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IDB COUNTRY STRATEGY 2016–2020

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ABBREVIATIONS

ANEP	Administración Nacional de Educación Pública [National Public Education Administration]
ANII	Agencia Nacional de Investigación e Innovación [National Research and Innovation Agency]
ASSE	Administración de los Servicios de Salud del Estado [State Health Services Administration]
AUCI	Agencia Uruguaya de Cooperación Internacional [Uruguayan International Cooperation Agency]
BCU	Central Bank of Uruguay
BROU	Banco de la República Oriental del Uruguay
CAF	Corporación Andina de Fomento [Andean Development Corporation]
DNE	Dirección Nacional de Energía [National Energy Division]
DNV	Dirección Nacional de Vialidad [National Highway Authority]
ECH	Continuous household survey
FDI	Foreign direct investment
FONASA	Fondo Nacional de Salud [National Health Fund]
GDP	Gross domestic product
IAMC	Instituciones de Asistencia Médica Colectiva [Collective Medical Assistance Institutions]
ICT	Information and communication technologies
IIC	Inter-American Investment Corporation
INE	Instituto Nacional de Estadística [National Institute of Statistics]
INEFOP	Instituto Nacional de Empleo y Formación Profesional [National Institute of Employment and Professional Training]
LNG	Liquefied natural gas
MEC	Ministry of Education and Culture
MEF	Ministry of Economy and Finance
MIF	Multilateral Investment Fund
MSP	Ministry of Public Health
NSG	Non-sovereign guaranteed
OECD	Organization for Economic Cooperation and Development
OMJ	Opportunities for the Majority Sector
OPP	Office of Planning and Budget
OVE	Office of Evaluation and Oversight
PBL	Policy-based loan
PISA	Programme for International Student Assessment
PPP	Public-private partnership
RIEPS	Red Integrada de Efectores Públicos de Salud [Integrated Network of Public Health Providers]
RISS	Redes Integradas de Servicios de Salud [Integrated Health Services Networks]
SCF	Structured and Corporate Financing Department
SEP	Social Entrepreneurship Program
SG	Sovereign guaranteed
SICA	Sistema Integrado de Control de Auditorías [Integrated Audit Control System]

SIIF	Sistema Integrado de Información Financiera [Integrated Financial Information System]
SMEs	Small and medium-sized enterprises
SNIC	Sistema Nacional Integrado de Cuidados [National Integrated Care System]
SNIS	Sistema Nacional Integrado de Salud [National Integrated Health System]
TFP	Total factor productivity
WHO	World Health Organization

EXECUTIVE SUMMARY

Country context	Since 2003, the Uruguayan economy has posted twelve years of uninterrupted growth, averaging 5% per year from 2003 to 2014. This expansion has been fueled by good performance in certain agribusiness sectors, energized by major investments in forestry, as well as by the development of the services, construction, and export sectors. However, over the last three years, the economy has slowed, with growth at 3.5% in 2014. While the economic expansion was reflected in improvements across the main social indicators, significant inequalities persist, and weaknesses in human capital formation, productive infrastructure, technology and innovation, financial markets, and trade development could limit growth in the medium and long term.
The IDB in Uruguay	The Bank's country strategy with Uruguay for the period 2010-2015 focused on the following priority areas: (i) transport; (ii) energy; (iii) water, sanitation, and solid waste; (iv) science and technology; (v) social protection; (vi) education and job training; (vii) agribusiness; (viii) services exports; (ix) public management and finances; and (x) urban development and security. During the effective period of the strategy up to the date of distribution of this document, 29 sovereign guaranteed (SG) loan operations were approved in an aggregate amount of US$1.908 billion,[1] along with 35 non-sovereign guaranteed (NSG) operations in an aggregate amount of US$967 million.[2]
Priority areas 2016-2020	The objectives of the country strategy for 2016–2020[3] are to: (i) boost productivity and competitiveness by promoting innovation, improving productive infrastructure, and supporting an integrated and coordinated policy for international positioning; (ii) promote equity and social inclusion by strengthening the human capital and employability of the population, supporting health care reform, improving habitat, and supporting the early childhood and youth segments of the most vulnerable population groups; and (iii) strengthen public sector management by supporting greater efficiency in public institutions and strengthening urban and departmental management.
Lending framework	The Bank anticipates approvals of sovereign guaranteed (SG) operations totaling approximately US$1.8 billion for the period 2016-2020. Under this scenario, the country's debt with the Bank would remain at around 3.6% of GDP on average for the entire period.
Main risks	The main risks to implementation of the strategy are: (i) the uncertain international environment, which could affect the priorities set by the government; and (ii) the size and political and institutional complexity of certain initiatives proposed by the government, which could complicate implementation and affect the Bank's program in those areas.

