in 2001 has led to a lower level of disbursements of the investment loans.

Figure 3.2



3.6 The efficiency-of-disbursement curve (EDC), as an approximate measure of the pace of the disbursements of a given group of projects compared to others, shows that the investment loan portfolio currently in execution in Uruguay is disbursing faster than the Bank average.[56] However, looking at the behavior of Uruguay's EDC over time, the pace has been slowing since 2001, despite a slight improvement in

2004 that can be explained by the increase in disbursements of the oldest projects in the portfolio.

3.7 **Execution capacity**. The execution capacity of Uruguayan institutions and their internal control mechanisms are generally adequate.[57] According to the Country Financial Accountability Assessment, the fiduciary risk presented by Uruguay is relatively low.[58] However, in response to the organizational restrictions on the public sector, the rule of thumb established in Uruguay for project execution has been to create and maintain for lengthy periods executing units with a large number of contracts.[59] Apart from limitations on the institutionalization of projects and institutional development, this practice has in some cases led to substitution effects or to the duplication of functions.

B. The Bank's supervision systems

3.8 **Supervision ratings**. The slowdown in portfolio disbursements is consistent with the information provided by the Bank's supervision systems.[60] As can be seen in the following table, the percentage of projects with problems in implementation progress (IP) or low classifications in terms of the materialization of assumptions (AS), and projects on alert status calculated by the PAIS system tripled in 2002, and both indicators remained high over the next two years.[61] Also, the 'problem' projects (rated by Management as having low probability of meeting their development objectives–DO) have risen since 2002.[62]

Table 3.1
Indicators calculated using IP/DO/AS ratings in the PPMRs* and the PAIS system

	1998	1999	2000	2001	2002	2003	2004
Projects in execution	20	21	19	22	23	22	22
% projects with DO risks/alert	5%	5%	8%	7%	22%	25%	26%
% problem projects (low DO)	0%	0%	0%	2%	0%	5%	7%
% projects on alert status in the PAIS	5%	14%	16%	9%	31%	27%	23%

Source: OVE estimate based on the IDB Datawarehouse (IIWP.PPMRSummary).
*Annual values calculated as the average of the two yearly PPMRs.

3.9 The types of problems mentioned in the PPMRs as explanations for the low IP and DO classifications have tended to grow since 2001, particularly the problems of insufficient institutional capacity and failure by the executing agency to take ownership.[63] An analysis of the frequency with which problems identified during the PPMRs are mentioned shows that difficulties stemming from fiscal constraints recurred most often, followed by problems with the institutional capacity of the executing agencies.[64] The trend reflects a considerable increase in these factors since the 2002 financial crisis. A complementary analysis of the anticipation of risks in the design of projects and their actual occurrence indicates that 92% of the cases of counterpart difficulties and 52.7% of the problems with the capacity of the executing agencies were anticipated in the design, but could not be mitigated during execution.[65]

3.10 **Performance of supervision**. As can be seen in the following table, Uruguay's level of compliance is acceptable and in harmony with supervision requirements.

Table 3.2

Instrument	Required	Complied	% Compliance
PPMR	156	152	97
PCR	26	26	100
Technical visits	516	476	92
Financial visits	160	143	89
Midterm evaluations	8	6	75
Ex post evaluations	14	4	29
Final evaluations	5	2	40
Audited financial statements	156	155 (14 qualified)	99 (9% qualified)

3.11 The positive performance of supervision was confirmed by the Completeness Monitoring Index (CMI) for 1998-2001, which ranks Uruguay as the highest in the whole region, with 93% compliance with the Bank's periodic and compulsory monitoring requirements.[66]

IV. EVALUATION OF RESULTS

A. Introduction and methodology

4.1 The 1991 and 1997 country papers identify general objectives, sector programmatic areas, and project pipelines which, although they do allow operations to be classified in a useful way for evaluation, do not specify the planned strategic outcomes.[67] Only the 2000 country paper includes a table of Bank action in Uruguay that defines indicators for macroeconomic outcomes and government policies developed with the Bank's contribution, without delimiting the part that can be attributed to the program. Of the 32 goals established at that time, 25 were not achieved, largely due to the consequences of the crisis in this last cycle and its repercussions on programming.[68]

4.2 Keeping these circumstances in mind, this evaluation of results took as its primary reference the sets of objectives planned in the design of the individual operations approved by the Bank in the period 1991-2004, to examine them on the basis of the programmatic areas that define the strategies. The analysis method used consisted of the four following sequential steps:

Step 1. Study of evaluability of the design documents for projects and programs (project reports).

Step 2. Identification of the information on outcomes (effects) compiled in the Bank's monitoring instruments (PCR or where there is none, the most recent PPMR).

Step 3. Independent validation of the outcomes obtained, based on official statistics or evidence obtained in the country.

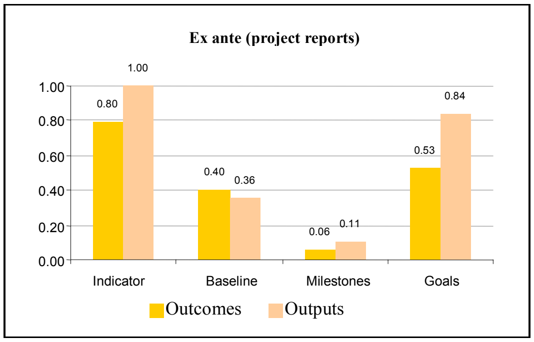
Step 4. Analysis of the outcomes found for each of the programmatic areas and long-term challenges set in the country papers.

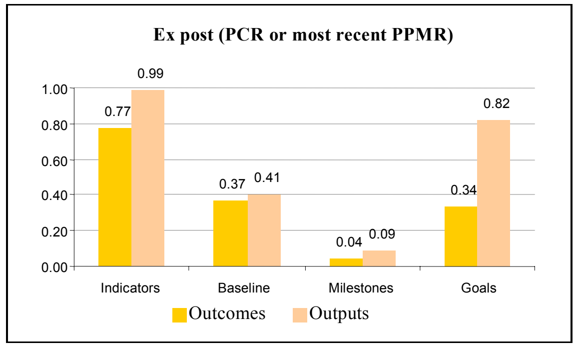
B. Evaluability of operations

4.3 To prepare this report, an initial analysis was made of the evaluability of operations using the methodology developed by OVE for that purpose.[69] This analysis determines whether the project reports identify the elements indispensable for evaluating results, particularly indicators, baselines, intermediate milestones, and above all, specific goals, in the original design and during monitoring.

4.4 As can be seen in the figures below, the projects studied clearly identified their output indicators, and to a lesser extent their outcome indicators, which are what this evaluation focuses on. For the outcome indicators in particular, the presence of the baselines and the specific goals to be achieved were the exception in the project designs, which placed limitations on performing a comparative analysis with what had been planned, which would have been desirable. In some cases, the monitoring reports (PCR or the most recent PPMR) incorporated outcomes (effects) indicators that could be used for their validation, although only for one out of every two operations included in this analysis.

Figure 4.1
Evaluability indicators for approved investment projects (1991-2004)





C. Analysis of results

4.5 As mentioned in Chapter I, in recent years the country has experienced a long-term transformation in its productive structure, the most serious crisis in its modern history, and more recently, a very significant policy change as an expression of citizen opinion. Given these factors, the long-term development challenges that were established in the strategies since the early 1990s either continue to be fully current today or have gained in importance.

4.6 The following sections present the results for each of the four strategic areas identified in the Bank's programming. As a reflection of the methodology applied, each section is composed of a presentation of each programming area in terms of the development objectives related to the operations, a summary of the information generated by the Bank on the outcomes for each of the areas and, last, an analysis of the results.

1. Social development and equity

4.7 In the transformation of Uruguay's social structure, the Bank's operations in this area had the following objectives: (i) to support the reform of secondary education; (ii) to back reform of the health care system; and (iii) to promote the efficient organization of social spending. According to this evaluation, eight of the 18 outcomes in these areas produced medium or high results.[70] The following table summarizes the situation before and after the programs and serves as a framework for the analysis that follows.

Table 4.1
Summary table of the results of the social development and equity portfolio

Objective	Situation at start of period	Situation at end of period
Reform of secondary education	Secondary education with high drop-out rates, and quality not sufficiently recognized by the labor market. Education administration system inefficient and with management problems.	Secondary education reformed and of better quality, without sufficient response by the labor market given the crisis. System structurally intact and expanded, with persistent management problems.
Reform of health care	A health care system with financial and management problems and differentiated by socioeconomic group (private, mutual, and public subsystems).	A system that is structurally identical with: * A mutual subsystem that alleviated its financial crisis without resolving it. * A public system whose capacity has been overwhelmed by the increase in users.
Organization of social spending	A universal social security model, sectoral in nature and not prepared for the appearance of vulnerable groups. Social spending threatened by liquidity requirements and cutbacks stemming from the crisis. An extensive infrastructure but with room to expand coverage.	A structurally identical model without tested capacity to act as support for social policies. Some protected programs although not the ones most closely linked to poverty. More infrastructure, but not necessarily distributed in function of unmet basic needs.

4.8 As mentioned below, social policies have not been capable of adapting effectively to the growth in marginalization and poverty, or to the need to create opportunities, particularly job opportunities. In fact, faced with the gradual appearance of a dualistic society, the Bank's programmatic response did not succeed in supporting the adaptation of the social welfare structure to this new reality. As a consequence, it supported initiatives to reform health care and education systems designed for a more egalitarian society on the one hand and, on the other, it tackled emerging social problems as if they were temporary, based on individual projects that diluted the interventions and created parallel cost structures. As we will see, in both cases this initial strategic approach made it possible to obtain the outputs of the operations but limited the scope of their outcomes. The following sections present an analysis of the results.

a. Reform of secondary education

4.9 In the period 1991-2004, the Bank financed a series of investment projects intended specifically to support the National Public Education Administration (ANEP), mainly focusing on secondary education.[71] According to the loan proposals, support for education reform had the following two objectives: (i) to improve the quality, efficiency, and equity of technical and secondary education; and (ii) to support reform of sector institutions, management, and the regulatory framework.[72] The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.2
Analysis of information on results

Outcome	**Bank**		**OVE**
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Secondary education:			
Improvement in quality (UR-0107, UR-0132)	Yes	Yes	Medium
Improvement in equity (UR-0107)	No	No	Limited
Improvement in efficiency (UR-0107)	Yes	No	Medium
Technical education:			
Adaptation to labor market requirements (UR-0018)	No	Yes	Medium
Education administration:			
Institutional and management improvement (UR-0107)	No	No	Limited
Regulatory reform (UR-0107)	No	No	Limited

4.10 An analysis of the outcome indicators (see supporting document 1) shows that achievements in education converged more on pedagogical aspects, where the results were positive, than on institutional development and better management, where the fundamental bottlenecks have persisted. In particular, equity in the distribution of secondary education and recognition by employers of the quality of teaching were affected by the recession and, consequently, the impact was limited compared to the challenges associated with a student body with wider income disparities and an increase in youth unemployment.

b. Reform of the health care system

4.11 The Bank financed a program to reform the health sector as a response to the financial problems and need to reform the existing health care model.[73] According to the loan proposal, the program had the following objectives: (i) to improve the efficiency, equity, and quality of health care services for citizens; and (ii) to support strengthening of the private and public subsystems and the regulatory framework for the sector. The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.3
Analysis of information on results

Outcome	Bank		OVE
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Health care services:			
Quality of care and improvement in health indicators (UR-0133)	No	No	Medium
Equity in care (UR-0133)	No	Yes	Limited
Heath care administration and institutional development:			
Institutional and management improvement (UR-0133)	No	No	Limited
Improvement in the financial situation of the mutual subsystem	No	No	Medium
Regulatory reform (UR-0133)	Yes	Yes	Medium

4.12 The analysis of the outcome indicators (see background document 2) indicates that this program served in particular to alleviate the capital deficit of the mutual subsystem in 2001, preventing a possible collapse of the health care system as a whole, but it did not produce the reforms envisaged in its design to develop a more equitable, better quality, and financially viable supply of health care offerings. In particular, the significant growth in recent years of the number of uninsured who depend on the public system has not favored the equity outcomes proposed in the design.

c. Rationalization and organization of social spending

4.13 Since the start of the last decade, the Bank carried out a series of projects intended to target social assistance to the poorest groups in general. Under the impact of the crisis, projects were added to target more specific groups, such as people living in marginal urban areas and at-risk children and their families.[74] According to the project reports, these operations had the following objectives: (i) to organize and rationalize social spending for better targeting of vulnerable groups; (ii) to improve the standard of living of vulnerable groups; (iii) to protect social spending programs during the 2002 financial crisis, to keep it from having an impact on the poorest sectors; and (iv) to support the development of social infrastructure. The following table shows the outcomes for this objective, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.4
Analysis of information on results

Outcome	Bank		OVE
	Initial target indicators	Monitoring indicators	Attainment level
Organization and targeting of social spending:			
Better targeting of social spending (UR-0024, UR-0087, UR-0134, UR-0123)	No	No	Limited
Standard of living of vulnerable groups:			
Improvement in the standard of living of the neediest groups (UR-0024)	No	Yes	Limited
Improvement in the standard of living of at-risk children and families (UR-0134)	No	No	Limited
Improvement in the standard of living in informal settlements (UR-0123)	No	No	Limited
Protection of social spending and social impact during the crisis:			
Protection of social spending during the 2002 crisis (UR-0151)	Yes	Yes	High
Impact of the crisis on the poorest groups (UR-0151)	No	No	Limited
Provision of social infrastructure:			
Improvement in the standard of living	No	No	Medium

4.14 The analysis of the outcome indicators (see background document 3) shows that owing to the focus of the individual projects in this portfolio, although impact was achieved in terms of improving the standard of living of the groups concerned, the achievement levels in developing capacity and effective management of social spending for vulnerable groups have been limited. In fact, at the end of the period evaluated, it is clear that the capacity developed by these programs was unable to set a precedent and become institutionalized, which would have produced considerable present value in the framework of the current social emergency program. With respect to social infrastructure and water and sanitation in particular, the Bank continued its decades of support, which translated into an expansion of coverage whose impact on the standard of living was, unfortunately, not subject to systematic monitoring.

2. Reform of the State

4.15 The Bank has provided continuous support for reform of the State through an abundant portfolio of investment and sector loans and technical-cooperation projects.[75] The programs for reform of the State had the following objectives: (i) to modernize government administration; (ii) to reform the social security system; and (iii) to promote private capital participation in essential services. According to this evaluation, 6 of the 11 outcomes in these areas attained medium or high results. The following table summarizes the situation before and after the programs and serves as a framework for the analysis that follows.

Table 4.5
Summary table of the results of the portfolio for reform of the State 1991-2004

Objective	Situation at start of period	Situation at end of period
Modernization of the administration	A central administration with a considerable number of employees that was a determining factor in the chronic fiscal deficit.	A central administration subjected to an initial stage of reform, later interrupted, and without having obtained the expected fiscal savings.
Reform of the social security system	A social security system with administrative problems, a financial deficit, and high fiscal cost.	A new social security model implemented, with some steps still necessary for financial sustainability and better coverage.
Participation by private capital in essential services	Public monopolies in several basic services markets, with scant incentives to improve quality or prices.	Some of these markets are open to limited competition, with great public resistance.

