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IMPLEMENTATION COMPLETION REPORT

EL SALVADOR

SECOND STRUCTURAL ADJUSTMENT LOAN
(LOAN No.3646-ES)

MARCH 26, 1996

Country Operations Division II
Country Department II
Latin America and the Caribbean Region

CURRENCY EQUIVALENTS

Currency Unit	=	Colón (c)
US$1.0	=	c 8.755 (February 1995)
c 1.0	=	US$0.1142

FISCAL YEAR

January 1 to December 31

GLOSSARY OF ACRONYMS AND ABBREVIATIONS

BCR	Central Bank of El Salvador
BFA	Agricultural Development Bank
BANAFI	Industrial Development Bank
CCR	Rural Credit Bureaus
CEL	National Electric Power Company
CEM	Monetary Stabilization Bonds
CONAMA	National Council for the Environment
CONAP	National Privatization Commission
CORSAIN	El Salvador Investment Corporation
DAFP	Advance Spending Authorization
DGII	Internal Revenue Service
FIS	Social Investment Fund
FOSAFFI	Fund for the Restructuring and Recapitalization of the Financial System
HRIS	Human Resources Information System
ICR	Implementation Completion Report
IDB	Inter-American Development Bank
IFM	Integrated Financial Management
IMF	International Monetary Fund
INAZUCAR	State Sugar Marketing Agency
INCAFE	National Coffee Marketing Board
KfW	Kreditanstalt für Wiederaufbau
MIFIN	Ministry of Finance
MIPLAN	Ministry of Planning
MOST	USAID sponsored project on Modernization of the Salvadoran Tax System
NFSP	Non-financial public sector
NTBs	Non-tariff Barriers
PSMAP	Public sector modernization action plan
SEMA	Executive Secretariat for Environmental Policy
SAL	Structural Adjustment Loan
SIF	Social Investment Fund
SIDUNEA	Automated Customs Control System
SRN	National Secretariat for Reconstruction
SSF	Financial System Superintendency
TAL	Technical Assistance Loan
USAID	U.S. Agency for International Development

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SECOND STRUCTURAL ADJUSTMENT LOAN (Loan No. 3646-ES)

Preface

This is the Implementation Completion Report (ICR) for the Second Structural Adjustment Loan in El Salvador, for which Loan Number 3646-ES in the amount of US$50 million equivalent was approved on September 1993, and made effective on December 17, 1993.

The Loan was closed on December 31, 1994 as specified in the original closing date. The first tranche, released upon effectiveness, was fully disbursed on February 18, 1994. The second and final tranche was fully disbursed on January 11, 1995. Co-financing for the project was provided by Germany (DM 20 million).

This ICR was prepared by Ian Bannon, Lead Economist and reviewed by Ms. Kreszentia Duer, Projects Advisor, Department II of the Latin American and the Caribbean Region. The Borrower contributed to the preparation of the ICR by preparing its own evaluation of the program which is included as Annex I of the ICR.

The ICR is based on the President's Report, the Loan Agreement, and other material in the project file. This report is based on discussions with Bank staff, and on the findings of a mission to El Salvador in April 1995, which held discussions with Government officials regarding the Loan. The assistance of representatives from the implementing agency during the mission is gratefully acknowledged.

SECOND STRUCTURAL ADJUSTMENT LOAN
(Loan Number 3646-ES)

EL SALVADOR

Evaluation Summary

i. Despite high economic growth in the 1960s and 1970s, gross inequalities in wealth, income and access to land severely exacerbated social tensions, which erupted into an open civil war in 1979. As the conflict escalated, the economy was also affected by adverse terms of trade and a contraction of regional markets which, coupled with inappropriate Government policies, led to severe macroeconomic imbalances and low growth. The conflict also diverted public resources from infrastructure and the social sectors to military expenditures. By 1989, a full fledged economic crisis had emerged and the Government fell into arrears with international creditors, including the World Bank.

ii. The Cristiani Administration, which assumed office in June 1989, adopted a far-reaching economic reform program designed to revive growth and reduce poverty, and initiated peace negotiations which culminated with the signing of a peace agreement in 1992. The Bank sought to support the Government's reform program through the First Structural Adjustment Loan (SAL I) and the reactivation of its project lending pipeline.

Program Design and Objectives

iii. SAL I was designed to support the Government's 1989-94 economic reform program. The objectives of the program were to: (i) improve incentives to stimulate savings and investment in more efficient export oriented and import-substituting activities; (ii) increase tax enforcement capacity; (iii) improve the efficiency of financial intermediation; (iv) improve agricultural productivity; and (v) prevent a deterioration in the nutritional status of the poor during adjustment. The Government's strong commitment to reforms contributed to the successful outcome of SAL I, and the Bank therefore sought to continue supporting the Government's Structural Adjustment Program through a second adjustment operation. SAL II was designed to: (i) lay the analytical framework for a comprehensive public sector modernization effort; (ii) consolidate and deepen reforms supported by SAL I in taxation, privatization, trade, the financial sector, and social sectors and poverty alleviation; and (iii) promote actions to strengthen public expenditure, civil service, and environmental management, and restructure the hydrocarbon sector. The Loan supported reforms in: public sector modernization, public expenditure management, the civil service, taxation, privatization, the financial sector, the hydrocarbon sector, trade, the social sectors and environmental policy. SAL II was accompanied by a Technical Assistance Loan, which is still under implementation (paras. 4-5).

Implementation Experience and Results

iv. The overall outcome of SAL II has been very positive. The success of the program, the strong support it has received from the new Administration, and the continuation and deepening of reforms since the Loan closed, bode well for its sustainability. An appropriate macroeconomic framework is being maintained and growth has rebounded strongly, averaging 6.8 percent over the past four years. In most cases, El Salvador's strong economic performance exceeded the Bank's expectations and the current Administration is carrying out comprehensive reform programs in public sector modernization, globalization of the economy, the private sector environment, and the social sectors (paras. 15-18).

v. SAL II supported an ambitious reform program, with second tranche conditionality covering 23 major areas, many of which included several sub-conditions. There was full compliance with actions required in all but two of these areas (there was partial compliance in sugar mill privatization and the hydrocarbon sector), and in a number of areas reforms exceeded the stipulated conditionality. In the case

of sugar mill privatization the Government chose a more comprehensive approach in order to privatize all six mills, instead of the more modest target of one privatized mill under SAL II. For hydrocarbons, the Government met four of the five subconditions and took alternative steps to deal with the fifth subcondition (implementing an alternative, less distortionary system for diesel subsidies). Partial waivers for these two subconditions were fully justified. Implementation suffered some delays, largely due to the change in Administration and the comprehensiveness of the conditionality. These delays, however, had little impact on the substantial success of the overall reform program (paras. 19-43).

vi. The Bank appropriately identified, appraised and supervised the program. Two key features in the Bank's performance were a high degree of organization in the design and implementation of the Loan, and staff continuity. The Borrower was actively involved in the design and implementation of the Loan, and clearly demonstrated strong ownership of the reform program. Borrower staff continuity was also an important factor (paras. 44-49).

vii. The summary ratings (Table 1) are:

- Achievement of objectives: substantial;
- Program sustainability: likely;
- Bank performance: highly satisfactory;
- Borrower performance: highly satisfactory; and
- Assessment of outcome: highly satisfactory

viii. The main conclusions and lessons learned are:

- Borrower ownership of an adjustment program is critical. Because of the Government's strong commitment to the reforms supported by SAL II, the negotiation and implementation of the program was achieved in an environment of mutual confidence.