[1] This includes US$366 million approved under the Reallocation Program and US$50 million from the China Cofinancing Fund.

[2] Of these operations, 10 are SCF operations totaling US$914.4 million.

[3] This country strategy will be in effect from 1 January 2016 to December 2020.

RESULTS MATRIX

Government objective	Strategic pillar	Priority area	IDB strategic objective	Expected results	Indicators	Baseline
To use information and communication technologies (ICT) as a public policy driving employment and income improvements, social inclusion and regional integration, and coordination of science and technology with the productive apparatus through creation of the National Competitiveness System	**Productivity and competitiveness**	Promotion of innovation	To promote business innovation	Increased private sector investment in innovation	Private sector investment in research and development in relation to the GDP	0.1% (ANII 2013, annual)
			To improve coordination of ICT policies	Launch of the National Competitiveness System	Percentage of the public budget of public ICT agencies monitored by the National Competitiveness System	0% (OPP 2015, annual)
To invest in transportation and logistics infrastructure, favor maritime and inland waterway transportation and railroad freight transportation, create a National Infrastructure System, and promote energy self-sufficiency by supporting local and renewable energy sources		Improvement of the productive infrastructure	To improve the transportation infrastructure	Improvement of the national road network	Percentage of the national road network in very good and good condition[a]	45% (DNV 2012, annual)
			To develop installed power generation capacity	Increased installed generation capacity from wind and solar photovoltaic energy	MW of wind and solar energy capacity	Wind: 481 MW Solar photovoltaic: 3.7 MW (DNE 2014, annual)
			To increase medium- and long-term financing[b]	More medium- and long-term bank credit	Total amount of bank loans with maturities of greater than one year/total amount of bank loans outstanding as at 31 December	4% (BCU 2013, annual)
To diversify the productive and market structure; deploy policies to attract investments targeted to sectors with high value added; and create the National Competitiveness System		Integrated and coordinated international positioning	To diversify export markets	Greater diversification of export markets	Herfindahl-Hirschman Index (HHI) of export concentration by market	0.11[c] (DNA 2014, annual)