4.16 In short, the results in this programming area represented concrete first steps toward gradual long-term and broader reforms, but some were virtually derailed before the crisis and others were derailed on its account. Except in the case of social security, the political restrictions and constitutional prohibitions basically prevented the progress that had been made from decisively channeling long-term processes for improvements. As explained below, the discontinuity in Bank support for the reform of public companies and social security, and the loss of impetus in the second stage of modernization of the central administration, limited progress to the level of outputs, thereby restricting the impact of these improvements.

a. Administrative modernization

4.17 The process of reforming the central administration was an initial systematic effort by the country targeted to the government's core and covering approximately 30% of public employees. This portfolio began taking shape in the early 1990s but grew in 1996 when there was a sequence of two sector loans paired with reimbursable technical-cooperation programs.[76] According to the loan proposals for this portfolio, it had the objective of improving the effectiveness, quality, and efficiency of public management.[77] The following table shows the outcomes for this objective, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.6
Analysis of information on results

Outcome	Bank		OVE
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Effectiveness:			
Improvement in effectiveness and quality (UR-0090, UR-0130)	No	No	Limited
Efficiency:			
Reduction in structure, jobs, and costs (UR-0090)	Yes	Yes	Medium
Improvement in human resource management (UR-0090, UR-0130)	Yes	Yes	Limited
Improvement in fiscal management by results (UR-0090, UR-0130)	Yes	Yes	Medium
Regulatory improvement and rationalization of rates (UR-0090, UR-0130)	Yes	Yes	Limited

4.18 The analysis of outcome indicators (see background document 4) shows that the results of these programs in terms of effectiveness and quality were limited by scant political latitude and the discontinuity of the process between the first sector loan and the second. Particularly in the first stage, the conditionalities of the sector loan promoted progress in efficiency, although in light of the results, some of the conditionalities, such as those linked to helping public servants find other employment, had a considerable fiscal cost. The widespread application of the improvements envisaged during the second stage was limited, partly owing to the demands for political attention linked to management of the crisis.

4.19 Owing to the scant political latitude in which the reforms were undertaken, they did not make enough progress to decisively channel long-term processes for improvements. In particular, fundamental aspects in the initial diagnostic analyses, such as capacity for management by results, strategic planning, and human resource management, have continued to be critical factors conditioning the effectiveness and quality of public services. The results of institutional strengthening were limited by using external executing agencies and personnel in key areas for the reform, financed by technical-cooperation projects that have had limited institutionalization.

b. Reform of the social security system

4.20 As a response to the fiscal imbalance caused by social security spending, the Bank joined the reform process by preparing and approving a sector program.[78] According to the loan proposal, this program sought: (i) to implement social security reform by improving institutional efficiency and fiscal viability; and (ii) to contribute to the development of capital markets by channeling pension savings. The following table shows the outcomes for this objective, indicates whether the

Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.7
Analysis of information on results

Outcome	Bank		OVE
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Implementation:			
Joining the new system (UR-0108)	No	Yes	High
Improvement in the efficiency and quality of the services of the Social Insurance Bank (UR-0108)	Yes	No	Medium
Fiscal savings by the system (UR-0108)	Yes	No	Limited
Contribution to the development of capital markets:			
Investment in pension fund managers (UR-0108)	No	No	Medium

4.21 The analysis of outcome indicators (see background document 5) shows that the achievements of the social security reform program led to the structural transformation of the system and put it in order. The conditionalities of the reform loan led to a change in the model that laid the groundwork for a broader process of structural transformation, long-term fiscal sustainability, and broader coverage which, however, has not been supported by the Bank in more recent years. In particular, making the need for increased coverage compatible with the fiscal feasibility of the social security system continues to be the main challenge in this process, which has already been set on the path to long-term improvement.

c. Participation by private capital in essential services

4.22 The model of opening basic services that had traditionally been public monopolies to competition and private capital was supported by the Bank at the beginning of the last decade through certain conditionalities included in a sector investment loan.[79] In particular, this program proposed as its objective to increase the efficiency of the services provided by public companies, promoting participation by private capital in port services, air transport, electric power, and telecommunications services.[80] The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.8
Analysis of information on results

Outcome	Bank		OVE
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Openness to competition			
Incorporation of private capital	No	No	Medium
Improvement in efficiency as service providers	No	No	Limited

4.23 The analysis of outcome indicators (see background document 6) shows that although progress was made in some markets included in the loan, such as port services and air transport, the results of the economic reforms were limited by the lack of political feasibility revealed by the ANTEL referendum in 1992 on the program's privatization strategy. Since that time, the government adopted a model of opening the markets to competition and developing regulatory institutions, and, in practice, the Bank abandoned support for the public companies, except through financing for infrastructure loans. Although improvements have been made in the quality of services in some of the sectors (such as telephone connectivity, reduction in waiting time, etc.), their rate systems still respond to public sector revenue requirements, which has a negative impact on the competitiveness of the economy as a whole.

3. Competitive economic development

4.24 To stimulate competitiveness as part of the process of trade liberalization, the Bank developed an extensive portfolio of operations to support greater productivity and competitiveness and the development of the financial markets. The Bank's operations in this programmatic area sought: (i) to promote the development of the financial system; (ii) to boost the competitiveness of agricultural production chains; (iii) to promote scientific and technological improvements intended to raise the productivity of companies; and (iv) to support the development and rehabilitation of productive infrastructure. According to this evaluation, 14 of the 19 outcomes in these areas attained medium or high results. The following table summarizes the situation before and after the programs and serves as a framework for the analysis that follows.

Table 4.9

Summary table of the results of the competitive economic development portfolio

Objective	Situation before	Situation after
Development of the financial system	Banking market concentrated in few institutions, inefficient, with a predominance of public banks overexposed to risk. Insufficient levels of private investment, with very low levels of medium- and long-term bank credit and a nonexistent stock market. Ineffective financial rules and bank supervision to mitigate the evident vulnerability of the system.	Banking market at the end of the decade with high intermediation margins and high portfolio risks in the public banks and operational risks in the private banks. Similar levels of private investment, insufficient medium-term credit, and the incipient stock market hobbled by episodes of fraud. (Pre-crisis UR-0031) Financial rules in harmony with the Basel rules, but with selective and insufficient supervisory capacity that was unable to anticipate the fragility of the banking system prior to the 2002 crisis. (Post-crisis UR-0050) Sanctioning power of the Central Bank recognized, enforcement capacity strengthened, and prudential regulations introduced.
Development of agricultural competitiveness	Entrenched agricultural sectors exposed to competition under freer trade and the exchange rate appreciation policy.	Agro-export sectors strongly supported, achieve increases in production despite external shocks (international prices, foot-and-mouth disease) and internal conditioning factors (absence of credit).
Adoption of science and technology	Insufficient technological development applied to companies to improve their competitiveness.	Some technological applications produced, but on a small scale and with insufficient results to affect the competitiveness of sectors of the economy.
Development of physical infrastructure	Electricity, road, and port infrastructure with high capacity but little maintenance and inefficient management.	Infrastructure expanded, although not sufficiently, in the electricity and ports sectors, with some cases of management and maintenance concessions.

4.25 In short, in this programmatic area, progress was made in some specific areas, although it did not have a significant impact on mitigating the economy's vulnerability to the behavior of neighboring markets in financial or commercial areas. The series of programs to support the development of the financial sector did not lead to effective supervision with sufficient reach to mitigate the system's vulnerability, as revealed by the 2002 banking crisis, or to the development of capital markets. With regard to external competitiveness, given the magnitude of the challenge of diversifying export markets to attenuate vulnerability, the Bank's programs translated into increased competitiveness in some traditional export sectors and led to specific experiences in which products and markets were diversified, which could be taken as models for future Bank actions.

a. Development of the financial system

4.26 To stimulate development of the financial markets, the Bank approved a series of lending and technical-cooperation operations in the period 1991-2004, approximately half of whose amounts were used to promote reforms in the sector's operational framework, with the other half being used to finance multisector credit programs.[81] According to the loan proposals, the portfolio to develop Uruguay's financial sector had the following objectives:[82] (i) to improve the efficiency and competitiveness of the financial intermediation system and restructure the public banks; (ii) to promote an increase in private investment and development of the medium- and long-term credit market and the stock market; and (iii) to strengthen the regulatory framework and bank supervision to preserve the solvency and liquidity of the system's institutions. The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.10
Analysis of information on results

Outcome	Bank		OVE
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Financial intermediation system:			
Improvement in market competition and concentration (UR-0031)	No	No	Limited
Improvement in the efficiency of financial institutions (UR-0031)	No	No	Medium
Restructuring of public banks (UR-0031)	No	No	Medium
Development of private investment:			
Increase in private investment (UR-0057)	No	Yes	Limited
Expansion of the medium- and long-term credit market (UR-0063, UR-0021, UR-0136)	No	Yes	Medium
Development of the stock market (UR-0057)	No	No	Limited
Regulatory and supervisory framework:			
Application of supervisory measures and solvency and liquidity indicators to the institutions in the system (UR-0031, UR-0150)	No (UR-0031) Yes (UR-0150)	No (UR-0031) Yes (UR-0150)	Limited Medium

4.27 The 2002 banking crisis itself is clear evidence that progress in these programs was insufficient to anticipate and mitigate the consequences of the crisis on the solvency and liquidity of the financial system, as an analysis of the outcomes indicators shows (see background document 7).[83] The long-term effects of the financial crisis on the credit and capital markets ended up undoing the incipient financial market development that had taken place in the 1990s. In particular, although intermediation margins as an indicator of the system's efficiency had fallen during that decade, they remained on average at 46.9% in domestic currency, and 8.2% in U.S. dollars, which is much higher than in the Chilean (15.1% and 4.3%) or Argentine (23.5% and 9.5%) markets. Despite the pronounced exposure to risk of the portfolio of the public banks and the operational and market risks to which the private banks were exposed, the capacity of the Central Bank for supervision and control that was supported in the 1990s was limited and unable to mitigate the impact of the crisis on the banking system. Since the 2002 crisis, the IDB's support for the banking sector has produced concrete progress in strengthening bank regulation and supervision and in the implementation of prudential regulations by the financial institutions, recognition of the Central Bank's capacity to sanction, and some measures for its institutional strengthening.

b. Agricultural sector development

4.28 To support greater competitiveness in the agricultural sector in a context of substantial government support for the traditional export sectors, the Bank approved a portfolio of specific projects during 1991-2004 to support the dairy, fruit and vegetable, grape and wine, and livestock sectors, supplemented by support for animal health and agricultural services.[84] The following table shows the outcomes for this objective, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.11
Analysis of information on results

Outcome	Bank		OVE
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Productive development			
Increase in production efficiency for dairy producers (UR-0065, UR-0062)	Yes	Yes	High
Increase in dairy exports (UR-0062)	No	No	High
Increase in production value and exports in the livestock sector (UR-0072)	Yes	Yes	High
Validation of the feasibility of production innovations (UR-0137)	Yes	Yes	High
Animal health and agricultural services			
Increase in production efficiency and exports of the agricultural and agribusiness sectors through technical services (UR-0116)	No	No	Medium

4.29 The analysis of outcome indicators (see background document 8) shows that the results in this area were generally positive and helped to protect and promote production in traditional export sectors in a context of greater competition and exchange rate appreciation. In particular, production in Dairy Belt I grew by 57% between 1990 and 2000 and in Dairy Belt II it grew by 80% in the same ten years. In the livestock sector, the technological improvements promoted by the project have led to a 15% increase in exports. Recently, the adoption and validation of innovations by private livestock producers along the production chain was promoted, with results that had a demonstration effect related to reproductive efficiency, average age at slaughter, and other production coefficients. The results of these investment projects were positive individually, although given the size of the challenge of trade liberalization, they were somewhat scattered. The main challenge for the future is to support a strategy for the diversification of products and markets that helps to make the economy less vulnerable.

c. Technology development to promote competitiveness

4.30 To stimulate the competitiveness of companies faced with the challenges of liberalization, the Bank established a sequence of two lending programs, the first approved in 1991 and the second in 2000, which is still in execution.[85] According to their loan proposals, these projects had the objective of increasing efficiency in productive activities by developing national science and technology capacity. The following table shows the outcomes for this objective, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.12
Analysis of information on results

Outcome	Bank		OVE
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Technology development: Improvement in national research capacity applied to production (UR-0095, UR-0110)	No	No	Limited

4.31 The analysis of outcome indicators (see background document 9) shows that the results in this area were not large enough in scale to help strengthen Uruguay's applied science and technology capacity. The results in terms of developing national capacity for innovation have not translated into effective linkage between the business community and the national innovation system, nor has a fluid mechanism for R&D incentives been instituted as yet. Although several of the research projects financed involved agricultural applications, no documented evidence was found linking those projects to the portfolio established by the Bank with the National Agricultural Research Institute (INIA).[86]

d. Development of physical infrastructure to promote competitiveness

4.32 In response to the competitive challenges posed by economic integration, the Bank established a portfolio of infrastructure projects that had the following objectives: (i) to boost the efficiency of electricity supplies; and (ii) to reduce the costs of overland and maritime transport by improving roads and ports. The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or monitoring indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.13
Analysis of information on results

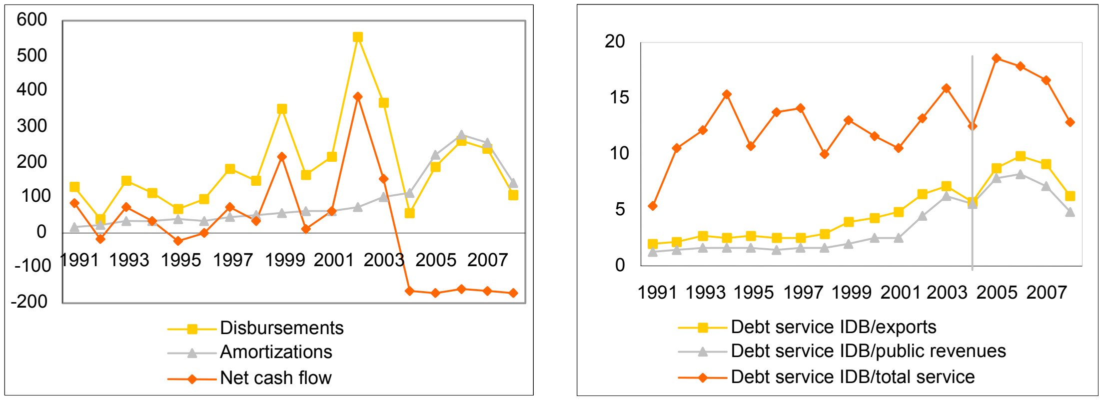
Outcome	Bank		OVE
	Initial target indicators	**Monitoring indicators**	**Attainment level**
Electricity supply: Efficiency of provision (UR-0022)	Yes	Yes	High
Commercial and tourist transport:			
Reduction in the costs of transport in integration corridors (UR-0113)	Yes	Yes	High
Improved tourist access to Punta del Este (UR-0029)	No	No	High
Improvement in wood and agricultural exports through the port of Mbopicua (UR-0142)	No	No	Medium

4.33 The analysis of outcome indicators (see background document 10) shows that the projects carried out in this area built infrastructure in the context of regional integration with a probable impact on mitigating power shortages and on the development of sectors in expansion such as tourism, agriculture, and forestry. In general, the projects have translated into improvements in efficiency and developed capacity, with a positive net present economic value. However, there are still challenges for expanding the capacity of infrastructure to serve the demands of the economy or the beneficiary sectors.

4. Financial relations and macroeconomic stability

4.34 In the process of converting the foreign debt under the Brady Plan, the Bank decided to become the country's main external creditor. This has translated into growth in disbursements in the 1990s, with a second spike in disbursements toward the end of the decade, and a third in 2002, when they rose to unprecedented heights in response to the financial crisis. The figures below show the evolution over time of a series of variables that describe the country's financial relations with the Bank between 1991 and 2004. Their trajectory is projected out into the future to analyze the deferred financial results of this portfolio.[87]

Figure 4.3



4.35 The evolution of the net cash flows reflects the buildup of financing for the country, particularly in 1999 and 2000, which can be attributed to the emergency financial package. The graphic analysis shows growth in the country's stock of debt with the Bank during this period and the relative increase in debt stock indicators compared to exports and fiscal revenues.[88]

4.36 As was to be expected, in the last six years the profile of payments from the country to the Bank became more accentuated. Debt service with the Bank in terms of exports and fiscal revenues grew steadily between 1999 and 2003. In 2004, the cash flow for the country was negative and projections for the future, based on IMF assumptions, indicate that negative net flows will continue in coming years.[89]

4.37 The buildup of the country's debt has led Uruguay's authorities to make very demanding commitments for primary surpluses in the coming years that affect the fiscal latitude necessary to return to normal levels of public spending associated with the equitable provision of public goods and progress in social spending. The priority of the social emergency plans, to make up for the negative impacts of the 2002 crisis associated with new debt, reduces immediate fiscal headroom even more in the coming years, to the detriment of projects in other areas.[90] The Bank's challenge consists of supporting the development of a program that makes attention to the country's new challenges compatible with maintaining a balanced macroeconomic position.