- A change in government during the implementation of a program inevitably leads to some delay in compliance. For this reason it is important to accentuate the use of first tranche conditionality whenever approaching an electoral year. SAL II was not designed in this manner, since the Bank originally expected that implementation would be completed within a single administration. In the event, the implementation period did extend beyond the life of one administration. However, because of the strong commitment of the new Government to continue the reforms, the change in administration did not prove to be a problem in this case.

- A follow-on structural adjustment operation is likely to be successful if: (i) sequencing is appropriate; and (ii) there is continuity in the staff, both in the Government and in the Bank, working on both operations.

- The financial sector is highly vulnerable to structural economic changes, requiring a gradual and careful sequencing of reforms. In the case of El Salvador, banking sector reforms were well sequenced and gradual (capitalization, and privatization of the banks, accompanied by actions to reinforce the Superintendency).

- It is essential to ensure Borrower consensus on the reform agenda at the time of appraisal. The communication of program goals and objectives to all affected entities is important in gaining the necessary support for successful implementation. In this sense, the careful preparation of detailed action plans and intensive coordination of studies, played an important role in communicating to the affected institutions the rationale and steps involved in the reform.

PART I: PROGRAM IMPLEMENTATION ASSESSMENT

1. Despite high economic growth in the 1960s and 1970s, gross inequalities in wealth, income and access to land severely exacerbated social tensions, which erupted into an open civil war in 1979. As the conflict escalated, the economy was also affected by adverse terms of trade and a contraction of regional markets which, coupled with inappropriate Government policies, led to severe macroeconomic imbalances and economic stagnation. The conflict also diverted public resources from infrastructure and the social sectors to military expenditures, and led to large migration—about one million people (20 percent of the population) migrated to the U.S. and now provide significant worker remittances.

A. The Structural Adjustment Program: Design and Objectives

2. After assuming office in June 1989, President Cristiani's Government set forth three primary goals: to end the civil war; re-introduce market discipline into the economy; and initiate a systematic attack on poverty. The Government introduced a far-reaching economic reform program emphasizing the reactivation of growth and the reduction of absolute poverty as its top economic priorities, while initiating negotiations with the Farabundo Marti National Liberation Front which subsequently resulted in the signing of a peace agreement in 1992, thus ending the decade-long civil conflict.

3. **SAL I** was designed to support the Government's 1989-94 economic reform program. The objectives of the program were to: (i) improve incentives to stimulate savings and investment in more efficient export oriented and import-substituting activities; (ii) increase tax enforcement capacity; (iii) improve the efficiency of financial intermediation; (iv) improve agricultural productivity; and (v) prevent a deterioration in the nutritional status of the poor during adjustment. The Government's strong commitment to reforms contributed to the successful outcome of SAL I.

4. **SAL II** aimed to continue supporting the Government's Structural Adjustment Program, which was designed to: (i) lay the analytical framework for a comprehensive public sector modernization effort; (ii) consolidate and deepen reforms supported by SAL I in taxation, privatization, trade, the financial sector, and social sectors and poverty alleviation; and (iii) promote actions to strengthen public expenditure, civil service, and environmental management, and restructure the hydrocarbon sector. The principal components were:

Public Sector Modernization. Prior to Board presentation, the Government prepared a comprehensive public sector modernization assessment, and initiated work toward the preparation of an Action Plan to implement a public sector modernization program (PSMAP), completion of which was defined as a second tranche condition.

Public Expenditure Management. Actions under SAL II would include: (i) budget unification; (ii) introduction of a new accounting system; (iii) implementation of the Integrated Financial Management (IFM) project involving budgeting, accounting, treasury, and procurement policies and procedures; (iv) implementation of new rules permitting advance spending authorizations (DAFP); (v) restructuring of the role of the Government Auditor (*Corte de Cuentas*) to that of an independent ex-post auditor; and (vi) development of a medium-term expenditure planning function under MIFIN and MIPLAN.

Civil Service Reform. The main focus under SAL II was to implement a Human Resources Information System (HRIS), and subsequently, to prepare a comprehensive human resources plan as part of the PSMAP.

Tax Reform. The program contained two major tax reform components. The first called for the Government to expand the tax base, and to enhance revenues through a series of agreed tax

measures. Actions included expansion of the VAT base, including the removal of tax exemptions. The second component dealt with tax and customs administration for which a separate policy matrix was developed.

Privatization. SAL II supported further actions initiated under SAL I, including offering for sale BFA's productive assets, the *San Bartolo* free trade zone, BANAFI's *Cemento Maya*, INCAFE's warehouses and processing plants, INAZUCAR sugar mills, and BANAFI/CORSAIN assets.

Financial sector reform. The SAL II targets were to maintain a market-based interest rate regime; to complete the privatization of banks and finance companies; to promote capital market development; and to reformulate the rural credit delivery system.

Hydrocarbon sector. The Government was to elaborate and initiate implementation of an action plan for reform of the hydrocarbon sector, including the design of an alternative system to protect low income consumers of diesel for public transportation and LPG, and finalization of a draft Hydrocarbons Law.

Trade reform. The Government was to take steps to further reduce tariff levels and their dispersion, to eliminate remaining NTBs, and to improve export incentives.

Social sector reform. The Government was to develop: (i) an evaluation of the main programs managed by the Social Investment Fund (FIS) and the National Secretariat for Reconstruction (SRN/CONARA); and (ii) a monitoring system to measure living standards.

Environmental policy. The Government was to prepare an Environmental Action Plan with input from CONAMA. In addition, the Government was to submit to Congress a draft of a comprehensive Environmental Law.

5. **Technical Assistance Loan**. Because SAL II involved the preparation of numerous studies, policy analysis, as well as the development of action plans, the Bank prepared a complementary Technical Assistance Loan (TAL). The TAL, however, was designed to go beyond SAL II, not only to strengthen the Government's capacity to design and implement policy reforms supported by the Loan, but also to assist in the preparation of further restructuring actions, within the framework of a longer-term public sector modernization effort.[1]

6. **Evaluation of Loan Objectives.** SAL II sought to maintain or continue those reforms initiated under the previous loan, and to expand policy reforms notably in the area of public sector modernization. The central theme was consolidation and continuity: to allow the Government to lock-in and to deepen reforms in the financial, trade, tax, and social sectors. Initially, the Bank considered disbursing the Loan in three tranches in order to involve the subsequent Government in the policy dialogue around third tranche conditions. However, it was finally decided to shorten the Loan to two tranches, so that it would coincide with the Cristiani Administration, and if appropriate, to negotiate a follow-up operation with the subsequent Government. In the event, second tranche was disbursed with the next Administration.

