



1. Project Data:		Date Posted : 02/03/2003	
PROJ ID: P062991		Appraisal	Actual
Project Name: AR Special SAL (SSAL)	Project Costs (US\$M)	8,300	40,000
Country: Argentina	Loan/Credit (US\$M)	2,525	2,275
Sector(s): Board: EP - Central government administration (28%), Banking (28%), General finance sector (17%), Compulsory pension and unemployment insurance (15%), Other social services (12%)	Cofinancing (US\$M)	5,775	37,725
L/C Number: L4405; LB115			
	Board Approval (FY)		99
Partners involved : IMF, IDB	Closing Date	12/31/1999	10/31/2000

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2. Project Objectives and Components

a. Objectives

The stated objective of the Special Structural Adjustment Loan (SSAL) was to reduce Argentina's "vulnerability to external financial shocks" while "simultaneously increasing (its) capacity for sustainable and equitable growth ." The loan was consistent with the 1997 CAS (and the February and November 1998 updates). Specifically, the loan was to:

- (A) facilitate the re-entry of Argentina into international capital markets without depleting foreign exchange reserves;
- (B) protect vulnerable groups during the period of high uncertainty;
- (C) help the banking system withstand liquidity shocks; and
- (D) continue the long term development of savings and capital markets with better regulation, tax and spending policies.

The larger objective of the SSAL, along with other loans from the Bank, Fund and the Inter -American Development Bank, was to help Argentina maintain its currency peg during what was perceived to be a temporary disruption in international capital flows aggravated by the August 1998 Russia crisis (but before the Brazilian devaluation in early 1999).

b. Components

The SSAL supported reforms in three broad areas :

- (A) intergovernmental fiscal relations under which intergovernmental transfers would be simplified and better allocated;
- (B) financial sector under which (1) banking supervision would be improved and public sector involvement would be reduced; (2) SME access to credit would be improved through better leasing laws; (3) capital markets would be deepened by introducing private pensions and by liberalizing insurance; and
- (C) human development under which (1) poverty programs would be better managed and targeted, (2) the quality and efficiency of public education would be improved, and (3) the health system efficiency would be improved .

The loans were to give the Government time to make its fiscal balance consistent with its currency peg . The SSAL's tranche release conditions supported structural reforms, and while some were central to averting the crisis (e.g. fiscal relations with provinces) others had longer term benefits (e.g. measures to make banking, education and health more efficient). Some measures like labor reforms would have reduced unemployment and thereby pressures on government spending. The measures were based on the Bank's considerable ESW in these sectors .

c. Comments on Project Cost, Financing and Dates

The SSAL of \$2,525 m, along with a \$505 m Special Repurchase Facility Support Loan (Repo loan described in the

same President's Report) approved in November 1998, were the Bank's portion of a \$8.3 b package of international support that included the Fund's Extended Fund Facility of \$ 2.8 b (in early 1998) and \$2.5 b from the IDB (which cofinanced the Bank's SSAL and repo loans with \$ 2,000 m and \$500 m respectively).

The SSAL differed from standard Bank terms : the loan was to be repaid in five years (including 3 years grace) with an interest rate of LIBOR plus 400 basis points. The loan was also processed quickly and approved speedily . Disbursement was in three tranches (with the first two being \$ 1,000 m each), but when Argentina's financing needs rose after the SSAL was approved, there was a delay as a new package was assembled . The Fund had increased its support from \$2.8 b to \$7.4 b (Standby Arrangement March 2000, after the Brazilian crisis) and \$250 m of the SSAL's second tranche was cancelled and allocated to a (separate) \$1.1 b policy based guarantee in October 1999. The SSAL's last tranche was released by September 2000 -- when the stabilization program appeared to be on track . Argentina's program with the Fund went off track in November 2000. The Fund further increased its support to \$ 15.5 b (January 2001); but even these proved insufficient to maintain the currency peg which was abandoned in late 2001.

3. Achievement of Relevant Objectives:

The agreed measures were passed despite difficulties . Specifically

(A) Intergovernmental fiscal relations: the tax pooling arrangement was simplified, and poorer provincial governments were to receive larger transfers . A provincial VAT was introduced, and earmarked taxes were consolidated to make them more transparent .