V. Conclusions and Recommendations

5.1 The following conclusions and lessons learned on the relationship between the Bank and the country can be drawn from the analysis of the strategy documents, the evolution of the projects, and their results for each programmatic area.

5.2 In a context of considerable changes in the country's social structure and economy, the 1991, 1997, and 2000 country papers defined a predominant role for the Bank compared to other international lending agencies, in support of some of the main priorities of the successive governments. However, the strategies did not lead to actions and policies that took a long-term view of the implications of those structural changes. In particular, the Bank's strategic contributions, based on its working experience in other countries, could have provided significant value added with respect to the adaptation of the social security model to a more polarized society, the scope of State reforms in a context of fundamental political restrictions, or the vulnerabilities associated with the move toward a more open economy.

5.3 These strategies gave rise to a large portfolio of operations marked by a relatively high fast-disbursing component, equivalent to nearly 50% of the total value. The individual operations were both designed and executed in partnership with the national authorities, who felt a sense of ownership of them. The loans generally performed well in terms of disbursements, except those affected by the 2002 crisis, and also demonstrated the country's capacity for fiduciary administration.

5.4 The programs in the area of social development and equity supported the priorities of the different governments in a setting of institutional reform and growing attention to vulnerable groups. However, their effectiveness suffered as a result of a partial reading of the implications of poverty growth and its influence on a programmatic response that divorced measures to address emerging poverty from measures to reform social welfare structures. On the one hand, the program supported reforms of the traditional social policy institutions designed for a more egalitarian society, with a limited approach to adapting them to a social structure that was gradually changing or to the rise of structural poverty. On the other, a series of programs were carried out to address the symptoms of poverty, basically interventions of a temporary nature, as if those symptoms were a transitory phenomenon, which meant that the results were also limited in scope. Today, developing a structure to provide a comprehensive response to poverty, both economically and socially, has become one of the main items on the new government's political agenda.

5.5 The programs in the field of modernization of the State linked the Bank to the main reforms undertaken by the authorities, first from the standpoint of economic reform and demonopolization of public companies and, in the second half of the 1990s, with stress on the administrative reform of the public sector. Although some of them had a considerable fiscal cost, the conditionalities of the Bank's loans were useful for spurring progress by the different ministries involved or by the legislative branch. However, the scope of the reforms that were supported was conditioned mainly by the scant political room to maneuver of minority governments and by constitutional prohibitions. As a result, except in the case of social security, such progress as was obtained—for instance the cutback in the size of the central government or the introduction of management by results—was unable to decisively channel processes for long-term improvements.

5.6 The programs in the area of economic openness and competitiveness were directed to promoting production in a series of traditional export sectors at a time when exports were being concentrated in neighboring markets, and to improving the investment climate through the development of financial markets. Although the programs to boost production were generally effective for the sectors concerned, the programs to develop capital markets and bank supervision did not anticipate the fragility of the banking system or cushion the impact of the 2002 crisis on it. Given the increased trade exposure to the Argentine and Brazilian markets up to 1998, it would have been desirable to support greater diversification of export markets toward the global economy, which would also have lessened Uruguay's economic, commercial, and financial vulnerability to the behavior of its neighbors.

5.7 Last, the Bank's contribution to macroeconomic stability and fiscal sustainability translated during the 1990s into growing amounts of financing to support the conversion of the foreign debt under the Brady Plan. Except for some difficulties in the middle of the decade, the fast-disbursing component of the loans behaved beneficially and tended to address government demands for liquidity in periods of fiscal adjustment. However, Uruguay's current high level of debt with the Bank and the repayments programmed for the next two and a half years represent a situation that is historically anomalous in relations between the Bank and the country, with repercussions for the government's fiscal headroom in the medium and long terms. This situation can largely be explained by the relative stringency of the terms and conditions of the 2002 financial emergency loan.

5.8 Based on these findings, this report proposes the following recommendations for the most effective possible partnership to address the country's main development challenges in the coming years.

5.9 **Recommendation 1**. The analysis of the country's external debt position indicates that today the Bank is a factor in its macroeconomic stability and fiscal sustainability. Keeping this in mind, the Bank should establish a schedule for flows in the coming years that helps to resolve the country's critical financial situation and is attuned to the macroeconomic balances and the need for long-term fiscal savings.

5.10 **Recommendation 2**. This evaluation notes that performance was generally better in those areas where the Bank found a niche with strategic long-term relevance, where it could concentrate its operations over time. Continuing in this direction, the Bank should establish a future program that is geared to the objectives of the national development agenda—in some cases for more than one administration's term of office—focusing its efforts on the areas where it can have the greatest impact, particularly:

a. Promoting economic growth as the main variable around which the recovery program revolves, by providing more support for improvement in the investment climate and revisiting actions to improve the efficiency of the economic services provided by public companies, among other measures; and

b. Adapting the structure of the social welfare system to the new long-term challenges related to poverty and a more unequal social structure, and improving the system's quality.

5.11 **Recommendation 3**. The processes of formulating country strategies and technical-cooperation programs have resulted in a buildup of know-how and capacity, although at discrete points in time. To continue these efforts, the Bank's programming should be backed up by a program of studies and ongoing institutional development. In particular, support should be provided for the government to identify the best opportunities for: (i) strengthening or redefining the social security model; (ii) developing management by results in the public administration; and (iii) performing cost-benefit analyses of interventions during the design stage to determine, in particular, the returns from investment, sector, or emergency loans compared to the cost of the debt.

5.12 **Recommendation 4**. Analysis of the outcome and conditionality tables of the sector programs indicates that the latter frequently served as reference points and incentives for coordination of the different stakeholders involved. In the current context of fiscal constraints, the Bank should support the establishment of a programmatic results framework that would permit:

a. The establishment of financing relations with the ministries responsible for execution, based on periodic accountability and results-based performance, from a position of partnership with the finance authorities; and

b. Maintenance of flexible financing relations with the Bank that are compatible with periods when there is a need for liquidity, associating disbursements with progress in national programs rather than specific projects, and that are a more effective way of addressing emergency situations that might arise.

5.13 **Recommendation 5**. The analysis of the program points to the country's existing capacity for efficient and flexible portfolio design and administration, based on a programmatic approach. Keeping this in mind, the financing modalities used in future should make the most of the possibilities provided by the New Lending Framework, such as: (i) discretion to use national capacity in designing programs and local administrative systems; (ii) combination of sector, investment, and technical-cooperation programs for a single purpose; (iii) disbursement against results rather than for payment of inputs or compliance with procedures; and (iv) a single programmatic approach of the existing portfolio to the future, including the possibility of restructuring it; and (v) local currency financing.

[1] The behavior of the election profile between the 1971 and the 2004 elections shows a complete reversal in the distribution of voter preferences. Support for the Partido Nacional party fell from 40% to 35% and for Partido Colorado to 10%, while Frente Amplio rose from 16% to more than 46%.

[2] These two factors alone meant an additional burden of more than 5% of GDP for the public treasury. The increase in liabilities that tied pensions to the salaries of public servants, under a constitutional reform, was the equivalent of 2% of GDP, while the fiscal cost of buying back the portfolio from the debt crisis at the beginning of the 1980s was 3.2% of GDP.

[3] Control over inflation was sacrificed in the first part of the administration's term to devaluation and later because it clashed with wage policy. The public debt/GDP ratio fell from 70% in 1990 to less than 40% in 1994, and would continue to fall to 35% until 1996 and remain under 40% until 1999.

[4] The decision to join MERCOSUR as a strategy for entry into the global economy was based on two arguments: that the country could not remain outside, there was no other option; and that the country could not change rapidly to conquer the world market. Once the decision was taken, the country tried to open up as quickly as possible. The reduction of tariffs in the customs union was speeded up, trying to achieve the lowest common external tariff.

[5] The results of the 1994 elections were a setback for the Partido Nacional party and an equivalent gain for Frente Amplio, with a slight improvement for Partido Colorado.

[6] The reforms were a response to projected fiscal savings. In the case of social security, the initial diagnosis was that it would be difficult to address the buildup of liabilities unless the system was reformed. An aging population and the very low asset-to-liability ratio (less than half of what it had been 25 years earlier) were simultaneous problems.

[7] Unlike in the previous administration's term, the numerous referendums did not block the initiatives, although they did determine their scope and configuration. The social security reform introduced a mixed pay-as-you-go/capitalization system and ordered it to be implemented, although it did not ease the financial burden as much as had been expected. The education reform introduced changes in the models and curricula for preschool, primary, and secondary school, accompanied by a significant increase in the budget for education. The reform of the central administration led to modifications in structure and a reduction in permanent public employment, particularly in the central civil service, as well as relevant administrative improvements, but it did not translate into a reduction in the primary fiscal spending/GDP ratio either.

[8] The process was driven by vigorous growth in the United States economy, coupled with a dollar that had strengthened against the main currencies, and an increase in the liquidity and mobility of international financial capital, which was accentuated by the proliferation of institutional investors.

[9] Historical factors—strict banking secrecy, a tradition of respect for savers, free movement of capital—and cyclical factors—liquidity of international markets, attractive returns for financial intermediation in dollars, and low exchange risk—influenced this behavior.

[10] The Central Bank's new charter was approved in 1995 and set the rules on its main powers, monetary policy and administration of reserves, and relations between the bank and the financial intermediation institutions, including the definition of the powers of the Superintendent of Financial Intermediation Institutions. In particular, the public banks continued to operate outside the supervisory orbit of the Central Bank even though their portfolio risks were recognized. Despite the large presence of offshore banks in the private banking business, the supervision criteria for those institutions were not differentiated from the criteria applied to domestic banks, and although a record was kept of the amounts involved in operations by nonresidents, no information was available on the types of assets they invested in or the currencies in which they were denominated.

[11] Dollarization in financial intermediation increased, the mismatches between currency and terms at BHU became more evident, and BROU's credit portfolio deteriorated significantly in quality on account of the assistance it provided to the agricultural sector, which was one of the hardest hit by the unfavorable change in the relative prices of regional and international trade. During 2001, total deposits in Uruguay's financial system rose by 12% and deposits denominated in U.S. dollars by nonresidents by 34%.

[12] The run on the banks led to a drop of nearly 50% in all the deposits in the system during 2002 (from US$17 billion at end-2001 to US$9.5 billion at end-2002) and the government's financial bailout of troubled banks amounted to more than US$2.3 billion (19% of GDP) in the same period.

[13] The fund for the stabilization of the banking system was created by law (Law 17523) in August 2002.

[14] The stock of credit for the private sector shrank by about US$4.5 billion in that year.

[15] Measured in current dollars, Uruguay's debt with the multilateral agencies grew by 183% between 1999 and 2003. Between 2001 and 2004, net financing from those agencies amounted to US$4.2 billion, with about 60% from the IMF, and most of it had to be repaid or refinanced in subsequent years.

[16] In 1955, Uruguay's per capita GDP in 1985 prices was US$4,285, which was 44% of the figure for the United States and higher than Austria and Italy. In 1998 it rose to US$6,058 (from US$2,704 in 1990) but it was 29% of the figure for the United States and half the level in Austria, Italy, and France, reflecting low long-term growth. Most of this performance can be attributed to the stagnation of the economy from 1955-1973, when per capita GDP declined at an annual cumulative rate of -0.2% as opposed to cumulative annual growth of 1.7% in 1974-2000. The 2002 crisis brought the level of per capita GDP to just over US$3,800 in 2003.

[17] IDB. Diagnóstico del mercado de trabajo en Uruguay [Diagnostic assessment of the labor market in Uruguay], C. Pages (2004).

[18] IDB. Pobreza, red de protección social y situación de la infancia en Uruguay [Poverty, social safety nets, and the status of children in Uruguay] (2004).

[19] The average for Uruguayans with more than 10 years of schooling is higher among emigrants than in the country. The percentage of technicians and professionals among émigrés is also higher. On the other hand, emigrant agricultural workers and laborers have fewer years of schooling than their counterparts in the country. More than half of emigrants live in Argentina, Brazil, Spain, and the United States.

[20] Flood et al. 2005.

[21] The population using the public health system grew from 34% in 1999 to 43% in 2003 and in the case of social security, the actuarial projections are worrisome due to the steady increase in the number of people who do not work. The social emergency demands unprecedented efforts to coordinate the welfare and job-creation models.

[22] See Mario Bergara et al. "Political institutions, policymaking processes and policy outcomes: The case of Uruguay" (2004).

[23] The government participates in the formulation and application of regulatory and production policies and the delivery of services. In some cases, the constitution determines the existence of many layers of agencies to apply policies, that are additional to the ministries and have their own budgets based on transfers. In other cases, the policy initiatives themselves have created their own offices, regardless of the fact that their powers belong by law to other existing offices.

[24] According to a comparative report on the capacity of public officials in the different Latin American countries, Uruguayan officials rank between average and low in most management indicators (Source: Beatriz Guinovart for the Red de Diálogo sobre Servicio Civil, 2002). The high average age of permanent

employees is determined by the fact that their contracts provide for job security and because it has been legally impossible to hire new employees since 1995.

[25] According to the designers of the reforms, the nature of the reform of the social security system responded to the need to avoid a referendum that incorporates a referendum-risk premium into the cost for affiliates. The matter of job security was not included in the labor reform of the central administration for the same reason. The referendums supported the legitimacy of the reform process, but in some cases they worsened the fiscal results, such as for social security in 1989. In other cases, they halted some major reforms, particularly those related to the privatization of public companies.

[26] Growth in domestic demand in these countries after their successive stabilization plans permitted Uruguayan exports to grow during the first half of the 1990s. The main examples of the intense influence of the policies of its neighbors were the Austral and Cruzado plans in 1986-1987, the Argentine Convertibility Plan in 1991, Brazil's Real Plan in 1994, in 1995 when Argentina and Brazil felt the tequila effect, the abandonment of the stabilization plan by Brazil in 1999 affected by the Russian and Asian crises, and the collapse of Argentine convertibility in 2001.

[27] Annex I includes an analysis of the correlation between the growth of the Uruguayan economy with the economies of Argentina and Brazil, which concludes that the correlation with Argentina has been increasing significantly and declining with Brazil between 1991 and 2003.

[28] More than 70% of its exports are directly or indirectly of agricultural origin and their competitiveness is explained by the behavior of raw materials in price and quality.

[29] The government continues to account for 25%. This growth is explained by the expansion in services for exports and value added (transportation and logistics, export processing zones, financial services, commerce, tourism and hotel chains, electronics, and communications among the most important). The large private conglomerates disappeared, except in collective transport and health care. Today, there are fewer than two dozen manufacturing companies that employ more than 400 people, while self-employment has proliferated.

[30] Between 1999, when the growth cycle of the previous decade ended, and September 2004 (when BCU published its last report), the debt of the nonfinancial public sector (NFPS) rose from US$6.3 billion to US$11.1 billion. More than 60% of this extraordinary increase is due to commitments to multilateral lending agencies. Owing to the devaluation of the peso, the numbers are even more impressive if measured in terms of gross product. The NFPS debt, which was less than one third of GDP in 1999, rose to 110% at the height of the financial crisis. Owing to the strong growth of the economy and the weakening of the dollar, the ratio is estimated to have fallen to 88.5% in 2004. Also, the stock of NFPS gross debt was nearly four times the country's total exports of goods in 2004 and triple its consolidated fiscal revenues. The NFPS debt involves the central government, the local governments, and the public companies, although these last two make only a marginal contribution to the total. The debt is even larger if the financial part of the public sector is included, specifically the Central Bank (US$2.317 billion in September 2004) and the public banks.

[31] A comparison of the levels of public sector investment in the revenue agencies (the Directorate General of Taxation, the National Customs Directorate, and the Social Insurance Bank) points to a disproportionate level of spending on the latter's operations compared to the amounts it collects.

[32] The anticipation rate is calculated as the ratio between the amount or number of projects approved compared with those programmed for each cycle. The improvisation rate is the ratio between the amount or number of projects approved but not programmed out of the total number approved. Annex 2 contains a full analysis of the anticipation and improvisation rates for the pipelines established by the programming.

[33] Although it is not included in this evaluation, the country paper currently in preparation does include an analysis of poverty as one of the medium- and long-term development challenges.