7. The successful implementation of SAL I facilitated the appraisal and negotiation of SAL II. The Loan was relatively well-balanced in terms of the type of conditionality. About half of the measures contained in the policy matrix called for specific action steps, which was consistent with the aim of supporting tangible economic reforms. The relatively high number of plans and studies called for by the Loan dealt mostly with public sector modernization, where the goal of the SAL II program was to first develop the analytical framework that would subsequently support the implementation of modernization

[1] The closing date for the TAL is June 30, 1996. For more discussion see *President's Report: Technical Assistance Project*, Report No. P-6126-ES, August 17, 1993.

strategies. The macroeconomic framework was specified in conjunction with an IMF-sponsored stabilization program aimed at reducing inflation and strengthening the country's international liquidity position. Just prior to Board presentation, the IMF had reported that the Government had made satisfactory progress with the program, and this performance was expected to continue.

8. **Public Sector Modernization.** The design of the public sector modernization component was comprehensive and called for inputs from numerous consultants in the form of studies and development of action plans. Modernization of the public sector had been part of President Cristiani's agenda, although it did not get off the ground until the second year of the Administration, and only after the Peace negotiations and reconstruction process had been set in motion. The scope of the program was somewhat ambitious in terms of the number of areas involved in the reform agenda which thus required crossing many institutional lines. Due to the complex structure of the public sector modernization program, its design accordingly called for extensive coordination of various work groups involved in public expenditure management, in tax and customs reforms, and in civil service reforms, while at the same time assuring compatibility with similar programs supported by other donors.

9. The specification of policy actions dealing with public sector modernization was realistic. The appraisal had appropriately identified the need to revamp the budgeting, treasury, accounting, and information systems in order to enhance the efficiency of public sector decisions. From an organizational perspective, the specification of a separate tax and customs administration policy matrix in SAL II was very helpful in separating the administrative aspects of public sector reforms from the other structural and policy requirements.

10. **Financial Sector Reform.** The financial sector conditionality was basically a continuation of work started in SAL I, which dealt with the privatization of commercial banks and the maintenance of market-determined interest rates. The agenda was expanded to include conditions dealing with the development of the capital market and reform of the rural credit delivery system. Support to strengthen prudential supervision of the financial system, a critical element of financial sector reform programs, was being provided by the IMF and IDB.[2]

11. The requirement of a rural credit delivery system study for Board Presentation was appropriate, but perhaps it could have gone further in calling for agreement on an action plan. In August 1993, the Bank was already familiar with three conflicting proposals/studies regarding rural credit delivery. The Government at that time was not clear on its own position regarding financial strategies for the rural sector. Although the Bank could have pressed for more specific reform actions, given the lack of clarity within Government, on balance the decision to focus on the preparation of a study to help the Government develop its own strategy appears appropriate.

12. Policy reforms in the **hydrocarbon sector** were necessary to correct serious distortions in the energy sector. Since another project was being designed for public utilities and the energy sector in general, the Bank appropriately excluded the public utilities from the conditionality.[3] **Trade reforms** were a continuation of SAL I which had already addressed most of the necessary changes in the tariff regime. Only minor tariff adjustments and reductions in NTBs were included in SAL II.

13. Conditionality on the **social sectors** and poverty alleviation dealt mostly with the evaluation of existing compensatory programs, and the preparation of an action plan to improve aid coordination and develop a mechanism to monitor the impact of these programs on poverty alleviation. The design of an action plan was very relevant to the process of reducing chronic poverty; in addition, a broader social program, as part of a separate social sector rehabilitation loan was being implemented at the time of loan

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[2] See IDB, *El Salvador: Investment Sector Reform Program*, ES-0016, October 1992.

[3] See *El Salvador: Energy Sector Modernization*, Report No. 12528-ES, February 1995.

appraisal.[4] The **environment policy** component of SAL II was relatively general since other donors, especially USAID and IDB, were actively supporting concrete programs to improve environmental management. Thus, SAL II aimed only to provide additional support to improve the overall environmental policy framework, leaving specific actions and programs to other donors.

B. Achievement of Program Objectives

14. SAL II supported an ambitious and comprehensive reform program. Second tranche conditionality covered 23 major areas, many of which included several sub-conditions. There was full compliance with actions required in all but two of these areas (there was partial compliance with the privatization of the sugar mills and reform of the hydrocarbon sector). The overall outcome of SAL II has been very positive. The success of the program, and the strong support it has received from the new Administration, bode well for its sustainability. This section highlights the principal issues concerning the outcome of the reform program. Details on the status of legal covenants regarding compliance of individual components is provided in Part II, Table 7.

15. **Macroeconomic Framework.** The objective of maintaining an appropriate macroeconomic environment was met. These achievements were significant in view of the change in Government. In March 1994, general elections were held and the new President, Dr. Armando Calderón Sol took office on June 1, 1994. The new Administration pledged to continue efforts to consolidate peace, maintain macroeconomic stability, and deepen the structural reform process initiated by the previous Government.[5] The reform program of the current Government has as its centerpiece the comprehensive modernization of the public sector and an ambitious effort to globalize El Salvador's economy.

16. Growth and stabilization objectives were met, and exceeded in some cases. A strong recovery, triggered by peace and the reforms supported by SAL I and II, led to accelerated growth. Over the past four years, GDP growth averaged 6.8 percent, far exceeding the Bank's projection of 4.3 percent. Inflation fell from an average of 22.2 percent during 1986-90 to 8.9 percent in 1994—it rose somewhat to 11.4 percent in 1995, due in part to an increase in the VAT rate (from 10 to 13 percent) and sharp increases in public utility rates. In the external sector, the current account deficit (excluding official grants) declined steadily, although the trade deficit doubled in the past five years. After two years of stagnation, exports grew strongly over the past three years, averaging 23 percent, although with considerable variability. Import growth was more steady, averaging about 16 percent over the past five years. The larger trade deficit has been largely financed by increasing remittances. However, to the extent that remittances go mostly to consumption expenditures, and the latter have a high import content, then the trade deficit is in turn pushed up by the remittances. Moreover, as the colón has remained nominally fixed to the dollar, it has continued to appreciate in real terms, and thus penalizes exports.

17. Overall fiscal performance in 1994 was significantly better than programmed. The Bank had expected a much more gradual reduction in the fiscal deficit. From a peak of 6.7 percent of GDP in 1992, it fell rapidly to 1.6 in 1995, in line with IMF targets. Public savings, targeted to double to 1.5 percent of GDP in 1994, actually increased to 1.9 percent as a result of higher tax revenues.

18. On May 10, 1993, the IMF Board approved a 10 month Stand-By Arrangement, which was subsequently extended through end-1994. On October 14, 1994, the Article IV consultations and the mid-term review of the 1994 program were completed. The mid-term review concluded that all performance criteria as of end-May 1994 were observed. During the first part of 1995 the IMF negotiated a new Stand-By, which was approved in July. The mid-term review indicated all performance criteria were

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[4] See *El Salvador: Social Sector Rehabilitation Project (Loan 3348-ES)*, approved in 1992.