(B) Financial sector: Fiscal requirements prevented full reforms of the financial instruments tax, and Congress did not pass the law giving regulators full immunity; but supervision and regulation are now better coordinated . The mortgage bank was privatized and laws on leasing and fund management were approved .

(C) Human development: poverty and health are measured better now, and government programs are better targeted. Labor laws that reduced taxes and eased restrictions on new workers were passed (when these issues were decoupled from collective bargaining reforms). More comprehensive proposals reducing severance payments and creating individual worker accounts were substituted for the original conditions (that were waived). Improvements in health insurance included increasing the number of providers and making their procurement transparent. Three federal nutrition programs were consolidated, cutting duplication, and new eligibility criteria were prepared for beneficiaries. Preparations began for reforms in higher education (merit selection, greater cost recovery etc.), although standardized tests may not have much backing (provincial responsibility).

4. Significant Outcomes/Impacts:

The international package of support (of which the SSAL was a significant part) failed to maintain Argentina's pegged exchange rate ("Convertibility Plan"). Outputs by SSAL's components were largely achieved, although the outcomes of the structural reforms were swamped by the subsequent economic collapse (in 2001). For example, the Government's decision to freeze banking deposits and convert them into pesos at a different exchange rate than loans has bankrupted the banks and undermined the improvements in banking supervision that the SSAL supported . Some of the improvements that the SSAL supported could bear fruit when conditions improve; hence the outcome is rated "unsatisfactory" (rather than "highly unsatisfactory").

5. Significant Shortcomings (including non-compliance with safeguard policies):

The peso's depreciation disrupted the economy because many contracts were dollar denominated . In particular, the Government required bank loans and deposits to be converted into pesos at differing rates thereby bankrupting banks. The political and economic turmoil undid many of the SSAL's achievements (e.g. in banking and provincial fiscal relations), and the economy is expected to shrink by 15 percent in 2002.

6. Ratings:	ICR	OED Review	Reason for Disagreement /Comments
Outcome:	Unsatisfactory	Unsatisfactory	(See section 4)
Institutional Dev .:	Modest	Modest	
Sustainability:	Unlikely	Unlikely	
Bank Performance:	Satisfactory	Satisfactory	
Borrower Perf .:	Satisfactory	Unsatisfactory	The Government did not maintain the necessary fiscal measures and was forced to abandon the peg in 2001, leading to banking controls, street protests, a change in government. GDP is expected to decline by 15% in 2002.
Quality of ICR:		Satisfactory	

NOTE: ICR rating values flagged with '*' don't comply with OP/BP 13.55, but are listed for completeness.

7. Lessons of Broad Applicability:

(A) Detailed ESW done during years of little lending allowed the Bank to lend quickly to support structural reforms

that were identified earlier.

(B) It is appropriate for crisis loans to support those structural reforms that *directly* and immediately help in dealing with the crisis (e.g. improving tax collections or inter-governmental fiscal transfers) or social programs protecting the economically vulnerable. It is less clear whether other needed structural reforms (e.g. improving the insurance industry) should be included (see section 8 below). The SSAL supported reforms of both types and the ICR mentions the conflicts between disbursing for liquidity support and the time-consuming process of getting the reforms underway.

(B) A short term crisis calls for a short term loan, and the SSAL is more appropriate than conventional Bank instruments. It is less clear, however, if the Bank should be a "residual lender" in Fund supported financial rescue packages. The loan amounts are unrelated to the benefits of structural reforms, and these benefits do not follow if stabilization fails.

8. Assessment Recommended? Yes No

Why? The large risks were well understood when the SSAL was prepared and approved. The sequence of events that subsequently unfolded leading to the economic collapse in 2001 are widely described both in the attachment to the ICR and in other publications.

A crisis is often seen as an opportunity for structural reforms because the political logjam is broken. On the other hand, (A) they could distract key people in government from focussing on more urgent issues and (B) any benefits may be swamped by the chaos of failed stabilization. It would be useful to know if the Bank should seek reforms in areas not directly related to the crisis at hand and if so, which type of reforms or sectors are more likely to endure. A cluster audit of similar loans to different countries conducted in a few years may help determine this.

9. Comments on Quality of ICR:

The ICR rightly emphasized the broader context and background of the loan. The Retrospective Review (attached as an Annex to the ICR) was particularly useful.