[34] The real evolution of poverty and inequity in Uruguay did not match the discontinuities in the analyses contained in the country papers (CP 1991 paragraphs 3.39 and 1.18; CP 1997 paragraph 1.21; and CP 2000, paragraph 1.14). The case of the housing sector in the programming is an analogous example with regard to the problems of providing housing for the low-income sector (CP 1991 paragraph 2.09; CP 1997 paragraphs 1.27 and 1.29; CP 2000 paragraph 2.75). The Bank programmed operations in this field in the 1991 and 2000 country papers but it only approved the program to support the irregular settlements.

[35] Program for the integration of irregular settlements, child and family program, or the civic violence program.

[36] In the health sector, the programming analysis in 1991 saw the core problem as being duplication and lack of coordination of the different subsystems and in 2000 it confirms lack of coordination among the institutions that provide services and the extreme institutional weakness of the Ministry of Public Health (CP 1991 paragraph 3.34; CP 2000 paragraph 2.72). While health sector programming did not focus primarily on organizational development, the program to reform human resources in the health sector, which was listed in 2000, was never approved (CP 2000 paragraph 2.73). In the water and sanitation sector, the institutional development needs of the State Sanitary Works Administration, which the Bank had been supporting since 1961, appeared in CP 1997 (paragraphs 5.51 and 5.52) and are the subject of a proposal for comprehensive institutional reform in CP 2000 which was never approved either (CP 1997 paragraphs 5.51 and 5.52; and CP 2000 paragraph 2.79).

[37] As a consequence, programming developed in parallel a portfolio of loans to reform social spending that were initially crosscutting, like the PRIS and FAS programs, and then with greater depth in health care and education, with strategic proposals that did not dovetail with the sector administrative reform programs. Since the central objective of reform of the State consisted of the organizational and administrative restructuring of the ministries and entities, these components were more tangential in the social programs.

[38] CP 2000 paragraph 2.52.

[39] Although the CP 1991 did not yet include State reform as a specific objective, placing all the stress on improving social policies, the Bank's positioning in the reform follows from a series of preparatory actions carried out during the first half of the 1990s, including reform of the Auditor General's Office. This strategic area gains strength in the programming, particularly starting in 1997, with the proposal for reform of the central administration and social security.

[40] In both cases, these are central segments in the framework for public sector reform, but without the part becoming the whole, or a universal reform as seems to be indicated in its original presentation in CP 1997, which introduces structural reform of the public sector as an objective.

[41] CP 1991 reflects the government's original guidelines for reform, which places tax reform and social security reform on the same strategic level (CP 1991 paragraph 1.12). The strategic approach reflected in CP 1997, which calls for a broader reform, does not make specific mention of the revenue component among the general objectives or the specific objectives of the program for reform of the State (CP 1997, paragraphs 5.6 and 5.9). CP 2000 returns explicitly to an improvement in the tax administration as a central objective (CP 2000 paragraph 2.18). As a reflection of this strategic approach, although the support for the tax administration was relevant, it was peripheral in nature, leaving tax reform and structural modernization of the tax administration pending, as they continue to be today.

[42] CP 2000 paragraph 2.28.

[43] The programming included relevant initiatives to support the agricultural sector from the standpoint of comprehensive support for producers, support for R&D in science and technology, support for upgrading the electric power and transportation infrastructure, support for entrepreneurial development from the MIF, a series of multisector credit programs, and sector programs to develop financial markets.

[44] CP 1997, paragraphs 1.13 and 1.18. In terms of timeliness, despite the fact that the CP warned four years in advance about the risks related to the Uruguayan economy's being slow to adjust to the external shock of open integration in 1995, the Bank did not approve operations in that regard until 1996 and 1997.

[45] In fact, CP 1991 made an analysis of the different sectors of the economy, identifying those that had already achieved international standards of efficiency and competitiveness (dairy, rice, citrus fruit, and some agri-businesses) and it is in those sectors where the Bank's portfolio for entrepreneurial support ended up concentrating, with an emphasis on producers that were already exporting (CP 1 paragraph 2.12; and CP 2 paragraph 3.16).

[46] Although the programming also pointed to the tertiary sector as an emerging sector with export potential under MERCOSUR (commercial services, financial services, transport and communications, and tourism services) and to manufacturing sectors with competitive potential in a process of greater openness (at that time the automotive assembly industry as per CP 2 paragraph 3.25, or the textile industry or meat packers as per CP 2 paragraph 5.12), but no specific supports were approved.

[47] The excessive risk exposure of some institutions in the banking system was known to the monetary authorities, but they were beyond the reach of the authorities' capacity to sanction.

[48] In accordance with the projections included in the annexes to CP 1991, at that time the Bank planned an increase in loans to the country from US$337 million to US$879 million by 1995, rising from 37% to 65% participation in the country's multilateral debt in that same period.

[49] The deliberate exceeding of the limits set in the weighting rules for fast-disbursing loans merited a detailed analysis of the associated risks and a justification in CP 1991, but not in the subsequent strategy papers.

[50] Financial sector loan approved in 1991.

[51] CP 1991 mentions debt-to-GDP of 46% for 1990 while debt-to-GDP in 2000 was 4x%.

[52] CP 2000 paragraph 2.99.

[53] There were seven sector loans among the fast-disbursing loans approved between 1991 and 2004, and one emergency loan.

[54] The reduction in costs in dollars on account of the devaluation in projects with inputs denominated in pesos was not considered on time and had a direct impact on the pace of portfolio disbursements, until partial cancellations were agreed on throughout the portfolio.

[55] The average number of years from project approval to disbursement rose from three in 2002 to five in 2005.

[56] The EDC shows the disbursement profile at a given moment in time for a given group of investment projects in execution and allows comparisons to be made with other groups of projects. The EDC links the percentage of current approvals that was disbursed to the percentage of time that has elapsed from the originally-stipulated execution schedule. This latter percentage can be measured at different times in the life cycle of projects (approval, signature, etc.). In this case, the EDC was calculated for Uruguay and for the Bank average using information on disbursements at 7 March 2005 for investment projects whose contracts had already been signed.

[57] The mechanisms imposed by the comptroller to control uncommitted expenditures is a duplicate control that, while assuring transparency in application, tends to delay disbursements.

[58] Country Financial Accountability Assessment dated 29 June 2005, a document prepared by the World Bank and the Inter-American Development Bank.

[59] The total number of contracts under Bank loans or technical-cooperation projects administered by the UNDP exceeded 3,800 in the period 1991-2004.

[60] Given that the Bank's systems only contain information since 1998 and that some of the supervisory tools have only been used since mid-1997 (PPMR), the following analysis is limited to the period 1998-2004.

[61] Explanation of the other indicators: 'Problem' projects rank low in their PPMRs in development objectives (DO) (low probability or improbability that the DO will be met).

[62] The projects with the greatest implementation difficulties are the urban recovery program (UR-0112), the agricultural services program (UR-0116), the informal settlements integration program (UR-0123), the program to strengthen the judicial system (UR-0122), the technology development program (UR-0110) and, more recently, the program for at-risk children, adolescents, and families (UR-0134).

[63] The 19 types of problems that appear as options in the PPMRs for explaining low IP and DO classifications were grouped into three broad categories: (i) problems with lack of commitment to the projects (commitment by the executing agency/borrower, lack of counterpart funds, political opposition, and changes in policy); (ii) problems with insufficient institutional capacity (institutional capacity of the executing agency, consultant performance, coordination between agencies, contractor performance, procurement difficulties, cost overruns, external audits with qualifications, changes in policy by the executing agency, and lack of an evaluation system); and (iii) problems related to the Bank (project/component design, delays in compliance with the contractual conditions, Bank efficiency (delays), environmental aspects, and changes in Bank policy).

[64] The PPMRs do not include a generic problem with fiscal constraints which, as in Uruguay's case, affects both costs charged to the debt and costs paid with country resources. Taking this into consideration, the frequency in the PPMRs was 11% (counterpart) and 8.3% (capacity of the executing agency). Frequency is calculated as the number of times that the problem appeared, taking all the periods analyzed by the PPMRs for the sample since this monitoring system was implemented.

[65] For a sample of 13 projects distributed uniformly in all sectors, it was examined whether they had detected these problems as possible risks in the loan proposals and if they ended up becoming problems. A high anticipation rate of the occurrence of a risk can be the product of high prediction capacity or of low risk mitigation capacity. In this same sample, the probability that the problem would appear in the first period, for those detected and mitigated, was 88.8% and 83.3% respectively.

[66] The CMI reflects the aggregate behavior of six monitoring instruments: administration missions, technical inspection visits, financial inspection visits, PPMRs, audited financial statements (AFS), and annual portfolio review missions.

[67] The document titled "Análisis de las estrategias de país del Banco [Analysis of Bank country strategies]," prepared by OVE in 2005, contains a detailed analysis of the capacity of these documents to define agreements with the borrowing member countries in terms of outcomes that can be used as tools for decisions on planning, management, and evaluation of results.

[68] Annex 4 presents the table of indicators in the 2000 country paper.

[69] The study of the evaluability of investment operations is based on a simple binomial analysis. If the elements for evaluability are present, they are computed as 1, and if not, they are computed as 0. The compound indicator for project evaluability is the arithmetic mean of the above and varies between value 0 (minimum evaluability) and value 1 (maximum evaluability). The analysis of the evaluability of policy reform operations was limited to their outcomes.

[70] The following criteria were used to determine the attainment levels of the outcomes (effects) of the projects: (i) high: when the problems addressed were significantly reduced, or the data supported progress equivalent to 80%; (ii) medium: when the problems addressed were partly reduced, or the data supported progress equivalent to 50%; and (iii) limited: when the problems persist or have grown, or the data indicate that progress has been less than 30%.

[71] In close association with the authorities that promoted general reform of the Uruguayan education system, the Bank's programs first proposed to promote secondary technical education (UR-0018 Technical education strengthening, US$28 million, 1993-2001) with the objective of matching it to labor market demand. Later, the Bank's portfolio supported these activities with two consecutive programs whose interventions extended to secondary education as a whole (UR-0107 Modernization of secondary education, US$40 million, 1996-2003, and UR-0321 Secondary education modernization and teacher training program, US$75 million, 2001-2006). Pursuant to a decision by the Uruguayan government in the early 1990s, the World Bank's portfolio was used to support primary education.

[72] Loans 799-OC-UR, 922/OC-UR, 1361/OC-UR, 811/OC-UR, 656/OC-UR, and 1417/OC-UR.

[73] UR-0133 Health sector reform program, US$75 million, 2001-2003 (sector loan).

[74] UR-0024 Social investment program (PRIS), US$36 million, 1991-1997; UR-0087 Program to strengthen social areas (FAS), US$27.1 million, 1994-2001; UR-0134 Comprehensive program for at-risk children, adolescents, and families, US$40 million, 2003-2007; UR-0123 Program for the integration of irregular settlements, US$77 million, 1999-2006; UR-0118 Program for citizen safety: crime and violence prevention, US$17.5 million, 1998-2004; and UR-0151 Social protection and sustainability, emergency program, US$500 million, 2002-2003.

[75] From 1991 to 2004, the portfolio of projects with influence on some aspect of reform was composed of a MIF program to support reform of the central administration, some of the conditionalities of the sector investment loan (UR-0057), and components to improve management of the PRIS (UR-0024) and FAS (UR-0087) programs. In 1996 and 1997, two large sector programs were approved, one for social security reform (UR-0108) for US$150 million, and one for reform of the central administration (UR-0090) for US$105 million. The public administration modernization program (UR-0130) and the program to strengthen the judicial system (UR-0112) were approved in 2001, and the municipality of Montevideo modernization program (UR-0139) was approved in 2002.

[76] Executed earlier were the PRIS and FAS programs, which form part of the social spending portfolio, a project to modernize the Tribunal de Cuentas [Auditor General's Office], particularly the International Loan Audits Department, which is responsible for the good overall quality of the portfolio audits, and a MIF project which in addition to paving the way for the reform, supported startup of the program to modernize the central administration, in conjunction with the other operations.

[77] UR-0090, UR-0130, and UR-0102.

[78] Social security reform program (UR-0108), US$150 million, 1996-1999.

[79] UR-0057, US$68.8 million, 1992. From a strategic standpoint, having the Bank's investment programs executed by public companies does not appear to be consistent with the objective of opening them up to competition.

[80] Under Law 16211 (called the Public Corporations Act), the Port Services Reform Act of 1992, and the corresponding regulatory regimes.

[81] The following operations make up the portfolio related to financial sector development: financial sector adjustment program (US-0031), investment sector program (UR-0057), global multisector credit programs (UR-0063, UR-0021, UR-0136), and the sector program to strengthen the banking system (UR-0150).

[82] Loan-1784, paragraph 1.13; loan-1877, paragraph 2.1; loan-1876, paragraph 3.1.

[83] In fact, the solvency and liquidity of the financial system during the 1990s depended on two supports that lay outside the reform: (i) the existence of a favorable regional and international context that assured access to external financing at low cost; and (ii) sovereign guarantees of deposits in the public banks. When the

economic agents began to realize that there was no assurance that these two conditions would be maintained, the system entered into the most serious crisis in its history.

[84] Dairy belt development programs I (UR-0065) and II (UR-0062), farm reconversion and development program (UR-0072), agricultural services program (UR-0116).

[85] Science and technology program (UR-0095) and technology development program (UR-0110).

[86] These programs sometimes competed with each other. The project's supports were more favorable than those offered in the agricultural services program, which used a method of allocating funds on the basis of competitions.

[87] Sources: Data from the IDB (OPS/FIN), the IMF, the World Bank, and the Central Bank of Uruguay.

[88] For example, in 2002 and 2003, the debt stock with the Bank was more than three quarters of the country's total exports and more than half of its fiscal revenues.

[89] A significant portion of the debt with the Bank is explained by the terms and conditions of the emergency loan financed in 2002.

[90] The scant fiscal breathing space makes it unlikely that levels of investment spending can be increased, particularly spending financed by loans already taken for that purpose by the country. This holds true for more than two thirds of the Bank's current portfolio. The preference for a portfolio that is more consistent with liquidity problems that requires compliance with demanding due dates by the Uruguayan authorities could alter the priorities of the portfolio and require that part of it be reformulated.

Background Document 1: Analysis of Outcome Indicators
Education

2.1 During the period 1991-2004, the Bank financed a series of investment projects intended specifically to support the National Public Education Administration (ANEP), focusing mainly on secondary education.[1] According to the respective loan documents, support for education reform had the following two objectives: (i) to improve the quality, efficiency, and equity of technical and secondary education; and (ii) to support reform of sector institutions, management, and the regulatory framework.[2] The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of the Office of Evaluation and Oversight's (OVE) evaluation of each of them.

Table 1.1: Analysis of Outcome Information

Outcomes	Bank		OVE
	Initial target indicator	Monitoring indicator	Attainment level
Secondary education:			
Improvement in quality (UR-0107, UR-0132)	Yes	Yes	Medium
Improvement in equity (UR-0107)	No	No	Limited
Improvement in efficiency (UR-0107)	Yes	No	Medium
Technical education:			
Adaptation to labor market requirements (UR-0018)	No	Yes	Medium
Education administration			
Institutional and management improvement (UR-0107)	No	No	Limited
Regulatory reform (UR-0107)	No	No	Limited

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Quality of Secondary Education. After the programs, Uruguay maintained a high level of quality compared to Latin America, according to the first national PISA report [Programme for International Student Assessment] prepared in 2003, although there is no prior similar comparator showing conclusive improvement in the quality of education. Some substitute indicators such as the repeater rate, which decreased from 30.8% in 1996 to 25.3% in 2002, or the dropout rate, which decreased from 16% to 12.9%, illustrate certain progress, although the latter rate is still relatively high compared to the rate in

1 In close association with the authorities that promoted general reform of the Uruguayan education system, the Bank's programs initially sought to promote secondary technical education (UR-0018 strengthening of technical education, US$28 million, 1993-2001) with the objective of adapting it to labor market demands. Later, the Bank's portfolio supported these activities with two consecutive programs whose interventions extended to secondary education as a whole (UR-0107 modernization of secondary education, US$40 million, 1996-2003, and UR-0132 secondary education modernization and teacher training program, US$75 million, 2001-2006). Pursuant to a decision by the Uruguayan government in the early 1990s, the World Bank's portfolio was used to support primary education.