Government objective	Strategic pillar	Priority area	IDB strategic objective	Expected outcomes	Indicators	Baseline
To guarantee universal access to early childhood education (from age three), transform secondary school education, move forward on developing technological secondary school education and job training, and expand the use of technologies in education	Equity and social inclusion	Strengthening of the human capital and employability of the population	To improve access to early childhood education	Expanded early childhood education coverage	Percentage of 3-year-olds who attend early childhood education centers	60% (MEC 2013, annual)
			To increase the secondary school graduation rate[d]	Increased rate of completion of both secondary school cycles	Percentage of 17- to 18-year-olds who complete the basic secondary school cycle; Percentage of 21- to 22-year-olds who complete the higher secondary school cycle	65% 38% (MEC 2013, annual)
			To improve the quality of education	Students improve learning in primary school and basic secondary school	Average PISA test score	Reading 411 Mathematics 409 Science 416 (PISA 2012, every 3 years)
			To improve access to job training	Expanded job training coverage financed through the public sector	Percentage of persons trained annually through the INEFOP/active population	1.1% (INEFOP 2014, annual)
Priority health programs; strengthening of the first level of care, integrated health services networks, and ASSE and RIEPS leadership; strategic plan for health workers; better targeted financing		Support for health care reform	To improve the first level of health care	Improved primary and preventive health care in the State Health Services Administration (ASSE) and Collective Medical Assistance Institutions (IAMC)	Percentage of pregnancies monitored in the first trimester Ratio of non-urgent/urgent visits	ASSE 54%; IAMC 87% ASSE 2.6; IAMC 5.3 (SINADI 2013, annual)
To eliminate the housing emergency; optimize intensive use of the housing and habitat stock; expand water and sanitation coverage; and strengthen public financing for housing		Habitat improvement	To reduce the qualitative housing deficit[e]	Reduction in the number of people residing in irregular settlements	Percentage of people living in irregular settlements	5% (ECH 2014, annual)
				Expanded sanitation coverage in the Montevideo metropolitan area	Percentage of households connected to the sanitation network in the Montevideo metropolitan area	70.7% (ECH 2014, annual)
To guarantee the exercise of social rights for the entire population and create the National Integrated Care System (SNIC) aimed at providing care for dependent population groups		Support for early childhood and youth segments of vulnerable population groups	To improve access to and quality of social benefits and services for the most vulnerable children and youth (quintiles 1 and 2)	Expanded access to parenting skills training workshops and “Experiencias Oportunas”[f] [Timely Experiences] for children in vulnerable households	Percentage of children 0-24 months from households in quintiles 1 and 2 who attend parenting skills training workshops and “Experiencias Oportunas” daily	18.4% (Based on the ECH and SIIAS/MIDES 2013, annual)
				Reduced rate of functional disengagement (individuals not attending school or working outside the home) among more vulnerable youth	Percentage of 15- to 29-year-olds not attending school or working in quintiles 1 and 2	Women: Q1 41%, Q2 21% Men: Q1 22%, Q2 13% (ECH 2014, annual)

Government objective	**Strategic pillar**	Priority area	IDB strategic objective	Expected outcomes	Indicators	Baseline
Modern, effective, and efficient public management	**Public sector management**	Greater efficiency in public institutions	To strengthen public management systems	Improved budget management	Unexecuted portion of the national budget (calculated as the percentage of the budget that remains unexecuted at the end of the each fiscal year for the central government and Article 220 agencies, plus subsidies and various credits)	5.5% (MEF 2013, annual)
			To increase the effectiveness of the National Police in preventing crime	Reduction in robberies	Number of robberies reported[g] to the National Police nationwide in the last 12 months	20,097 (Ministry of Interior, Dec 2014, annual)
				Increase in the proportion of victims of robberies who report them to the National Police	Percentage of victims of robberies who have reported them to the National Police in the last five years	47% (Victimization Survey, Ministry of Interior 2011)
To consolidate the institutional framework of municipios		Strengthening of urban and departmental management	To strengthen the decentralization process	Development of third level of government	Percentage of municipalized territory	20% (OPP 2014, annual)

[a] A road pavement is considered in very good condition if the surface condition index is higher than 85; in good condition if the index is between 70 and 85; in fair condition if it is between 50 and 70; and in poor condition if it is lower than 50. The methodology is described in a road pavement visual evaluation manual prepared by the Dirección Nacional de Vialidad [National Housing Authority] (DNV) and is based on the Pavement Condition Index (ASTM D6433-11), adapted and calibrated to reflect local conditions.

[b] Medium-term loans refer to loans for terms of 12 to 24 months, and long-term loans refer to loans for terms of more than 24 months.

[c] The Herfindahl-Hirschman Index (HHI) measures the concentration of exports by market and ranges from 0 to1, where values close to 0 (1) indicate low (high) concentration. In 2008, the HHI averaged 0.06 in advanced economies and 0.14 in emerging countries.

[d] Secondary education is divided into two levels: basic secondary education (first to third year of secondary school) and higher secondary education (fourth to sixth year of secondary school), the latter being more focused and specialized.

[e] Qualitative deficit is defined as housing that exhibits problems with construction materials, lack of water or sanitation, overcrowding, etc.