[5] For more discussion see the Bank's CEM: *EL Salvador: Meeting the Challenge of Globalization*, Report No. 14109-ES, October 1995.

observed, although the mission noted a need to tighten financial policies for 1996.

19. **Public Sector Modernization.** The objective of public sector modernization as established in SAL II was met. The PSMAP, finalized in September 1994,[6] is a mission statement for the modernization of the public sector at all levels of Government. One of the key benefits of this planning exercise has been the ability to articulate a comprehensive public sector vision, which provides a longer-term framework for coordinating the various donor activities involved in public sector modernization. The principal areas in the PSMAP are: (i) decentralization; (ii) privatization; (iii) regulatory reforms; (iv) development of human resources; (v) procurement policies; (vi) consolidation of management information systems; and (vii) strengthening of internal control and auditing. A September 1995 Bank mission reported satisfactory progress in the implementation of the PSMAP. This section reviews the specific public sector modernization actions that were part of SAL II, and then summarizes the recent implementation experience as it pertains to some of the other principal areas of the PSMAP.

20. **Public expenditure management**. Performance of this component should be reviewed from two perspectives: (i) implementation of the Integrated Financial Management Project (IFM); and (ii) development of a new unified budget structure and a medium-term sectoral budget for selected ministries. Achievement of objectives under the IFM was satisfactory. With respect to IFM, the Government's goal is to decentralize the process of financial control at the central (MIFIN), institutional and department levels. There are three functional areas under the IFM: (i) accounting; (ii) budgeting, which was organized under a new concept of management units, versus the previous budgeting system by individual programs; and (iii) treasury, which was designed as a decentralized payments system. The Government has developed the necessary policies and procedures, and the system has begun implementation.[7]

21. The enhancement to the general accounting framework was satisfactory. Some weakness was noted in the implementation of the Advance Global Spending Authorizations (DAFPs) which was a Board Presentation condition. While this condition was complied with, it appears that each entity is using the DAFP according to its own criteria, and not necessarily according to the standard procedures established by the new regulations.

22. The 1996 budget was prepared under the IFM's new system of management units. In addition, the National Budget Office initiated a training program for 2,000 representatives from ministries and agencies on the new budgeting methodology. Given the novelty and complexity of the new budgeting system, it is reasonable to expect that full implementation will likely take several years.

23. The integrity of the IFM system will hinge on the competency of internal control mechanisms. For this purpose, the public expenditure management component of the program called for the reform of the Court of Accounts, which is the Government's internal auditor. Recently the Congress approved a law to reform the Court of Accounts by eliminating its role in ex-ante control, limiting its activities to ex-post expenditure control. Nevertheless, the Court of Accounts needs to undergo additional organizational changes to enhance its auditing capabilities.

24. The development of a unified budget structure should enhance the planning capabilities of the Government. The medium-term budget preparation was completed for three government entities. A medium-term sectoral budget for the Ministry of Education was completed in September 1994, including a new program classification, a new unified budget structure for 1992-94, and the design of a medium-

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[6] See Ministry of Planning, *Programa de Modernización del Sector Público*, November 1994.

[7] See the following manuals developed by MIFIN: *Manual de Programación de la Ejecución Presupuestaria*, date N/A; *Enfoque Presupuestario: Por Areas de Gestión del Sector Público*, October 1993; *Manual de Clasificación para las Transacciones Financieras del Sector Público No Financiero*, January 1995; *Instrumentos Técnicos para Elaborar el Presupuesto Por Areas de Gestión*, date N/A.

term budget for 1994-96. Similar work was completed for the Vice-Ministry of Housing and MSPAS.

25. Civil service reform objectives in SAL II were achieved. Implementation of the TAL-financed HRIS is proceeding in a satisfactory manner and in accordance with the agreed timetables. The Government has shown a strong commitment to this effort. A central HRIS unit in MIFIN has successfully implemented a pilot local system in the Ministries of Finance and Agriculture. The objectives of the HRIS are to: (i) complete a centralized and detailed data base on public sector personnel; (ii) implement the HRIS system in all entities, through the creation of a personnel department; (iii) establish a uniform job classification, which would evolve from a new Civil Service Law; and (iv) develop a payroll function within each localized unit. During the initial phase, the principal goal has been to develop a personnel data base. While much progress has been made in the construction of a data base, the sheer size of the public sector work force relative to the limited resources of the HRIS unit suggests that attaining adequate coverage will take longer than originally expected. The planned Public Sector Modernization Loan contains a component to conclude work on the establishment of the HRIS.

26. The HRIS unit has encountered some difficulties in obtaining information, particularly in the Ministry of Education which has the largest payroll (about 38,000). Some of the Ministries have voiced concern about sharing their personnel data with the HRIS unit. This may point to the need for additional efforts in communicating the goals of the project to the Ministries, and in explaining the potential efficiency gains that they could obtain by applying the HRIS information to their personnel management function. Progress has also been made in setting up a limited number of local HRIS units within selected Government entities, but the development of a full fledged personnel department will require extensive planning, restructuring, and training within each of the entities.

27. The objectives dealing with **tax reform**, which emphasized tax and customs administration, have been met as specified in the policy matrix, although the implementation of a new automated customs procedure encountered some delays. The main objectives were to achieve improvements in tax administration, enforce compliance, and reduce evasion through the implementation of a tax and customs administration reform program. In tax administration the achievements included: (i) an increase in the efficiency of collection by restructuring units in the internal revenue service (DGII); (ii) coordination of evasion and smuggling control programs by DGII and Customs; and (iii) improved coordination of technical assistance under the Vice-Minister of Finance. In customs administration, actions included: (i) simplifying and streamlining customs procedures; and (ii) approval by the Assembly of two pieces of legislation aimed at enhancing revenue collection and simplifying administrative procedures.

28. Tax revenues as a percent of GDP increased from 8.5 percent in 1991, to 12.0 percent in 1995, almost exactly in line with Bank projections. This has resulted from the success of the tax reform program combined with improved economic conditions. In the area of compliance, the Government has built a register of about 44,000 VAT contributors, prepared an ownership tree for a selected sample of corporations and individuals, and some attempts are being made to cross reference tax information electronically. However, customs reforms have not gone as well as expected, in part due to weak commitment from the customs administration. The automated customs control system (SIDUNEA) was set up in 1992, but is not yet operational.

29. The **privatization** objectives of the Government were largely met. The Government demonstrated its commitment to sell the assets of INCAFE, CORSAIN, and BANAFI as established in the Loan Agreement. In all cases, except the sugar mills, this has been done by publishing the offers for sale in major national newspapers. The recent Government decision to liquidate BANAFI has temporarily delayed the privatization of the fisheries complex and the remaining portion (30 percent) of the *San Bartolo* Free Zone which were part of BANAFI's portfolio. At the time of this report, it was believed that these remaining assets would be transferred to CORSAIN which would then assume responsibility for their sale.