2 Loans 799-OC-UR, 922/OC-UR, 1361/OC-UR, 811/OC-UR, 656/OC-UR, and 1417/OC-UR.

countries at an equivalent stage of development.[3] Consequently, only one out of three students who enter secondary school complete their education, and only two out of three complete the short cycle.[4] The following table shows the main trends recorded in terms of secondary education outcomes before and after the programs.

Table 1.2: Secondary Education Outcomes

Indicator	Before	After
Repeater rates[1]	1996: 1st grade: 30.8% 5th year: 22.6%	2002: 1st grade: 25.3% 5th year: 31.6%
Dropout rates[1]	1996: Total 1st grade: 16% Total 5th year: 30.3%	2002: Total 1st grade: 12.9% Total 5th year: 19.6%
Graduation rate	Not available	2000: 33.5 % for complete secondary 2003: 60% for basic secondary
Student assessment exams	Not available	1999: 56% and 68% of students with average-high or high performance in mathematics and language arts, respectively.[2]
Enrollment benchmarks Secondary school enrollment Technical school enrollment	 1994: 184,083 1994: 61,521	 2002: 224,559 2003: 68,779

[1] Only for day schools.
[2] National Education Census, 1999, 3rd years of basic cycle.
Source: Internal document based on data provided by MEMFOD [Modernization of Secondary Education and Teacher Training].

Equity of secondary education. In terms of distribution equity, the program outcomes show substantial differences by quintiles beginning quite some time before the crisis, which were exacerbated by the significant increase in poverty in recent years. Indicators of inequity in access show an increase from 2.1% in the 1991-1992 period to 2.6% in 1996-1997, and 3.4% in 2000-2001.[5] Official data also reflect a change for the worse prior to the crisis in the number of youths between the ages of 12 and 17, corresponding to the first quintile, who neither go to school nor work (from 15.8% in 1991 to 18.6% in 1999). This indicator improves for the highest income quintile (from 3.6% to 3.1%).[6] These trends do not suggest that there was an improvement in equity in admittance to, or completion of, secondary education in the years following the crisis. In 2001, whereas the repeater rate in the first year of public secondary education was 8.4% for schools in a highly favorable socioeconomic setting, the rate was 25.1% for schools in a highly unfavorable setting.

Technical education and adaptation to labor market. Given the labor market's still limited recognition of technical school graduates, there are no data confirming whether the program has produced the expected effects on the quality of the nation's human capital. Although the impact of the extended recession on the labor market starting in 2000 is not to be taken into consideration in the analysis, the outcomes in terms of reducing the unemployment rate of technical school graduates were initially poor between the 1998 and 2002, albeit not as poor as the rate for secondary school graduates. Changes in the monthly

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3 Dropout rates among youths aged 15 to 19 for the years 1990 and 2002, respectively, are as follows: 37% and 30% for Uruguay, 23% and 17% for Argentina, 21% and 14% for Chile, 40% and 21% for Brazil, and 30% and 24% for Colombia.

4 An analysis by cohorts shows that positive outcomes were achieved in terms of attracting youths to complete basic secondary education, but that it was difficult to keep them in the system to start the upper secondary cycle. For the 1986-1988 cohort (19-21 years), 16.2% completed the basic secondary cycle but did not begin the upper cycle, whereas the rate was 12% (12-15 years) for the 1992-1995 cohort.

5 Source: UNICEF-Uruguay 2003.

6 Source: Continuous Household Survey, 1991 and 1999.

pay of graduates of the new technical education program reflected limited recognition by employers, particularly for graduates with a technical school diploma.[7]

Table 1.3: Outcomes for Technical Education

Outcome Indicator	1998	2002
Unemployment Rate		
Unemployment rate of recent technical education graduates (CETP)	14.1%	20.8%
Unemployment rate of recent graduates with technical school diploma (BT)	15.0%	17.3%
Comparator 1: Unemployment rate of recent secondary graduates	9.4% (2000)	28.0%
Earnings		
Monthly earnings of recent CETP graduates (current Uruguayan pesos)	4,880	4,905
Monthly earnings of recent graduates with BT (current Uruguayan pesos)	7,420	5,081

Source: Follow-up survey of Technical Education Graduates and Continuous Household Survey.

Institutional development and education administration. Some of the most obvious constraints to institutional development and improvements in the management of the National Education Administration (ANEP), such as the multitude of agencies involved, centralized decision-making or the existence of a single registry, were still there after the Bank programs.[8] As with other State reform programs, the strategy of reforming institutions from the outside as a response to internal institutional constraints and restrictions probably allowed faster progress to be made, but limited the scope of the improvements and buy-in of changes. The development of new institutions such as regional teacher centers projected recurring fiscal costs which did not seem to conform to considerations of fiscal sustainability. A comparison of indicators before and after the programs reveals no change in some key organizational and operational areas.

Table 1.4: Management Outcomes

Management indicators	Before	After
Simplification of excessively vertical and multiple structure	Basic structure: Ministry of Education and Culture, ANEP, CODICEN, decentralized councils and Basic and Advanced Teacher Training Administration	Offices added and other offices restructured Additional structures appear: MECAEP (World Bank), MESyFOD, MEMFOD (IDB)
Decentralization of decision-making	Centralized within ANEP	Decentralized councils or educational centers still do not have delegated authority
Development of information systems to manage resources and assign teacher hours	No single registry of teachers, salaries and hour assignments	There is still no database containing all ANEP officials or students
Elimination of regulations restricting the expansion of education opportunities	Obstacles to the approval of private programs and entrance exam requirements	Continued regulatory obstacles to liberalization of the sector at all levels

Source: Internal document based on data from Caraballo et al, MEMFOD and ANEP.

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7 Source: 1998 Survey of Recent Graduates and Continuous Household Survey. This survey began in 1998 and no baseline indicator for the project is available.

8 Institutions in the education system are centralized within ANEP (National Public Education Administration), as an autonomous entity, a top government body called CODICEN [Central Executive Board of Public Education] and decentralized councils.

Background Document 2: Analysis of outcome indicators
Reform of the healthcare system

The Bank financed a program to reform the health sector in response to financial problems and the need to reform the existing healthcare model.[9] According to the project report, the program had the following two objectives: (i) to improve the efficiency, equity, and quality of healthcare services for citizens; and (ii) to support strengthening of the private and public subsystems and the regulatory framework for the sector. The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 2.1: Analysis of Outcome Information

Outcomes	Bank		OVE
	Initial target indicator	Monitoring indicator	Attainment level
Healthcare services:			
Quality of care and improvement in health indicators (UR-0133)	No	No	Medium
Equity in care (UR-0133)	No	Yes	Limited
Heath care administration and institutional development:			
Institutional and management improvement (UR-0133)	No	No	Limited
Improvement in the financial situation of the mutual subsystem	No	No	Medium
Regulatory reform (UR-0133)	Yes	Yes	Medium

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Quality of services and improvements in health. Although progress was made in the course of the program in terms of processing information on users through the mutual subsystem registry, it did not produce indicators on the utilization and quality of healthcare.[10] In terms of the healthcare services provided, good progress was made in the area of highly sophisticated medicine, but, given the lack of data, it is difficult to evaluate indicators on the quality of primary care. Some health outcome indicators improved, such as infant mortality which fell from 14.6 per thousand in 2000 to 13.5 per thousand in 2002, increasing to 15.0 per thousand in 2003, but it is difficult to attribute these results to the loan activities.[11]

Equity in healthcare services. The significant increase in the number of people dependent on the public healthcare system, which according to official data rose from 34% to 43% of the population between 1999 and 2003, did not lead to improved equity in the quality of services provided to different population groups, pointing up a healthcare system increasingly differentiated by socioeconomic levels. This trend, in line with an average 7% annual decrease in the budgets allocated to this area, also suggests a deterioration in the quality of the public healthcare system that serves lower income

9 UR-0133 health sector reform program, US$75 million, 2001-2003 (sector loan).

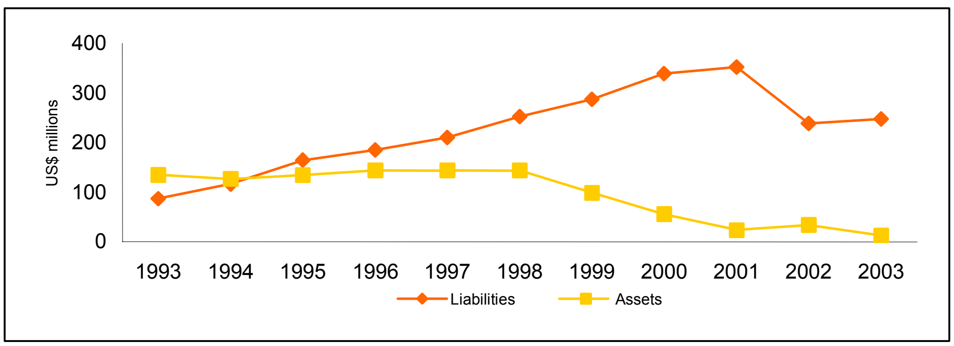
10 The RUCAF database [Master Registry of Formal Health Assistance Coverage] was introduced in 2000 to track individuals covered by the private subsystem. In 2002 the manual records were computerized. Today, the State Health Services Administration (ASSE) has a computerized registry of users, but does not yet have information on the types and quality of healthcare.

11 Source: National Statistics Institute (INE), Human Development Report (UNDP).

populations and the mutual system.[12] The difference in pay structures between the public healthcare system and the mutual system does not encourage the best specialists to care for the neediest population.[13] To illustrate, 90% of the public subsector's recipient group currently corresponds to the poorest quintile of the total population in terms of income.[14] The Bank's financial support of the mutual subsystem was not in line with its equity objective, particularly during the period when the number of people without coverage who depended on public healthcare was growing.

Health administration and institutional development. Financial support of the mutual system sought to eliminate the accrued liabilities of the Montevideo mutual healthcare institutions (IAMCs), which had liabilities that far exceeded their net assets.[15] However, short-term funding did not succeed in resolving the problem and those institutions continue to have negative consolidated financial statements, a problem made worse by the financial crisis. As a result, these institutions currently have few prospects for improving their finances in the short run. The following graph shows the historical performance of the imbalance between the assets and liabilities of the Montevideo IAMCs, which despite an improvement starting in 2001 and continuing in 2002 with the Bank's assistance, maintained a significant gap that widened throughout 2003.

Graph 2.1: Asset-Liability Performance (Montevideo IAMCs)[16]



[12] Spending by the system of ASSE executing agencies indicates that, in constant pesos, there have been significant decreases since 2001 (7% average annual decrease). This implies a 22% drop in healthcare spending per capita. The same trend is seen in the indicator on personnel spending in relation to the number of medical visits.

[13] In 1990 there was a total of 9,093 active doctors, and 12,388 in 2002 (a cumulative growth rate of 36.24% between 1990 and 2002, and 271 inhabitants per doctor in 2002). The country had an oversupply of doctors working in public health with very low salaries, and an elite of professionals in highly sophisticated medicine and technology who charged per event. The segmentation of these two professional markets tends to affect the quality of professional services.

[14] These data have only been available since the ASSE databases were computerized (2002), so there is no historical data.

[15] Around 2001, the mutual healthcare institutions (IAMCs) had accrued liabilities of US$350 million, and the National Resource Fund (FNR), the agency that finances high-cost, highly sophisticated services in Uruguay, had an operating deficit and accrued liabilities of US$70 million in 2000. This led to a financial crisis among the mutual companies that pushed several into bankruptcy, as well as mergers and takeovers and a decline in the quality of healthcare offered.

[16] Source: Ministry of Public Health.

Making funding contingent on plans to improve the management of mutual companies resulted in insufficient means to structurally adapt or sustain the number of affiliated companies during periods of recession and unemployment. The Ministry of Public Health was also restructured, although there are still opportunities to improve its policy coordination capacities, particularly with respect to the various healthcare service providers.[17] The loan's activities to enhance the regulatory area have led to a unified body of laws and a health institution regulatory agency that is not, however, very effective in practice.

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[17] Surveys of the users of healthcare services say they believe that there is insufficient oversight of institutions and more changes are needed, but they are satisfied with the quality of care received and the improvement in regulatory activities.

Background Document 3: Analysis of outcome indicators
Streamlining and organization of social spending

Beginning early in the last decade, the Bank carried out a series of projects to target social assistance to the most disadvantaged groups in general. Under the impact of the crisis, projects were added to target more specific groups, such as people living in fringe urban areas and at-risk children and their families.[18] According to the loan proposals, these operations had the following objectives: (i) to organize and streamline social spending for better targeting of vulnerable groups; (ii) to improve the living conditions of vulnerable groups; (iii) to protect social spending programs during the 2002 financial crisis, to prevent it from impacting the poorest sectors; and (iv) to support the development of social infrastructure. The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 3.1: Analysis of Outcome Information

Outcomes	Bank		OVE
	Initial target indicator	Monitoring indicator	Attainment level
Organization and targeting of social spending:			
Better targeting of social spending (UR-0024, UR-0087, UR-0134, UR-0123)	No	No	Limited
Living conditions of vulnerable groups:			
Improvement in the quality of life of the neediest groups (UR-0024)	No	Yes	Limited
Improvement in living conditions of at-risk children and families (UR-0134)	No	No	Limited
Improvement in the quality of life in squatter settlements (UR-0123)	No	No	Limited
Protection of social spending and social impact during the crisis:			
Protection of social spending during the 2002 crisis (UR-0151)	Yes	Yes	High
Impact of the crisis on the poorest groups (UR-0151)	No	No	Limited
Provision of social infrastructure:			
Improvement in living conditions	No	No	Medium

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Organization of social spending. The series of projects to organize social spending did not succeed in developing installed capacity to coordinate the social spending needed to optimize the quality of assistance provided to the most vulnerable groups, and this need is being reconsidered by the new administration. The evaluation did not find data indicating that these programs helped to coordinate or retarget individual ministry spending on the neediest population or on the specific groups targeted by such programs. In the 1990s, the methods used to implement components or subcomponents and the creation of parallel structures in both the program to strengthen social areas (FAS) and the social investment program (PRIS) were not conducive to an orderly institutional, management, and administrative structure or to the institutionalization of efforts. Since 2000, the program

[18] UR-0024 social investment program (PRIS), US$36 million, 1991-1997; UR-0087 program to strengthen social areas (FAS), US$27.1 million, 1994-2001; UR-0134 comprehensive program for at-risk children, adolescents, and families, US$40 million, 2003-2007; UR-0123 program for the integration of squatter settlements, US$77 million, 1999-2006; UR-0118 program for citizen safety: crime and violence prevention, US$17.5 million, 1998-2004; and UR-0151 emergency program, US$500 million, 2002-2003.

for the integration of squatter settlements (PIAI) and the comprehensive program for at-risk children, adolescents, and families, which are still being executed, have not yet shown progress in targeting and coordinating policies as originally planned.

Impact on improvement of the living conditions of vulnerable groups. Because of insufficient criteria to target resource allocation, these programs do not have the data to validate their effectiveness in terms of improving the living conditions of the beneficiary groups. The PRIS and FAS programs resulted in the construction of infrastructure, but the Bank's monitoring tools do not include objective indicators of well-being and quality of life for these groups.[19] Only the PRIS identifies the percentage of its users whose basic needs were unmet (55%).[20] Due to the impact of the crisis in particular, the squatter settlement program did not meet its target of reducing the annual growth rate of such settlements, which has remained at approximately 10% per year, nor did it provide information on improvement in the living conditions of the target population. The program for citizen safety supported innovative crime prevention methods in areas of social risk, and resulted in the construction of rehabilitation infrastructure with capacity to house 1.4% of the country's prison population.