[f] "Experiencias Oportunas " is a type of service at child and family care centers that supports mothers and/or caretakers by providing childrearing guidelines (nutrition, health, care) and practices to stimulate child development from the earliest age.

[g] Includes reports of actual and attempted robberies.

MATRIX OF COUNTRY SYSTEMS

Government objective	IDB strategic objective	Expected outcomes	Indicator	Baseline	Indicative targets
Greater efficiency, effectiveness, and transparency in public procurement and finances	Strengthening of country systems or subsystems	Implementation of the Integrated Audit Control System (SICA) in Bank projects audited by the State Audit Office	Percentage of projects audited by the State Audit Office that use the SICA	13% (2014)	100% (2020)
		Strengthening of the national competitive bidding subsystem	Number of new procurement mechanisms under the TOCAF that are regulated and implemented	0 (2014)	3 (2020)
	Use of country fiduciary systems	Framework agreements and electronic auction implemented and in use in Bank operations	Percentage of the portfolio that uses a framework agreement or the electronic auction mechanism as a procurement method	0% (2014)	40% (2020)
		Increase in the use of country financial management systems in operations	Percentage of use of the accounting and reporting subsystem (International Projects System, SPI)	22% (2014)	50%[a] (2020)

[a] The SPI is an accounting model that connects with the SIIF and is only used for loan operations executed by the central government. The indicative target refers to 100% of these loan operations, which according to the current portfolio composition would be 50% of the current loan portfolio.

I. Country Context

1.1 Since 2003, the Uruguayan economy has posted twelve years of uninterrupted growth, driven by a highly favorable international environment and a stable macroeconomic environment sustained by effective economic policies. Between 2003 and 2014, the economy grew at an average annual rate of 5%. This expansion was fueled by the dynamic performance of certain agribusiness sectors, energized by major investments in forestry, as well as by the development of the services sector and robust results in construction and exports.[4] In addition to high investment levels, this growth was bolstered by higher employment and improved productivity.[5]

1.2 Over the last three years, the economy began to slow, with growth at 3.5% in 2014. The forecasts for 2015 and 2016 point to growth rates ranging from 2% to 2.5%. This projected weakening comes on slower growth in the economies of important trading partners such as Argentina, Brazil, and China, appreciation of the bilateral exchange rate with Brazil, a decline in commodity prices, and a potential rise in interest rates in the United States, which could affect the inflow of foreign private capital. The fiscal deficit (3.5% of GDP in 2014) and the inflation level (8.3% in 2014) are the main macroeconomic policy challenges. Inflation has exceeded the Central Bank's target range (3%-7%) since 2011.

1.3 The economic buoyancy has been reflected in improvements in the main social indicators. Poverty fell from 33% of the population in 2006 to 10% in 2014, while the rate of indigence decreased from 2.5% to 0.3% of the population over the same period. Inequality indicators have likewise trended downwards, and the Gini coefficient fell from 0.46 to 0.38 between 2007 and 2014.[6]

1.4 However, significant inequalities persist, and urban violence and insecurity are on the rise. Despite the strong impact that economic growth has had on redistribution, the effects on different income groups have been uneven, and social exclusion levels (by age, sex, and geographic location) remain high. For example, while the unemployment rate was 6.6% in 2014, it was 8.3% for women and 20.4% for those under the age of 25. In the case of education, whereas 74% of young people from households in the top income quintile complete their secondary education, only 17% for young people from households in the bottom quintile do. In addition, the rise in homicides and robberies,[7] among other crimes, is taking a heavy toll not

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[4] Between 2004 and 2014, exports of goods and services contributed an average of 2.1 percentage points to GDP growth. Trade in services has been gaining ground, going from 28% of exports in 2005 to 32% of exports in 2012 (including exports from free trade zones). Uruguay has comparative advantages in the tourism, transportation, and global services sectors. In particular, between 2003 and 2010, software exports in current dollars rose by a factor of nearly 3.8, while total exports multiplied by a factor of 2.6 during the same period (OECD, 2014).