30. In the case of sugar mill privatization, SAL II supported the offering for sale of at least one sugar mill and the completion of preparatory work for the privatization of the remaining five. The Government, however, followed a slightly different privatization strategy than originally contemplated in the program. A law to privatize sugar mills and alcohol plants was approved by the Assembly in August 1994, providing for a staged and fully transparent process for sale of the six mills. Although none of the mills actually reached the point of sale during SAL II implementation, all six had been approved for sale by the new law at the time of second tranche disbursement. The Bank considered that through this process the Government exceeded the original expectations of the Loan and therefore recommended approval of a partial waiver on the privatization of at least one sugar mill. In the event, one mill was sold in early 1995 and another was offered for sale in November 1995.

31. Progress is being made on implementation of **other PSMAP strategies.** Although they go beyond the conditions in SAL II, they are mentioned because of their relevance to the sustainability of public sector reforms. A mandatory employment reduction program was approved by the Assembly in November 1995, which will result in the elimination in early 1996 of about 15,000 positions (about 11 percent of employment in the public sector). Decentralization strategies are still fragmented, although key steps have been taken at the sectoral level such as EDUCO within the Ministry of Education. A recent reorganization of the FIS has led to the creation of a unit to promote local community development as part of the decentralization strategy. With respect to privatization, progress has been slower than initially announced by the new Administration, but important steps are expected in 1996. Legislation to establish a framework allowing the privatization of the electricity company will be presented to the Assembly in early 1996; draft legislation that would allow the operation of private pension fund managers will also be presented to the Assembly in the first half of 1996; and a bill to establish a single regulatory agency for all public utilities will be ready by June 1996. In November 1995, a private power plant (96 MW) started operations. Implementation of the PSMAP will be supported through the proposed Public Sector Modernization Loan.

32. **Financial Sector Reform.** SAL II's financial sector reform objectives were met as specified in the program. Actions taken by the Government included: (i) maintenance of market-determined interest rates; (ii) privatization of the remaining banks; (iii) preparation and implementation of an action plan for rural credit; (iv) development of the capital market; and (v) improved supervision of the financial system.

33. Interest rate liberalization began in 1991, with quarterly adjustments to interest rates according to a pre-specified formula based on prior inflation rates. By March 1992, the Government had liberalized all domestic interest rates, one year in advance of the commitment under SAL I. Positive real, or inflation adjusted, interest rates have stimulated savings in the banking system.

34. Between December 1990 and April 1991, the Government approved several laws dealing with the restructuring of the banking system. The legislation set the stage for first reviving and then privatizing the banks. It also strengthened standards with respect to the safety and soundness of the financial system. The Government began to privatize the banks in 1991 with support from SAL I, this process was completed as part of SAL II. In February 1995, the final bank, *Banco Hipotecario* was offered for sale.

35. While it may be too soon to make a judgement on the success of privatization, recent financial trends indicate that the banking system appears to have benefitted from restructuring and privatization. With the exception of 1991, when the banking system incurred a sizeable loss due to the loan portfolio restructuring, the banks' return on equity has averaged a steady 19.5 percent during 1992-94. In real terms, after adjusting by the average inflation during the same period, return on equity was 5.6 percent. In addition to the improvement in interest margins, the positive earnings performance can be attributed to: (i) better control over operating expenses; and (ii) improved asset quality. At the same time, the economic recovery has reduced the risk of losses on non-performing assets.

36. Banks interviewed for this report confirm a closer scrutiny of the loan portfolio on the part of the Superintendency. In addition, the Government has taken further steps to strengthen the financial system. In February 1995, the Assembly approved modifications to the securities law and is considering modifications to the Banking Law. The latter are designed to strengthen the regulatory framework by, *inter alia*, raising the capital assets ratio (from 8 to 10 percent over six years), increasing minimum capital requirements and raising penalties for non-compliance.

37. The Central Bank adopted a reform plan to improve and expand rural financial markets on May 17, 1994; and the plan was reconfirmed by the new Administration in October 1994. Actions taken to date include: (i) a proposal to reform the Rural Credit Bureaus that would decentralize their operations; (ii) creation of a creditworthiness data base within the Superintendency to lower transaction costs by allowing greater use of "character" lending; and (iii) development of training programs to foster sustainable agricultural practices. The Action Plan also identifies the target markets for BFA and FEDECREDITO, but further steps will be necessary to clarify implementation details, especially in terms of funding sources and depository base.

38. SAL II's contribution to capital markets development focused on the passage of the Capital Markets Law in 1994. Prior to 1992, El Salvador had no formal capital market. This situation changed as a result of the Government's reform program initiated in 1990. The Securities Exchange (*Bolsa*) was created in February 1992. The first public trading of shares of stock at the *Bolsa* occurred with the auction of the privatized banks' shares. A considerable strengthening of the Superintendency will be required to ensure sustainability of the financial sector reforms, especially in areas such as capital markets, where its responsibilities and the complexity of supervision have expanded.

39. **Hydrocarbon Sector.** Four of the five actions required for satisfactory progress in the implementation of the comprehensive action plan to reform the hydrocarbons sector were taken: (i) the draft Hydrocarbons Law was submitted to the Assembly in November 1994; (ii) a Bank-financed study on standards and technical specifications for petroleum and its derivatives was completed; (iii) a system based on import parity pricing was implemented; and (iv) a study analyzing alternative systems of LPG subsidy was completed. The fifth action, to put into effect a revised diesel pricing system, was only partially carried out. Diesel price distortions to the general public have been eliminated except for public transport bus owners. The price liberalization measures have so far produced a 46 percent reduction in the cost of the diesel subsidy. These positive results were considered sufficient to grant a partial waiver to this condition for the second tranche release. The Energy Sector Modernization Loan approved by the Board in July 1995 should help to resolve these market distortions.

40. **Trade Reform.** Objectives in the area of trade reform were met. A draft decree was submitted which would bring all tariff codes in Part III of the Central American Tariff Code within the 5-20 percent range, although this was delayed by the change in Government. In addition, several decrees and laws were modified in order to eliminate non-tariff barriers (NTBs) from food and drug regulations. As part of its globalization strategy, the Government recently approved a further reduction in the tariff on capital goods from 5 to 1 percent and plans further steps in 1996—staring July 1996, tariffs on consumer goods will be reduced from 20 to 15 percent by end-1996, on raw materials from 5 percent to zero, and on capital goods from 1 percent to zero. The aim is to achieve an overall tariff ceiling of 6 percent by 1999. Clearly these actions go much beyond the original objectives of SAL II. Their implementation will depend critically on the Government's ability to mobilize additional offsetting revenues.

41. **Social Sectors and Poverty Alleviation.** The Government undertook to develop its Poverty Alleviation Strategy and Action Plan by evaluating: (i) compensatory programs managed by the Social Investment Fund (FIS) and the National Reconstruction Secretariat (SRN/CONARA); (ii) training and productive support programs; and (iii) social services managed by the Ministries of Education and Health. The Government initiated implementation of the Poverty Alleviation Action Plan for 1994-98 with the goal of increasing the quantity, quality, and efficiency of social services. This is being achieved by: (i)

increased budget allocations for the social sectors in the 1995 and 1996 budgets; and (ii) establishing task forces for the education and health sectors to spearhead the reforms included in the Plan. FIS expanded its investment program by 22 percent in 1995. For 1996, the Government plans to merge into a National Development Fund, three existing social programs: FIS, Municipalities in Action and SRN.