Maintenance of social spending during the 2002 crisis. A conditionality of the 2002 financial emergency loan was the budget protection of nonwage expenditure levels for a number of priority social programs in existence during the crisis, in the areas of education, healthcare and social security.[21] Given the loan's ambitious objective, which was to prevent the crisis from adversely affecting poverty, its outcomes were limited. Nonetheless, the program was able to shelter the budget of a select number of programs, primarily by maintaining large-scale social security spending.[22] It guaranteed transfers to the pension fund management companies (AFAPs), thereby protecting retirement contributions during the financial crisis. Yet given the loan's objective, the initial selection of programs nevertheless revealed a preference for traditional programs as opposed to others intended to head off poverty growth and strengthen the system of social safety nets. Due to the medium-term fiscal impact of the crisis, social spending as a whole fell 13% from 1999 onward, which as a practical matter reduced spending per beneficiary, particularly in the areas of healthcare and primary education.[23]

Provision of social infrastructure. During the period 1991-2004, the Bank continued to provide ongoing support in the area of infrastructure and sanitation, in order to improve

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19 Schools, neighborhood centers, community kitchens, housing, etc. were built. The Project Completion Reports (PCRs) claim that admittance to preschools increased, infant mortality improved through prevention and promotion activities, 6,820 workers were trained between 1995 and 1999 (FAS), investments were made in infrastructure and there was better access to education and healthcare. Improvements in quality of life and well-being attributable to the programs could not be objectively verified. The comprehensive program for at-risk children, adolescents, and families started to be implemented at the end of 2004 and there is still no information on progress and outcomes.

20 According to the PCR for the PRIS program on education, 54% of the beneficiaries' basic needs were unmet, with 33.4% in the area of health and 50% in other areas.

21 Loan proposal UR-0151.

22 In fact, the PCR indicates that some specific goals were not achieved in the execution of certain specific priority social programs such as the campaign to prevent dengue fever (budget performance 35.1% in 2002) program to modernize the health sector (budget performance 48.7% in 2002).

23 Source: Ferreira, Coimbra and Forteza, 2004.

basic service coverage and the living conditions of the population.[24] In the area of water and sanitation, there was a 16% increase in water supply coverage throughout the country and a 10% increase in sanitary sewerage. Municipal development programs helped expand coverage of basic services, particularly urban drainage. In terms of the Bank's sustained support over several decades, 90% of Uruguay's people now have urban sanitation, and the water quality in Río de La Plata has improved significantly. Lastly, the urban renewal project in the area between downtown Montevideo and the port resulted in the cancellation of 57% of the loan proceeds, due to problems with the participation of the various stakeholders.[25]

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[24] UR-0092, national water and sanitation program, US$44.47 million, 1993-2003; UR-0036, housing sector support program, US$42.67 million, 1992-2001; UR-0023, Montevideo urban sanitation program II, US$24,525, 1992-1996; UR-0111, municipal development program II, US$24,821 million, 1990-1998; UR-0089, Montevideo and metropolitan area sanitation program, US$153.3 million, 1996-2005; UR-0112, urban renewal program, US$28 million, 1998-2005; UR-0118, citizen safety: prevention of violence and crime, US$17.5 million, 1998-2004.

[25] From the beginning, there were significant delays in the execution of the program. The economic crisis seriously affected the dynamics of the real estate sector, the needed response from the private sector and the possibility of completing the projects that had been started. In addition, the Sociedad Anónima de Desarrollos Urbanísticos [Urban Development Corporation] was unable to obtain cooperation and coordination among the various public agencies involved.

Background Document 4: Analysis of outcome indicators
Modernization of the Central Administration

The process of reforming the Central Administration was an initial systematic effort by the country targeting the government's core and covering approximately 30% of public employees. This portfolio began taking shape in the early 1990s, but grew from 1996 onward, when there was a series of two sector loans paired with reimbursable technical-cooperation programs.[26] According to the loan documents, this portfolio had the objective of improving the effectiveness, quality, and efficiency of public administration.[27] The following table shows the outcomes for this objective, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 4.1: Analysis of Outcome Information

Outcomes	Bank		OVE
	Initial target indicator	**Monitoring indicator**	**Attainment level**
Effectiveness:			
Improvement in effectiveness and quality (UR-0090, UR-0130)	No	No	Limited
Efficiency:			
Reduction in structure, jobs, and costs (UR-0090)	Yes	Yes	Medium
Improvement in human resource management (UR-0090, UR-0130)	Yes	No	Limited
Improvement in results-based fiscal performance (UR-0090, UR-0130)	Yes	Yes	Medium
Regulatory improvement and streamlining of rates (UR-0090, UR-0130)	Yes	Yes	Limited

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Improvement in effectiveness and quality. The implementation of a results-based management model as proposed in the first sector loan led to only partial progress, so the reform process was not carried out based on considerations of effectiveness. As a result, while this program did introduce certain performance reporting routines and indicators for individual activity centers, these were barely used to make management decisions, evaluate policies or generate information on the effectiveness of the reform. In addition to the performance-based management capacity, factors such as strategic planning capacity and human resources management continued to place critical constraints on the effectiveness and quality of public services.[28]

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[26] Executed in previous years were the PRIS and FAS programs, which are part of the social spending portfolio, a project to modify the Tribunal de Cuentas [Auditor General's Office], particularly the International Loan Audit Department, which is responsible for the good overall quality of portfolio audits, and a multilateral investment fund project which, in addition to paving the way for the reform, supported the startup of the program to modernize the central administration.

[27] UR-0090, UR-0130, and UR-0102.

[28] Michele Santo, "Uruguay: Principal Restrictions to Sustainable Growth." Document commissioned by RE1-IADB (2005); The Contaduría General de la Nación [Office of the Comptroller General] is under the authority of the Ministry of Economic Affairs and Finance and is responsible for budgeting the current spending of the Central Administration; and Schick, Allen "State Modernization in Uruguay." Document commissioned by RE1-IADB (revised version, June 2004).

Reduction in structure and costs. The activity and administrative restructuring initiatives led to a 37% decrease in the number of basic activity units, and a 46% decrease in first- and second-tier organizational units.[29] In conjunction with the process of eliminating or merging organizational units, approximately 50 government activities were transferred to for-profit private companies or third-sector companies. However, the reorganization process in and of itself, which occurred at the request of various ministries, was not initially designed to ensure the elimination of overlapping functions or the selection of essential functions based on considerations of subsidiarity.[30] The restructuring activities were considered satisfactorily completed at the end of the first sector loan and not included in the design of the second loan, which proposed a series of administrative improvement agreements at the specific level of the executing agencies with limited application.

Central administration staff cuts had a net effect that was less than reported by the Bank at project end, if one also counts non-civil-service hires, including staff with public functions hired in executing agencies funded by multilateral organizations.[31] Voluntary retirement and outplacement plans were implemented as part of the staff reduction process. In addition to the considerable cost, these did not necessarily minimize adverse selection with the resulting potential loss of human capital.[32]

From the perspective of changes in long-term fiscal spending, the reform of the central administration did not produce the expected results of reducing spending with respect to the GDP. In fact, according to official data in recent years, there was an initial increase in primary spending during the period 1999-2001 as well as in staff outlays.[33]

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29 According to official data, the program resulted in the restructuring of 82 executing agencies (EAs), the elimination or merger of 40 EAs, and the elimination of 46% of the first- and second-tier organizational levels. The number of surplus jobs declared was 9,221 (including 1,828 eliminated vacant positions). The number of surplus jobs declared was 16% of the total number of jobs in the participating ministries.

30 This observation that decision-making was less than optimal in the restructuring process is especially true, considering that a minority government was in office with cabinet posts distributed among the different parties. This meant that decisions had to be negotiated, even though the Budget Act set a procedural sequence for the selection of structural units that varied somewhat from section to section.

31 According to data from the National Civil Service Office (ONSC), combined with the effect of the new hiring freeze legislation of 1995, the declaration of surplus jobs sponsored by the reform resulted in a staff reduction of 7,800 civil servants between 1997 and 2000, which later increased by 2,650 between 2001 and 2004. A total of 9,000 central administration employees were not public servants during those years (grant holders, hiring of industry, term contracts). This number began to increase significantly in 2002, to reach a high of 12,200 employees at the end of 2004.

32 In order to stimulate voluntary retirement of civil servants, the program instituted a series of initiatives that encouraged outplacement, which included consulting services and business startup loans. However, there was no minimum follow-up on the repayment of these loans and survival rates, which would be necessary to evaluate the program's impact. The design of the voluntary retirement plan and variability in the enforcement of rules from one ministry to another did not ensure a staff reduction process that would minimize adverse selection.

33 The increase in the central administration's outlays in terms of the GDP in the last few years was due primarily to the significant increase in financing the social security deficit, and more recently, the explosion in the burden of debt servicing. In terms of the product, central administration staff spending increased from 4.7% of the GDP in 1996-1998 to an average of 5.5% in the period 1999-2001.

Table 4.2

	Central Administration Spending (% of GDP)			
	Average 1991-1994	Average 1996-1998	Average 1999-2001	Average 2002-2003
Total spending	16.5%	20.5%	23.5%	26.4%
Primary spending	14.6%	18.9%	21.0%	20.2%
Interest and fees	1.8%	1.6%	2.5%	7.1%
Wages and salaries	4.7%	4.7%	5.5%	5.4%

Source: Indicators prepared by OVE based on data provided by the Office of the Comptroller General.

Improvement in human resource management. The programs did not address structural constraints such as the modification of the rule on the tenure rights of civil servants or overhauling the ONSC's corporation-like practices, probably for political reasons. Following certain changes for demonstration purposes, such as the creation of 67 upper management jobs filled by competitive processes with revocable contracts, reforms in human resource management were cut short and now constitute one of the main medium-term challenges to improving the functioning of the administration.[34] Throughout those years, the pay structure continued to be characterized by a very flat wage pyramid and a wide range of different wages that caused significant differences in the remuneration of the same jobs, which were out of synch with the marketplace. Although certain isolated initiatives were carried out to streamline working conditions, they had little impact.[35] The Bank's first loan was based on pragmatic logic that avoided any reform of the ONSC and duplicated some of its functions in the project's implementing agency. The second program also included a conditionality in this area, but it was later waived.[36]

Improvement of fiscal management. The implementation of performance-based budget management routines resulted in initial progress, although reforms are still needed to transform budget planning and management into strategic practices. The first program resulted in the introduction of a number of information systems, such as the Integrated Financial Information System (SIIF), the Public Expenditure System (SEG), and the Performance-based Management Assessment System (SEV) in the central administration, the Internal Public Management System (SIG), and some legislative reforms such as the Financial Management Act passed in 1999.[37] The second stage of the program sought to

34 Some changes were made in the career path structure, such as the creation of upper management jobs filled on an open competition basis with revocable contracts for one-third of the first-tier management positions (67 highly specialized positions were created between the years 1997 and 1999; Source: ONSC).

35 42 executing units with the Objective Employment Conditions Oversight System (SCOT) implemented at 195 executing units of the central administration (2004).

36 The technical cooperation program associated with the first sector reform of the central administration was a technical secretariat that assumed some of the constitutional duties of the ONSC. The Executive Committee on State Reform (CEPRE) is composed of the ONSC, the Planning and Budget Office (OPP), and the Ministry of Economic Affairs and Finance (MEF). Although a proposal was prepared by the OPP on the reform of the ONSC, it did not reach the political negotiation stage; the second program granted a waiver of the ONSC reform with the second tranche.

37 Introduction of the Integrated Financial Information System (SIIF), particularly the Public Expenditure System (SEG); the Financial Management Act passed in 1999; introduction of the Performance-based Management Assessment System (SEV) in the central administration; development of the Internal Public Management System (SIG) and pilot program in 5 executing units; drafting of the 2000-2004 National Budget Act with the new methodology. The compensation system was implemented in 100% of the executing units paying civilian central administration salaries, including public health.

promote widespread use of management systems, with partial and variable levels of success depending on the ministry, based on case-by-case political negotiations.[38]

Tax administration was supported by the sector programs as well as a large number of technical cooperation programs. Although there were improvements in infrastructure, personnel, equipment and systems, these programs had to contend with fundamental political restrictions and did not succeed in addressing the problems associated with a lack of financial autonomy, lack of an investment budget and organizational autonomy of the Directorate General of Taxation (DGI), as well as the problems of tax evasion, nonpayment and inequity of the tax system.[39] It is now recognized that these structural changes would have been necessary to maximize the effects of collection and ultimately the contribution of revenues to fiscal sustainability.[40] The following table shows changes in a number of critical DGI management indicators before and after these programs, which indicate too little investment in the ability to generate public revenues, as well as continued structural deficiencies.

Table 4.3: Management Results

Indicator	Before[1]	After
Public investment in the DGI Spending as a % of revenue collection	1.13% (2000)	0.69% (2004)
Revenue collection potential: VAT evasion by private sector (%) Fiscal waiver due to exemptions	19.9% (1997) >30%	36.0% (2002) exemptions not removed
Conflicts of interest Law on conflicts of interest in staff rules	DGI employees advised companies	Regulations implementing the law on conflicts of interest were instituted subsequently
Administrative and financial autonomy	Nonexistent	Included in the current reform proposal

[1] IDB, Luisa Rains (1999) and DGI data and estimates, Díaz Yubero (2003), and DGI and CINVE (Economic Research Center) 2004 data.

Regulatory improvements and rationalization of rates. The programs led to progress in the deregulation of the State's market involvement, but their impact was less than expected in terms of lifting barriers to competition. During the first sector loan, progress

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38 99% of the executing units of the Central Administration (which represented 82% of spending in 2000) implemented spending by activity center (in connection with the Public Expenditure System, SEG). SEG authorized for the entire central administration with the exception of the National State Services Administration/Ministry of Public Health (ASSE/MSP). The widespread implementation of the SCOT and management improvement measures encountered problems which could be attributed to negotiations with each section.

39 These problems were documented in several studies, some of which were commissioned by the Bank. (Mission headed by Luisa Rains (INT/FIS in April 1999); studies conducted by Díaz Yubero (2001) "Dirección General Impositiva – Diagnóstico de Situación y Principales Recomendaciones" [Directorate General of Taxation: Assessment of Situation and Principal Recommendations]; and more recently, a study by Pérez, L., G. Oddone and F. Lorenzo (2004), "Ideas y Lineamientos para la Reforma Tributaria" [Ideas and Guidelines for Tax Reform], in the section "Agenda de la Reforma de la Administración Tributaria" [Agenda on the Reform of the Tax Administration].

40 This assistance allowed a number of peripheral measures to be carried out in the National Customs Directorate (DNA) as well as the Directorate General of Taxation (DGI). Through the Bank's projects, computer infrastructure was updated and improvements were made in the master registry, the administration of large taxpayers and the addition of staff to better serve the taxpayer.

was made in the mass of regulations, and criteria were introduced to set prices and public rates based on cost recovery. However, this progress was less than expected and the conditionality stipulated in the plan was ultimately waived. During the second loan, progress was made in the creation of regulatory administration systems, but there have been no improvements to date in the regulatory area that could have considerable sector and productive impact, such as those associated with relaxing labor relations or the startup or regularization of companies.[41]

[41] According to data provided by the Planning and Budget Office (OPP) which became actively involved, no deregulations were approved between 2002-2003 (compared to 102 deregulations in 2000-2001). An institutionalized system was created to oversee and analyze the creation and modification of regulations and provide methodology for this analysis (Regulatory Impact Methodology, MIR). The reduction in the tax on foreign exchange purchases (ICOME) and the employer contributions of public companies, which was to be passed on to users in the form of lower rates, were also waived. New regulations in the health and transportation sectors were recently added.

Background Document 5: Analysis of outcome indicators Reform of the social security system

In response to the fiscal imbalance caused by social security spending, the Bank joined the reform process by preparing and approving a sector program.[42] According to the loan proposal, this program sought: (i) to implement social security reform by improving institutional efficiency and fiscal viability; and (ii) to contribute to the development of capital markets by channeling pension savings. The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 5.1: Analysis of Outcome Information

Outcome	Bank		OVE
	Initial target indicator	Monitoring indicator	Attainment level
Implementation			
Joining the new system (UR-0108)	No	Yes	High
Improvement in the efficiency and quality of the services of the Banco de Previsión Social [Social Security Bank] (UR-0108)	Yes	No	Medium
Fiscal savings by the system (UR-0108)	Yes	No	Limited
Contribution to capital market development:			
Investment in pension fund management companies (UR-0108)	No	No	Medium

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Joining the new system. With the incentive plan that was implemented, 86% of workers who had the option of joining the new system did so, through the individual savings component. However, in terms of access to social security, the requirements of the original plan and the cost of joining the system were determining factors that resulted in more than one-third of the country's working population not being covered by social security, and the system has not done well in recent years.[43] This was aggravated by the 2002 crisis, which increased evasion levels, particularly among low-paid casual workers, due to the high cost of contributions, which equaled 40% of the amount of their gross pay.[44] Since according to recent studies the lack of social security coverage is one of the main factors behind the recent rise in poverty, the level of inclusion in the system is a major challenge for the future.[45]

Improvement in efficiency and fiscal impact. Improvements in the administration and quality of service of the Banco de Previsión Social [Social Security Bank] (BPS) have not resulted in a decrease in its spending efficiency.[46] In fact, the institution's operating expenses as a percentage of total spending have risen steadily from 5.3% in 2000 to 6.6%

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42 Sector loan: social security reform program (UR-0108), US$150 million, 1996-1999.

43 Source: Banco de Previsión Social [Social Security Bank] (BPS).

44 Currently, employee and employer social security assessments represent an average of 38% of gross pay. If work-related risk coverage is included, the charge exceeds 40%.

45 IDB. Poverty, social safety net and the situation of children in Uruguay (2004).

46 Outputs of the technical support program associated with the sector include the leveraging of retiree records and employment history databases, the telephone assistance network, and the pension payment system.

in 2003.[47] To date, the fiscal impact of the reform has been less than originally expected, and social security remains a major tax burden: transfers from the central administration to the BPS rose from 1.7% of the average GDP during the years 1991-1994 to an average of 4.3% during the period 2000-2003.[48] The limited results in terms of reducing the system's deficit are due to factors such as indexing contributions to actual rising wages, exempting employer and health insurance contributions to the BPS and the progressive drop in the ratio between taxpayers and beneficiaries due to changing demographic variables.[49] According to an analysis of financial projections of the new system, the generation of savings over time critically depends on the assumption of excluding people who are ineligible under the new requirements, but who would have received pensions under the old system. This feature puts the system's fiscal objectives at odds with its social objectives, constituting a significant future challenge.[50]

Expansion of capital markets. The creation of domestic institutional investors (pension fund managers known as AFAPs) as part of the program resulted in a high concentration of capital in a single company, without significantly influencing the development of capital markets.[51] According to central bank data, as of December 2004 the pension fund managers invested nearly 80% of their total funds in government financial instruments (nonfinancial public sector, central bank and public banks), thereby contributing more to financing the fiscal deficit than to financing the private sector. However, some experiences such as the creation of trusts by the pension fund managers, particularly in the agriculture sector, signal their potential for financing productive investments.

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47 It is also worth noting that total expenses and social insurance costs increased during those years, so this outcome cannot be attributed to a "denominator effect." Unfortunately, data on operating expenses in past years could not be obtained. See www.bps.gub.uy, Statistical Data, Principal Indicators.

48 Source: Economic and Actuarial Consulting of the BPS and Office of the Comptroller General. In particular, Annex 1.2 to the loan document provides a projection of total BPS outlays for each five-year period from the year prior to the reform (1995) to 2040. Under the assumptions of an "intermediate scenario," the projection predicts that BPS spending in all areas (i.e. for pension and activity benefits) would be US$2.332 billion in the year 2000, whereas the amount spent according to internal BPS data totaled US$3.012 billion. The same annex projects that the amount of the BPS deficit to be covered by the Treasury (net financial assistance) in the year 2000 would be US$520 million, whereas the actual total according to data from the Office of the Comptroller General was US$909 million.

49 Among the factors directly related to social security are the cost of conversion to the capitalization system and the legal impossibility of eliminating the mechanism of indexing contributions to the average wage change in the private and public sectors (this has not been possible since 1989, as a result of a change in the National Constitution). Indirectly related factors include demographic and economic factors; economic factors are fundamentally related to the exchange appreciation process and strengthening of actual salaries which was verified in the years preceding the reform, and more recently to the impact of the crisis on the system's revenues.

50 Forteza, Alvaro. "Uruguay Opts for Pension Reform" (2004).

51 Pension savings under the capitalization plan were originally managed by six pension fund managers (which currently number four) with a majority stake held by the state-owned pension fund manager, República.

Background Document 6: Analysis of outcome indicators
Private capital participation in essential services

The model of opening essential services that had traditionally been public monopolies to competition and private capital was supported by the Bank early in the last decade through certain conditionalities included in a sector investment loan.[52] In particular, this program's objective was to enhance the efficiency of the services provided by public companies through promotion of private capital participation in port services, air transportation, electric power, and telecommunications.[53] The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 6.1: Analysis of Outcome Information

Outcome	Bank		OVE
	Initial target indicator	Monitoring indicator	Attainment level
Opening to competition			
Incorporation of private capital	No	No	Medium
Improvement in efficiency as service providers	No	No	Limited

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Incorporation of private capital. Public opinion generally ran against opening these markets to competition. This gave rise to political controversy, leading to partial, dissimilar outcomes for each of the markets in question.[54] Although private capital was successfully incorporated into port services and air transportation, in the telecommunications sector the attempt to privatize ANTEL, the state-owned telecommunications company, had no effect as a result of a constitutional referendum. In the electrical power industry, the private sector was allowed greater participation in the generation stage, although no private capital has been attracted to date.

Improvement in service efficiency. Partially opening public utility markets to competition has not necessarily resulted in an improvement in their cost structures or their efficiency as providers of essential services. Although there has been improvement in the quality of services provided in some sectors (e.g. telephone connectivity, shorter wait times, etc.), the rate systems still respond to the revenue requirements of the public sector, making the economy less competitive as a whole.

[52] UR-0057, US$68.8 million, 1992. From a strategic standpoint, having the Bank's investment programs executed by public companies does not appear to be consistent with the objective of opening them up to competition.

[53] Under Law 16211 of 1991 (called the Public Corporations Act), the Port Services Reform Act of 1992, and the corresponding regulations.

[54] The most recent example that illustrates this situation is the state fuel company, ANCAP. In March 2001 a law was passed which allowed ANCAP to partner with foreign private capital, but it was repealed by referendum in December of the same year.

Background Document 7: Analysis of outcome indicators
Development of the financial system

To stimulate financial market development, the Bank approved a series of loan and technical-cooperation operations in the period 1991-2004.[55] According to the loan documents, the portfolio to develop Uruguay's financial sector had the following objectives:[56] (i) to improve the efficiency and competitiveness of the financial intermediation system and restructure public banks; (ii) to promote an increase in private investment and development of the medium- and long-term credit market and the stock market; and (iii) to strengthen the regulatory and bank supervision framework, so as to preserve the soundness and liquidity of the system's institutions. The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 7.1: Analysis of Outcome Indicators

Outcome Indicator	Bank		OVE
	Initial target indicator	**Monitoring indicator**	**Attainment level**
Financial intermediation system:			
Improvement in market competition and concentration (UR-0031)	No	No	Limited
Improvement in the efficiency of financial institutions (UR-0031)	No	No	Medium
Restructuring of public banks (UR-0031)	No	No	Medium
Development of private investment:			
Increase in private investment (UR-0057)	No	Yes	Limited
Expansion of the medium- and long-term credit market (UR-0063, UR-0021, UR-0136)	No	Yes	Medium
Development of the stock market (UR-0057)	No	No	Limited
Regulatory and supervision framework:			
Application of supervisory measures and soundness and liquidity indicators to institutions in the system (UR-0031, UR-0150)	No (UR-0031) Yes (UR-0150)	No (UR-0031) Yes (UR-0150)	Limited Medium

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Competition and concentration of financial intermediation. According to central bank data, the banking market in Uruguay remained highly concentrated in the 1990s in the form of a public bank that comprised Banco de la República Oriental del Uruguay [Bank of the Oriental Republic of Uruguay] (BROU) and Banco Hipotecario del Uruguay [Mortgage Bank of Uruguay] (BHU), in terms of both deposit-taking and lending. During the last three-year period covered in the table (1999-2001), there was a slowdown in the public banks' participation in the system, but this occurred within the overall context of a contraction in credit and temporary increase in nonresident deposits in private banks.[57]

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55 The following operations make up the financial sector development portfolio: financial sector adjustment program (UR-0031), investment sector program (UR-0057), global multisector credit programs (UR-0063, UR-0021, UR-0136), and the sector program to strengthen the banking system (UR-0150).

56 PR-1784, paragraph 1.13; PR-1877, paragraph 2.1; PR-1876, paragraph 3.1.

57 Source: Data from the Central Bank of Uruguay's (BCU) Statistics Bulletin.

Table 7.2

Percentage of deposits in the system[1]			
	BROU	BHU	Private Banks
Average 90-92	32.3%	10.6%	57.2%
Average 96-98	31.4%	11.4%	57.2%
Average 99-01	26.8%	10.5%	62.7%

Percentage of loans to the private sector[2]			
	BROU	BHU	Private Banks
Average 90-92	31.7%	27.7%	40.6%
Average 96-98	27.5%	25.1%	47.5%
Average 99-01	26.5%	18.1%	55.4%

Source: Internal document based on data published in the BCU's Statistics Bulletin, June 2003.

1 Includes deposits in Uruguayan pesos and foreign currency, from both the private sector and public companies. Excludes deposits in the central bank.

2 Largest component of the total loan portfolio of each institution or group.

Efficiency of financial intermediation. The expected outcomes in terms of making the bank intermediation system more efficient were limited by the lack of competition, as well as by a number of structural problems such as information discrepancies, limited access to financing for most local operators and the low level of monetization of the economy, which generated high administrative and transaction costs. As a result, intermediation margins as an indicator of efficiency, although falling during the 1990s, remained at an average of 46.9% in national currency and 8.2% in dollars, well above the figures for the Chilean market (15.1% and 4.3%) or the Argentine market (23.5% and 9.5%).[58]

Restructuring of public banks. The conditionalities related to the restructuring of public banks did not result in improvements in their portfolio quality, financial position or exposure to exchange risk. In particular, BROU retained a significant proportion of the lending market during the 1990s on terms that did not always reflect market conditions, a situation that led to a growing financial and capital impairment.[59] At the end of the program, BROU continued to enjoy certain privileges compared to private banks, such as exclusive intermediation in deposits from public companies, collection of the international trade tax and exemption from VAT on its consumer loans. Meanwhile, BHU, whose structural reform was also part of the financial sector loan conditions, continued to be largely financed by deposits from the public (mainly dollar-denominated with relatively

58 See Philip Brok and Helmut Franken, M. "Sobre los determinantes de los spreads marginales y promedio de las tasas de interés bancarias: Chile 1994-2001 [Determinants of margin spreads and average bank interest rates: Chile 1994-2001]." Central Bank of Chile. Vol. 6, No. 3, December 2003; and Luis Catão, "Intermediation Spreads in a Dual Currency Economy: Argentina in the 1990s" Working Paper, IMF, June 1998.

59 An example of this situation was when BROU granted soft credit lines to the agricultural sector late in the last decade. This subsequently forced a large part of the delinquent portfolio to be refinanced, due to liquidity problems in this sector caused by foreign exchange appreciation and less favorable terms of trade. As reported in Bank document PR-2674, in 2001 the government gave BROU US$20 million in budgetary funds, thereby revealing the subsidy granted to producers in debt, who by virtue of this measure were able to refinance their debts of up to US$200,000. As might be expected, this situation worsened with the financial crisis of 2002. According to data published by the Asociación de Empleados Bancarios del Uruguay [Uruguayan Association of Bank Employees] (AEBU) in 2003, the percentage of BROU loans to agricultural producers that were recovered through collection proceedings, both in and out of court (loans considered delinquent, regardless of the number of months in arrears), increased in recent years from US$268 million at year-end 2001 to US$351.7 million in July 2003. The same source reports that BROU had 15,010 rural customers in mid-2003, 26% of whose debts were considered bad debts.

short maturity dates) and extended medium- and long-term lines of credit offset primarily by salary deductions, leading to high exchange risk exposure.[60] When the peso was devalued and the 2002 financial crisis began, BHU lost a total of US$1.1 billion, more than any other bank in the country.

Development of medium- and long-term bank credit and the stock market. There were problems involved in investing the funds of multisector credit loans, and no data is available which relates the periods of loan concentration to the development of the medium- and long-term credit market.[61] Because these facilities brokered by the banks were made available at a time of high liquidity of the system and low market rates, there was little demand for the multisector credit programs for extended periods of time. The times when funds were concentrated occurred under highly restrictive market conditions, including the financing of unproductive investments such as real estate purchases (for 24% of the funds of the first multisector credit program), from 1996 onward. The lack of long-term credit remains a bottleneck for the growth of the economy.

Support for stock market development as a supplementary measure to stimulate private investment paved the way for the initial investment in private issues in the 1990s, although this activity practically ceased later on.[62] During the 1998 stock market boom, volumes close to US$1.8 billion (approximately 8% of the GDP) were traded, although 86% of the transactions were treasury bonds and certificates of deposit.[63] Private issues for long-term financing through negotiable bonds represented a marginal share (2% of total stock market transactions in 1998). Due to regulatory and supervisory problems which occurred before

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60 These subjects have been documented in a recent research project by the Bank (IADB-RES Working Paper No. 503, "Los efectos del sector público en el financiamiento de la vivienda: El mercado hipotecario del Uruguay [The effects of the public sector on the financing of housing: The mortgage market in Uruguay]," January 2004. In terms of the currency mismatch, the working paper shows that in the period 1992-2001, the proportion of assets to liabilities (distinguishing between national currency and foreign currency) was nearly 1 for all private banks, whereas the foreign currency assets of BHU never exceeded 10% of liabilities in any one year. Regarding the maturity mismatch, during the same period it was reported that private banks maintained current assets to finance an average of 70% of their current liabilities (with a maturity of less than one year), whereas in the case of BHU assets readily convertible in less than one year did not cover 1% of all liabilities falling due within 12 months or less. Finally, the study also addressed the high rate of delinquency in that institution's credit portfolio, which was due to the lack of efficient methods for evaluating borrowers, character risk problems, etc. According to data provided from that source, the ratio of overdue loans to total current loans was 11% in December 1998, a rate that worsened drastically thereafter, reaching 42% at the end of 2001.

61 In terms of bank savings, taking the banking system as a whole, the ratio of private sector time deposits to this sector's total deposits in national currency remained nearly constant during the second half of the 1990s, with a slight decline at the end of that period. It should also be considered that the definition of 'time' deposits in national currency refers in general to contracts of no more than 90-120 days.

62 Approval of the Stock Market Act (Law 16749 of 1996), included in the sector investment loan, must be viewed within the context of the approval of other measures such as the deregulation of the insurance market, the creation of pension funds (through social security reform) and local investment funds. These funds were considered essential to sustained growth and the expansion of the stock market.

63 A large portion of these instruments (e.g. euro bonds and euro notes, brokered by commercial banks and having an average maturity of 10 years) had to be refinanced through the voluntary swapping of the Uruguayan government's debt with the private sector in 2003.

those during the banking crisis, these issues gave rise to fraud that ultimately led to lasting public distrust of this type of financial instrument.

Bank regulation and supervision. The conditionalities of the 1991 financial sector loan led to improvements in adapting regulations to the Basel standards.[64] However, these structural problems in the regulatory system persisted during those years, and in some cases were related to the limited practical application of the approved rules, and in others to the limited supervisory capacity assigned to the central bank, leaving the system highly vulnerable during the 2002 crisis.[65] Despite the public bank portfolio's clear exposure to risk, this issue was practically sidelined with respect to the applicability of the bank supervision and control criteria.[66] The importance of offshore business to private banks did not lead to separate supervisory criteria for these types of transactions, which caused great exposure to risk.[67] The supervision system instituted in this stage did not cover the operating and market risks of the managed banks, which accelerated the banking crisis.[68]

The crisis of 2002 revealed a number of weaknesses in the supervision system developed during the 1990s with Bank support, and considerably impaired the assets of the country's main banks. The sector program to strengthen the banking industry approved in the last quarter of 2003 sought to make up for many shortcomings of the previous model and

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[64] The most important progress in terms of financial legislation was the following: in 1992, approval of Decree 614/992 implementing the Financial Intermediation Act (Law 15332); and in 1995, approval of Law 16656, establishing the central bank's charter and rules governing its main powers, monetary policy and management of reserves, relationships with financial intermediation institutions, including authority to deal with troubled banks, entering and leaving the system, the authority of the Office of the Superintendent of Financial Intermediation Institutions (SIIF), etc.