42. The Government initiated a program to decentralize school management at the community level, supported by the Bank through a Social Sector Rehabilitation Project (Loan 3348-ES). This new educational program is based on community-managed schools which receive their funding directly from the Ministry of Education, but actual spending decisions are made at the local level. The impact of the EDUCO program has been very positive, especially in increasing enrollments in poor rural areas.[8]

43. **Environmental Policy.** The Environmental Action Plan was approved by CONAMA in April 1994, and a draft Environmental Law was submitted to the Assembly in May 1994. The Plan, which contains a series of institutional and regulatory reforms, is now being implemented. However, organizational changes in SEMA introduced by a new administration in 1994 produced a significant outflow of technical personnel. This gave rise to significant delays in the implementation of the Plan. The Assembly is currently considering the Government's environmental strategy, which includes an environmental impact analysis for all projects and public works and a plan for environmental education.

C. Bank Performance

44. Bank performance was **highly satisfactory**. From the start, the Bank's staff played a pro-active role in supporting the Government's own reform initiatives. The analysis of the economic problems and the prognosis of needed action steps, performed by the Bank, were both in-depth and of a high degree of accuracy. The staff's prior experience with SAL I facilitated the identification and appraisal process. The staff was also helpful in maintaining a productive ongoing dialogue with key Government officials involved in the preparation and implementation of the Loan.

45. Supervision of program performance was highly satisfactory. Once again, the experience of SAL I was instrumental in facilitating supervision of SAL II, since the strengths and weaknesses of the borrower were already identified. Continuity of Bank staff was an essential ingredient in the successful monitoring of the program. The frequency of missions was adequate in view of the implementing agency's high technical capacity in dealing with a complex adjustment program.

46. One of the strengths of Bank performance was a high degree of organization in the design and implementation of the Loan as exemplified by the following: (i) in designing the second tranche conditions, the bulk of the program's policy matrix was explicitly incorporated into the text of the Loan Agreement, which minimized the possibility of misunderstandings; and (ii) in supervising the Loan, the staff made an extensive compilation of relevant documentation on Loan compliance which was easily accessible.

47. The staff responded quickly in resolving a problem with the loan's disbursement procedure. Due to the Government's cash-flow needs, it was imperative to obtain full tranche release upon effectiveness. Because the process of import verification is time-consuming and cumbersome, an exception to the 20 percent limit on retroactive financing was granted. The decision to increase the amount of retroactive financing was in line with the aim of providing essential balance of payments support.

D. Borrower Performance

48. Borrower performance was **highly satisfactory**. One of the principal factors for the success of

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[8] See *El Salvador: Community Education Strategy: Decentralized School Management*, World Bank, Report No. 13502-ES, December 1994.

the loan was the Government's high degree of commitment to the program. The Borrower remains committed to the adjustment effort, and has requested Bank assistance for a comprehensive public sector modernization project which is currently under preparation. One of the main reasons for the highly satisfactory outcome was the continuity of senior administration officials involved in the implementation of the Loan. Borrower compliance was very strong, which is an indication of borrower ownership of conditionality.

49. The agency in charge of program implementation in the Ministry of Planning (MIPLAN: GAES) was very effective, and its staff was characterized by a high level of technical expertise. One of the salient characteristics of GAES's performance was the continuity in the staff directly involved in the Loan's implementation. Key agency personnel were associated with both SAL I and SAL II, and they have remained in critical policy positions despite the phasing out of GAES under the new Government.

E. Assessment and Conclusions

50. **Program Sustainability.** The sustainability of the reform program supported by SAL II is **highly likely**. The risk of policy reversals is minimal and the current Government has continued to deepen the structural adjustment process, with a view to fostering the globalization of El Salvador's economy and furthering public sector reforms. The Bank is supporting the next phase of reforms through technical assistance.

51. Although progress has been substantial and economic prospects are favorable, a considerable stabilization and adjustment agenda remains. In addition to the need to complete the public sector modernization program and improve conditions for private sector development, key aspects of the remaining agenda include: (i) further efforts to consolidate the peace process by ensuring that the benefits of growth are more equally shared; (ii) improved policies in the agriculture sector, especially to support growth of small-scale producers; (iii) strengthening the human capital base, especially basic education; (iv) expanding and diversifying the export base, to reduce external vulnerability and dependence on short-term capital flows and remittances; (v) further strengthening of the tax base, to improve fiscal policies and finance increased investment in the social sectors and poverty alleviation programs; and (vi) continued improvements in environmental management and policies.

52. **Overall Assessment.** The program supported by SAL II has been very successful. The achievement of the Loan's objectives is considered as **substantial**. Both the Borrower and the Bank's performance are classified as **highly satisfactory**. Thus, the overall outcome of the Loan is rated as **highly satisfactory**[9]. The success of this Loan can be attributed in large part to the strong commitment shown by both the previous and the current Governments. While the loan was made effective during the Administration of President Cristiani, his successor, President Calderón Sol, has continued to support the reform program. The good track record of the Government during SAL I was easily maintained during SAL II. The macroeconomic framework has been appropriate and the Government has complied with IMF programs, although some concerns remain regarding the real appreciation of the exchange rate, and its negative impact on the development of exports. The sequencing of reforms was well managed. For example, public sector modernization initiatives in SAL II followed the stabilization program started in SAL I. Development of the capital markets was initiated after the banking sector had shown significant improvement through the privatization program.

53. **Specific Findings and Lessons Learned.** The main conclusions and lessons learned are:

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[9] The cofinancier, KfW, fully agrees that the outcome of SAL II has been very successful. In a letter to the Bank (February 9, 1996) KfW states: "Nearly all economic indicators have improved and in many cases this improvement has been even better than projected at the time of designing the program. We consider it worth mentioning that this development has been achieved despite the fact of the change in Government which took place during implementation of the program. We share your view that sustainability of the program is very likely."

- As in any adjustment program, Borrower ownership is critical. Because of the Government's strong commitment to the reforms supported by SAL II, the negotiation and implementation of the program was achieved in an environment of mutual confidence.

- A change in government during the implementation of a program inevitably leads to some delay in compliance. The views of a new administration regarding the reform agenda may differ with those of its predecessor. For this reason it is important to accentuate the use of first tranche conditionality whenever approaching an electoral year. SAL II was not designed in this manner, since the Bank originally expected that implementation would be completed within a single administration. In the event, the Loan period did extend beyond the life of one administration. However, because of the strong commitment of the incoming Government to continue the reforms, the change in administration did not prove to be a problem in this case.

- The success of one structural adjustment operation is likely to be repeated in a follow-on operation if: (i) sequencing is appropriate; and (ii) there is continuity in the staff, both in the Government and in the Bank, working on both operations.

- The financial sector is highly vulnerable to structural economic changes, requiring a gradual and careful sequencing of reforms. In the case of El Salvador, banking sector reforms were well sequenced and gradual (restructuring, capitalization, and privatization of the banks, accompanied by actions to reinforce the Superintendency).

- It is essential to ensure Borrower consensus on the reform agenda at the time of appraisal. The communication of program goals and objectives to all affected entities in and out of the government is important in gaining the necessary support for its successful implementation. In this sense, the careful preparation of detailed action plans, and the intensive coordination of studies and consultant inputs, played an important role in communicating to the affected institutions the rationale and steps involved in the reform.

PART II: STATISTICAL TABLES

Table 1: SUMMARY OF ASSESSMENTS

A. Achievement of Objectives	Substantial	Partial	Negligible	N/A
Macroeconomic Policies	✓	—	—	—
Sector policies	✓	—	—	—
Financial objectives	✓	—	—	—
Institutional development	✓	—	—	—
Physical objectives	—	—	—	✓
Poverty reduction	—	—	—	✓
Gender concerns	—	—	—	✓
Other social objectives	✓	—	—	—
Environmental objectives	✓	—	—	—
Public sector management	✓	—	—	—
Private sector development	✓	—	—	—

B. Program Sustainability	Likely	Unlikely	Uncertain
	✓	—	—

C. Bank Performance	Highly Satisfactory	Satisfactory	Deficient
Identification	✓	—	—
Preparation assistance	✓	—	—
Appraisal	✓	—	—
Supervision	✓	—	—

D. Borrower Performance	Highly Satisfactory	Satisfactory	Deficient
Preparation	✓	—	—
Implementation	✓	—	—
Covenant Compliance	—	✓	—

E. Assessment of Outcome	Highly Satisfactory	Satisfactory	Unsatisfactory	Highly Unsatisfactory
	✓	—	—	—

Table 2: RELATED BANK LOANS

Loan/Credit Title	Purpose	Fiscal Year Approved	Status
Preceding Operations			
Structural Adjustment Loan (Loan 3293-ES)	Support Government reform program.	1991	Closed December 1992
Social Sector Rehabilitation Project (Loan 3348-ES)	Improve delivery of social services in poorest municipalities	1992	Under implementation
Agricultural Sector Reform (Loan 3576-ES)	Institutional strengthening in agriculture and improved research and extension focused on small farmers.	1993	Under implementation
Parallel Operation			
Technical Assistance Loan (Loan 3648-ES)	Strengthen Government capacity to design and implement policy reforms.	1993	Under implementation
Following Operations:			
Energy Sector Modernization Loan (Loan 3920-ES)	Modernization and expansion of power supply, pricing and regulatory reform.	1996	Under implementation
Public Sector Modernization Project	Support public sector modernization program, continuing reforms in SAL II.		In preparation
Competitiveness Enhancement Loan (Loan 3946-ES)	Support the business environment and the Government's globalization strategy.	1996	Under implementation

Table 3: PROJECT TIMETABLE

Steps in the Project Cycle	Date Planned	Date Actual
Identification	May 1992	May 1992
Preparation	October 1993	October 1992
Appraisal	April 1993	June 1993
Negotiations	May 1992	July 1993
Letter of Development Policy	June 1993	August 1993
Board Presentation	August 1993	September 1993
Signing	September 1993	October 1993
Effectiveness	October 1994	December 1993
First Tranche Release	November 1994	February 1994
Second Tranche Release	June 1994	January 1995
Loan Closing	December 1994	December 1994

Table 4: LOAN DISBURSEMENTS

	FY94	FY95
Appraisal Estimate (US$m)	50.0	--
Actual (US$m)	30.0 (1st Tranche)	20.0 (2nd Tranche)
Cumulative (US$m)	30.0	50.0
Date of Tranche Disbursements	February 18, 1994 (1st)	January 11, 1995 (2nd)

Table 5: KEY INDICATORS, ACTUALS AND PROJECTED, 1986-95
(% unless otherwise indicated)

	Actuals						Bank Projections[1]		
	1986-90	1991	1992	1993	1994	1995	1993	1994	1995
GDP Growth	2.1	3.6	7.5	7.4	6.0	6.3	4.3	4.3	4.3
Inflation (end-year)	22.2	9.8	20.0	12.1	8.9	11.4	12.0	9.9	7.2
Investment/GDP	13.5	15.4	18.5	18.6	18.8	19.7	16.2	18.2	18.2
of which: Private	10.0	12.6	14.5	14.6	15.0	15.7	12.9	14.1	14.2
Fiscal Balance (before grants)/GDP	-3.4	-4.4	-6.7	-3.6	-2.0	-1.6	-6.2	-5.4	-2.9
Tax Revenues/GDP	9.8	8.5	9.6	10.3	10.8	12.0	9.1	10.5	12.0
Export Growth (US$)	-22.9	1.0	1.7	24.1	10.2	35.2	14.2	9.7	12.2
Import Growth (US$)	35.0	11.4	20.8	13.3	17.0	15.4	7.8	6.2	6.6
Current Account Balance (bef grants) /GDP	-5.9	-5.0	-5.7	-4.3	-3.7	-2.8	-5.6	-5.4	-4.9
Reserves (months of imports)	3.2	3.8	3.5	4.0	4.2	4.5	--	--	--

[1] Projections are from the SAL II President's Report.

Table 6: STUDIES INCLUDED IN THE LOAN

Study	Purpose	Status
1.Public sector modernization assessment	Support of PSMAP	Per policy matrix, Board Presentation: Completed
2. Prepare pilot review of three ministries	Support of PSMAP	Per policy matrix, Board Presentation: Completed
3.Identify the unified budget structure and format	Support budget unification efforts	Per policy matrix, 2nd tranche: Completed
4. Initiate comprehensive review of tax system	Background information for tax policy	Per policy matrix, Board Presentation: Initiated
5. Complete review of tax system, including a tax reform agenda for the next administration	Background information for tax policy	Per policy matrix, 2nd tranche: substantially completed
6. Evaluate tax audits, based on cross-section sample	Assist in strengthening tax enforcement	Per policy matrix, 2nd tranche: substantially completed
7. Present analysis of the results of enforcing the Ley del Delito Fiscal	Assist in strengthening of tax enforcement	Per policy matrix, 2nd tranche: partially completed
8. Prepare a diagnosis of DGA and custom's current structure	Assist in strengthening of tax enforcement	Per policy matrix, Board presentation: completed
9. Complete analysis of achievements/failures of technical assistance projects	Assist in strengthening of tax enforcement	Per policy matrix, 2nd tranche: substantially completed
10. Complete rural credit delivery system study	Assist in development of rural credit action plan	Per policy matrix, Board presentation: completed
11. Initiated review of the current duty drawback system	Assist in development of export promotion strategy	Per policy matrix, Board presentation: substantially completed