[65] The conditionalities of sector loans consisted primarily of legislative approvals, but full application of the rules and regulations was not guaranteed. For example, in the case of the financial sector loan program (UR-0031), the Office of the Superintendent of Financial Institutions and its hierarchical structure were established, but there were still problems associated with enforcing regulatory and supervisory rules, especially in the case of the country's largest banks. In addition, there were problems related to the design of the conditionalities which obviously restricted their potential impact. Referring again to the financial sector loan, insufficient consideration was given to the fact that BROU was regulated (by law) as an independent agency of the executive branch of government, which is why its transformation or restructuring could not be imposed by the Bank (see Ex Post Evaluation, PPR-11/70, EVO, December 1997, paragraph 3.18).

[66] Significant delays and a lack of transparency were observed in the presentation of balance sheets, along with a failure to submit income statements, etc. In addition, financial oversight of these institutions was frequently bypassed, which resulted, for example, in worse currency and term mismatch problems at BHU, and in the refinancing (funded by the Treasury) of the portfolio of delinquent loans made to the agricultural sector by BROU. Despite the importance of the public banks in Uruguay in terms of size and "market share" during the entire period analyzed, the SIIF (subordinate to the BCU) did not have the power to sanction them.

[67] Although records were kept on the amounts involved in nonresident transactions, there was no information on where those resources were invested or in what type of assets or currency.

[68] Although operating risk is related to the internal governance problems of the institutions, market risk focuses on problems related to a potential widespread drop in the value of a group of financial assets which would force one or more banks to absorb significant losses.

correct the effects of the crisis on the financial system's liquidity.[69] Restoring the liquidity and reliability of the system was extraordinarily costly to the country, which relied on syndicated financing provided by multilateral lenders.[70] To date, this program has made tangible progress in terms of strengthening bank regulation and supervision as well as the implementation of prudential rules by financial institutions, recognition of the central bank's sanction-wielding authority and certain measures to strengthen it as an institution.[71] Since the rescheduling of deposits has been completed, the banking system can now operate with high levels of liquidity, with the ability to handle any withdrawals of short-term liabilities.[72]

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69 Paradoxically, the restructuring of the public banks is not included in this program's objectives, but is part of the conditionalities of additional World Bank and IMF loans. BHU is carrying out its restructuring process by refraining from taking deposits from the public, securing part of its asset portfolio, and transferring its portfolio of deposits (which requires paying a BHU note (or if none exists, a government note) to BROU). BROU has reassigned most of its poor quality asset portfolio to recovery funds (trusts), which performed better than expected over the course of 2004 (see "IMF, Uruguay: Letter of intent and technical memorandum of understanding," November 2004).

70 The cost of the government's assistance to the financial sector as a result of the 2002 crisis was an estimated US$2.37 billion (19% of the GDP). Part of this assistance consisted of creating a Fund To Stabilize the Banking System (FESB) in August 2002 (the worst point of the crisis), in order to provide the liquidity necessary to contend with any withdrawals of deposits from sight and savings accounts in the system's banks. This fund, valued at approximately US$1.5 billion, was fully financed through the contributions of multilateral agencies. In gross figures, some US$800 million were contributed through new IMF financing, with another US$700 million provided by rechanneling and/or accelerating disbursements from the already existing programs of the IDB (US$500 million) and the World Bank (US$200 million).

71 In the most recent project performance monitoring report (PPMR) of June 2005, it is estimated that by August 2005 the three still-pending conditionalities could be satisfied in order to implement the second part of the loan, i.e.: (i) introduction of rules on minimum bank capital in financial regulation, based on market risks; (ii) addition of sufficient technical and professional staff to strengthen human resources assigned to supervise banks and other financial intermediaries; and (iii) a review, satisfactory to the Bank, of the quality of bank inspections conducted by the Office of the Superintendent of Banks of Uruguay.

72 The system's liquidity ratio, defined as the ratio of liquid assets to current short-term liabilities (less than 90 days), was about 80% in 2004 for the average private bank, 70% for BROU, and 140% for Nuevo Banco Comercial (NBC). NBC's short-term liabilities are considerably less than those of the other banks in the system, due to the fact that the majority of its liabilities consist of six-year certificates of deposit.

Background Document 8: Analysis of outcome indicators
Development of the agricultural sector

To support greater competitiveness in the agricultural sector, the Bank approved a portfolio of specific projects during 1991-2004 to support the dairy, fruit and vegetable, grape and wine, and livestock sectors, supplemented by support for animal health and agricultural services.[73] The following table shows the outcomes for this objective, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 8.1: Analysis of Outcome Information

Outcome	Bank		OVE
	Initial target indicator	Monitoring indicator	Attainment level
Productive development			
Increase in production efficiency for dairy producers (UR-0065, UR-0062)	Yes	Yes	High
Increase in dairy exports (UR-0062)	No	No	High
Increase in value of farm products and exports (UR-0072)	Yes	Yes	High
Validation of the feasibility of production innovations (UR-0137)	Yes	Yes	High
Animal health and agricultural services			
Increase in production efficiency and exports of the agricultural and agroindustry sectors through technical services (UR-0116)	No	No	Limited

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Production efficiency of dairy producers. The provision of electricity and roads to improve production and reduce transportation costs in the dairy belts led to significant increases in production and output during the 1990s. According to agricultural census data, milk production in Dairy Belt I (Canelones, Colonia, San José and Florida) rose 57% between 1990 and 2000, just trailing the sector average. Milk production in Dairy Belt II (Durazno, Flores, Paysandú, Río Negro, Salto and Soriano) increased 80% over those ten years, and the productivity per head of cattle rose 1% per year.[74] The improvement of roads used for bulk shipments in the dairy belt helped reduce harvesting costs by 35%.[75]

Increased value of farm products and exports. According to data provided by the institution in charge of the project (PREDEG), the technological improvements made under the project resulted in an estimated 15% increase in exports.[76] Due to

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[73] Dairy belt development program I (UR-0065) and II (UR-0062), farm reconversion and development program (UR-0072), agricultural services program (UR-0116).

[74] Source: 1990 and 2000 National Agricultural Census. The programs supporting dairy belts led to improved health conditions, essential for building confidence the country's dairy industry.

[75] There were strong growth trends in export volumes between 1990 and 2003, with less dramatic growth in their dollar value. For Dairy Belt II, there was a 35% drop in milk collection costs (the project expected 30%), a 100% increase in bulk milk shipments (the program expected 90%), and a 5.2% increase in milk shipments to processing plants (the project expected 4.4%).

[76] The Logical Framework assumptions that did not hold were: national and regional economic stability, performance of commercial integration agreements in MERCOSUR, access to credit, continuity of the PRENADER program for the development of natural resources and irrigation (WB) to support irrigation investments and approval of regulations on the marketing of fruits and vegetables by the Ministry of Livestock, Agriculture and Fishing (MGAP).

competitiveness gains by small- and medium-sized farmers, deciduous tree exports increased to 6,000 metric tons, and honey exports increased to 8,000 metric tons, double the expected goals in both cases.[77] In addition, the project reached the goals set for the renovation of fruit plantations and vineyards, replacing existing varieties with others of greater commercial value, and the program was effective in terms of diversification of foreign wine markets.

Increased livestock competitiveness. The pilot project to improve livestock competitiveness promoted the adoption and validation of innovations by private parties all along the production chain with proven productivity gains in reproductive efficiency, average age of operation and other production factors. Despite the fact that the project indicated a lack of coordination between producers and markets and a need to identify new commercial opportunities, consistent information was not gathered on increased billings in sales and exports as an indicator of competitiveness. Meeting its demonstration objective, the project clearly showed that there was strong demand for technological innovation and was used to prepare a larger-scale program to improve livestock competitiveness.[78]

Increased production efficiency in the agricultural and agroindustry sectors through the provision of agricultural services. The services provided under the phytosanitary certification project and technological research project did not furnish data on outcomes in terms of production efficiency, and private sector participation was less than expected.[79] According to existing documentation, the animal health project technically contributed to erradication measures which made it possible to obtain status as a "foot-and-mouth disease free country where vaccination is not practiced" after the first outbreak of that disease.[80] However, limited developed capacities in the area of prevention and border control, combined with the ease of contracting foot-and-mouth disease, led to another outbreak in 2001 with serious consequences for the sector's exports and the economy as a whole.[81] The agricultural services program helped Uruguay to later be declared a "foot-and-mouth disease free country where vaccination is practiced."

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77 Source: FAO Agrostat and PREDEG.

78 UR-0141 program to develop livestock competitiveness.

79 The subcomponent on restructuring of the Livestock Services Directorate was used as an additional source of administrative resources. Moreover, the National Agricultural Research Institute (INIA) funded 11 areas of strategic research, so this dilution of funds limited the results achieved by the project in this specific area and overestimated the private sector's demand to participate in the execution of the applied research projects.

80 The status of foot-and-mouth disease free country where vaccination is not practiced (PLASV) constitutes the highest health status that exists.

81 The closure of high-value international markets caused a 37% drop in volumes and a 40% drop in exports between 2001 and 2003. The reopening of these markets in 2003 led to a recovery of values in 2001. The cost to the Uruguayan economy was estimated to be 2% of the GDP in 2001 and 2002 and 1.5% of the GDP in 2003 (Source: Office of Agricultural Programs and Policies (OPYPA) 2004 Yearbook).

Background Document 9: Analysis of outcome indicators
Technology development to promote competitiveness

To stimulate the competitiveness of companies challenged by trade liberalization, the Bank established a sequence of two lending programs, the first approved in 1991 and the second in 2000, which is still in execution.[82] According to their loan documents, these projects sought to increase efficiency in productive activities by developing national science and technology capacity. The following table shows the outcomes for this objective, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 9.1: Analysis of Outcome Indicators

Outcome	Bank		OVE
	Initial target indicator	**Monitoring indicator**	**Attainment level**
Technology development: Improvement in national research capacity for productive applications (UR-0095, UR-0110)	No	No	Limited

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Improvement in national research capacity for productive applications. The thematic selectivity of the support provided by the first program was inconsistent with the focus on productive applications that was the basis of the program's original design and formed part of its objective.[83] The amount allocated to companies was small, just 3.5% of national investment in applied research and development.[84] The project's low rate of productive application is closely related to the institutional arrangements set in its design.[85] In the second stage of the program, which is still in execution, the program was subject to reductions in resource allocations as a result of the fiscal crisis, concentrating relatively

82 Science and technology program (UR-0095) and technology development program (UR-0110).

83 Loan document PR-1806, paragraph 2.5, and operational objective.

84 Equal to 3.5% of national investment in R&D applied to business, according to data from the Ibero-American Network on Science and Technology Indicators (RYCIT) and the World Bank on the average amount of the program investment applied to business.

85 The limited results in the area of competitiveness are partly due to the decision to localize the project in the National Innovation, Science and Technology Council (CONACYT) which did not necessarily maintain a focus on applied research and had limitations in terms of the necessary coordination among institutions. Shortfalls in institutional capacity were not corrected by the project nor by the technical cooperation resources that were allocated for its institutional strengthening, which is why the second program addressed different institutional stakes, creating a new unit reporting directly to the Ministry of Education and Culture and parallel with the recently created National Science, Technology and Innovation Directorate (DINACYT). According to the December 1999 PPMR, "CONICYT [sic] did not manage to effectively use the resources for the technical cooperation project which was approved to strengthen it, among other objectives" (ATN/SF-3871-UR). The program executing agency was deliberately created as a parallel structure, in addition to and separate from the DINACYT. However, both are located in the same place, and currently the staff expenses of the program executing agency and DINACYT cannot be clearly differentiated, since former DINACYT staff are working for the project, with salaries paid partly by DINACYT and partly by the project counterpart (item "PCU employee incentives," in the project's accounting records).

high percentages of its reduced resources in program management activities.[86] Because of this, uncertainty spread among the companies with respect to the repayment of investments already made, which, within a context of financial problems and risk aversion, was reflected in shrinking demand for production-oriented projects.[87] From the standpoint of their impact on competitiveness, the programs did not appear to have had significant influence, considering the discouraging trends in national investments in technology development.[88]

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86 According to the December 2002 PPMR, "the program did not direct the fewer resources available to the execution of the top priority components aimed at reactivating production, but allotted relatively high percentages of resources to the administration of the program and the institutional strengthening of organizations in the national science and technology system."

87 Half-yearly report, December 2004, technology development project.

88 Source: Ibero-American Network on Science and Technology Indicators (RYCIT) and the World Bank, 2003.

Background Document 10: Analysis of outcome indicators
Development of physical infrastructure to promote competitiveness

1.1 In response to the competitive challenges posed by economic integration, the Bank introduced a portfolio of infrastructure projects with the following objectives: (i) to boost the efficiency of the electric power supply; and (ii) to reduce the costs of overland and maritime transportation by improving roads and ports. The following table shows the outcomes for these objectives, indicates whether the Bank established initial target or attainment indicators, and presents the conclusions of OVE's evaluation of each of them.

Table 10.1: Analysis of Outcome Indicators

Outcome	Bank		OVE
	Initial target indicator	Monitoring indicator	Attainment level
Electric power supply: Efficiency of supply (UR-0022)	Yes	Yes	High
Commercial and tourist transportation: Reduction of transportation costs in integration corridors (UR-0113)	Yes	Yes	High
Improved tourist access to Punta del Este (UR-0029)	No	No	High
Improvement in competitiveness of wood and agricultural exports shipped through the port of M'bopicua (UR-0142)	No	No	Medium

Below is the detailed analysis to support the conclusions of this evaluation for each outcome, based on impact indicators verified by OVE.

Improved efficiency of electric power supply. Financing of the project to connect Ribera-Libramento with Brazil and corresponding improvements reduced outages from 12.5 hours per year to 2.7 per year in the cities covered by the project outside the metropolitan area of the capital. However, the connection was used less than expected during the life of the project, primarily because it designed as a backup, although its use likely increased as a result of shortages in the power supplied by Argentina.[89] Nonetheless, in the context of the current energy shortage, the power transmission capacity from Brazil developed under this project is insufficient.[90]

Improved efficiency in commercial and tourist transportation. The programs that were funded resulted in the rehabilitation of the national roads and bridges which are part of the integration corridors, thereby reducing estimated transportation costs from 22.9 to 21.7 cents per kilometer. The project's social and economic return was impacted by the effects of the crisis in terms of reduced road use.[91] The highway concession financed by

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89 The ex post cost-benefit evaluation of the Rivera-Libramento component shows that exchanges for the year 2001 were 78.4 GWh, 0.151 GWh for 2002, 0.45 GWh for 2003 and 281.055 GWh for 2004 (up to September) which is much less than anticipated by the project, which was an average of 1500 GWh between 1998 and 2002. However, compared to projections provided by the company UTE, current net value exceeded expectations (US$35 million vs. US$23 million).

90 One of the alternatives studied since the prefeasibility stage of the project, albeit with a significantly higher cost, was a connection with Brazil from the Porto Alegre side.

91 According to the project completion report (UR-0113), page 10, the internal rates of return re-calculated ex post all sections and bridges were lower than budgeted. In the case of the Montevideo-Punta del Este highway, the evaluation of expost profitability was adversely affected by the impact of the crisis on toll sales.

the Bank's Private Sector Department (PRI) for the section from Montevideo to Punta del Este had considerable socioeconomic impact in terms of the expansion of this tourist enclave. In terms of port transportation, PRI funds were used to construct the port of M'bopicua, specifically to address the recent expansion of the timber industry in the northern part of Uruguay and Argentina. Although the port has had significant economic impact on this industry, maximization of its financial and economic return is contingent upon its still limited water depth, which limits the capacity of the load being shipped.[92]

[92] There is currently an institutional coordination problem with the Río Uruguay Administration Commission (CARU), on reaching a binational decision to approve and execute the dredging work required to increase the water depth of the river, which would create navigable conditions for higher capacity ships that travel upstream to such ports as M'bopiqua.