Table 7: STATUS OF LEGAL COVENANTS

Loan agreement section	Description of covenant	Comments
Schedule 4, No.1	Borrower shall have prepared the Public Sector Modernization Action Plan	PSMAP completed; in process of implementation.
Schedule 4, No.2	Borrower shall have submitted to the Legislative Assembly the Draft Budget Law.	IFM law submitted in November 1994.
Schedule 4, No.3	Borrower shall have submitted to the Legislative Assembly the Draft Treasury Law.	Covered under IFM law, 1996 budget presented under new system.
Schedule 4, No.4	Borrower shall have commenced the application of the Government Accounting System in all the public sector entities listed in its letter to the Bank dated July 7, 1993.	By June 1994 GAS was applied to all NFPS agencies.
Schedule 4, No.5	Borrower shall have completed the implementation of the Ministry of Education Sector Budget Plan, and shall have prepared a Sector Budget Plan for the Ministry of Health and for one additional ministry or vice-ministry.	Completed.
Schedule 4, No.6	Borrower shall have put into effect the Advance Spending Authorization Procedures in all its ministries and the agencies thereof.	Completed.
Schedule 4, No.7	Borrower shall have made progress in the implementation of the Court of Accounts Audit Plan.	New Court of Accounts Law applies ex-post audit function.
Schedule 4, No.8	Borrower shall have established, in the latest available issue of the Central Bank's publication entitled "Programa Monetario y Financiero" a public savings target of at least 0.6 percent of its gross domestic product for fiscal year 1994.	Condition met.
Schedule 4, No.9	Borrower shall have made progress in the implementation of the Human Resources Information System.	Data base largely completed; more work needed in terms of timely updates.
Schedule 4, No.10	Borrower shall have completed the implementation of the Action Plan for the Reduction of Trade Duty Exemptions.	Condition met.
Schedule 4, No.11	Borrower shall have completed the Tax Studies, including the preparation of an action plan for the amendments thereof.	Studies being used to prepare additional tax enhancement policies.
Schedule 4, No.12	Borrower shall have completed the Tax and Customs Administration Reform Program.	Completed with some delays.

Schedule 4, No.13	Borrower shall have: (a) offered for sale all INCAFE's assets, at least one of INAZUCAR's assets excluding Complejo Pesquero; (b) offered for sale or lease all the assets of Complejo Pesquero; and (c) completed preparatory work for privatization of INAZUCAR's remaining sugar mills.	Partially met, some delays encountered; INAZUCAR privatization proceeding beyond original scope (**partial waiver granted**).
Schedule 4, No.14	Borrower shall have offered for sale CREDISA and ATLACATL.	Completed.
Schedule 4, No.15	Borrower shall have offered for sale its shares in the capita stock of Banco Hipotecario.	Minor delays due to problem on resolution of contingent liabilities.
Schedule 4, No.16	Borrower shall have: (a) adopted an action plan for improvement of rural credit system; and (b) commenced implementation of plan.	Condition met.
Schedule 4, No.17	Borrower shall have made progress in the implementation of the Hydrocarbons Reform Action Plan, including in particular: the submission to the Legislative Assembly of the draft Hydrocarbons Law and putting into effect the Revised Diesel Pricing System.	Condition partially met (**partial waiver granted**), Energy Sector Modernization Loan will address follow-up issues.
Schedule 4, No.18	Borrower shall have submitted to the Legislative Assembly a bill or bills revising the import tariffs for all Part III items so that the maximum tariff shall not exceed 20% and the minimum tariff shall not be lower than 5 % of the dutiable value of the respective items.	Condition met; recent Government announcement calls for additional tariff reductions.
Schedule 4, No.19	Borrower shall have submitted to the Legislative Assembly the Draft NTBs Removal Laws.	Condition met.
Schedule 4, No.20	Borrower shall have developed the Poverty Alleviation Strategy.	Condition met; education program more successful, other components in need of additional resources.
Schedule 4, No.21	Borrower shall have: (a) adopted the Poverty Alleviation Plan; and (b) commenced implementation of such plan.	Condition met.
Schedule 4, No.22	(a) CONAMA shall have approved the Environmental Action Plan; and (b) Borrower shall have put into effect such action plan.	Condition met, although change in Administration caused delays in implementation.
Schedule 4, No.23	Borrower shall have submitted to the Legislative Assembly the Draft Environmental Law.	Condition met.

Table 8: BANK RESOURCES—MISSIONS

Stage of the Project Cycle	Month/Year	No. of Persons	Days in Field
Through Appraisal	May-Nov 1992	39	53
Appraisal through Board Approval	June/July 1993	5	5
Board Approval through Effectiveness	Aug 2-7, 1993	1	5
Supervision	Oct 4-8, 1993	4	5
Completion	Oct/Nov 1995	2	9

BORROWER ASSESSMENT[10]

SAL II was accompanied by policy measures which, on the one hand, aimed to complete the macroeconomic stabilization phase initiated in 1989 and SAL I, and on the other, included measures aimed at preparing the phase involving productive reconversion and modernization of the economy.

Negotiations and implementation of SAL II were quite fast. In this connection, special mention should be made of the way in which the negotiations and implementation of SAL II were organized. In terms of the design of measures, as well as their negotiation and implementation, the process was fully participatory. Institutions were responsible for their corresponding areas in technical and political terms, the inter-institutional working groups contributed to the discussions on progress, creating synergy and complementing efforts.

1.- Completing the Macroeconomic Stabilization Phase

In terms of the measures included in this area, efforts to improve tax and customs administration should be mentioned. SAL I included among others, measures directed toward simplifying taxes and import duties. SAL II complemented these measures by supporting the modernization of tax and customs administration systems; mainly through modernization of the legal and regulatory frameworks, the simplification of procedures, the strengthening of information systems and the integration of data bases.

Strict vigilance was maintained on the fiscal deficit, through efforts to mobilize additional public revenues and the rationalization of fiscal expenditures (mainly on salaries).

Privatization can be considered as part of the second phase of the structural adjustment process: productive reconversion and modernization of the economy. Nonetheless, it should be mentioned here because of its relevance in enhancing the confidence of entrepreneurs, through actions that demonstrate the Government's clear sense of direction.

2.- Productive Reconversion and Modernization of the Economy

It is worth while emphasizing the contribution made by SAL II to the design and initiation of the public sector modernization process.

- It supported the elaboration of a comprehensive vision of modernization, through the development of an action plan for the public sector modernization; as well as through the modernization of some of the macro-systems which cut across the whole public sector: budget, auditing, and human resources.
- It promoted the development of the technical base for the modernization, by providing implementation guidelines for the different technical groups that participated at the institutional level and which were being coordinated on the basis of these joint efforts.
- It launched comprehensive institutional modernization in some Ministries or public sector entities, by supporting the institutional diagnoses.
- It supported the construction of a reliable and timely social information system.
- It was possible to carry out an inventory of human resources and the design and implementation of the Human Resource Information System (SIRH), which is being adopted by institution and which will enable a new management of human resources in the public sector.

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[10] This is an unedited, unofficial translation of the Borrower's assessment of the results achieved through the Loan.

IMAGING

Report No: 15472
Type: ICR