[5] Between 2005 and 2014, the investment/GDP ratio went from 17% to 23%, the activity rate climbed from 60% to 65%, and total factor productivity grew at an average annual rate of 1.3% (BCU, INE, and calculations by the authors).

[6] Income inequality in Uruguay, though high by OECD member country standards, is the lowest in the region (INE and World Bank).

[7] Between 2009 and 2013, homicides rose by 15% and robberies by 48%. This explains why more than half of the population cites insecurity as its greatest concern.

only on the country's economy (the economic cost of containing the violence being estimated at 3.4% of GDP) but also on the underlying social fabric.[8]

1.5 In the coming years, Uruguay will face major challenges in addressing certain gaps that could limit the country's medium- and long-term growth.[9] An insufficient and inadequate supply of human capital is one of the most significant constraints on economic growth, especially as exports become more intensive in skilled labor. Uruguay has shortcomings in terms of the quality, relevance, and equity of secondary and technical-vocational education. Over 60% of young people fail to complete secondary school, and the supply of skilled labor in the workforce is insufficient.[10]

1.6 In addition, the costs associated with the infrastructure deficit and the difficulties in obtaining access to infrastructure financing[11] are affecting economic growth and competitiveness. According to the Global Competitiveness Index 2014-2015, Uruguay is ranked in 80th place among 144 countries: in 96th place in the transport infrastructure subindex, in 90th place in the quality of roads subindex, and in 103rd place in the quality of railroad infrastructure subindex. Furthermore, the country's cost of energy, particularly electric power, is higher than the average for the region.[12]

1.7 Another constraint on achieving improvements in productivity and competitiveness is the low level of investment in technology and innovation.[13] Investment in technology and innovation accounts for less than 10% of Uruguay's recent productivity growth. A comparison with successful small economies suggests that this figure is not sufficient to ensure sustainable productivity growth,[14] which is essential in order to sustain economic growth over the long term and avoid being drawn into a critical development stage known as the "middle income trap."[15]

1.8 With regard to trade development, Uruguay has a significant gap in the level of export diversification. Despite its dynamic performance in recent years, Uruguay's export sector continues to be concentrated in a few products that are susceptible to fluctuations in international commodity prices.[16]

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8 See "Sector Note: Citizen Security," IDB, 2015.

9 See "Technical Note: Economic Growth and Development Gaps in Uruguay," IDB, 2015.

10 See "Sector Note: Labor Markets," IDB, 2015.

11 The financial sector in Uruguay is poorly developed (in terms of private sector credit, volume of insurance premiums, number of bank branches, and market capitalization) and financial inclusion levels are not only inconsistent with the country's income levels but also low in the regional context. The Financial Inclusion Law enacted in 2014 seeks to raise financial inclusion levels in the population, primarily for low-income groups.

12 See "Sector Note: Energy," IDB, 2015.

13 Uruguay invests 0.3% of GDP in innovation, while the region as a whole invests 0.7% of GDP and OECD countries invest 2.5% of GDP ("Sector Note: Competitiveness and Innovation," IDB, 2015).

14 Between 1991 and 2010, innovation accounted for less than 10% of total factor productivity (TFP) growth in Uruguay, but for more than 50% of TFP growth in South Korea, Ireland, and Finland.

15 This stage is characterized by slower growth due to the inability to achieve continuous improvements in productive efficiency, impairing the economy's transition to productive structures with higher value added.

16 In 2014, 51% of goods exports were accounted for by five products: soybeans, beef, dairy products, pulp, and rice, while more than half of all exports were destined for six countries: China, Brazil, Argentina, Netherlands, United States, and Venezuela (Uruguay XXI, 2015).

1.9 The country strategy for 2016-2020 proposes addressing some of these challenges around three core pillars: (i) improve productivity and competitiveness; (ii) foster equity and social inclusion; and (iii) strengthen public management.

II. THE IDB IN URUGUAY

2.1 The IDB is the main multilateral institution in the country. Over the past five years, its disbursements accounted for about 50% of all multilateral financing for the public sector and 5% of overall public debt. On the private sector side, between 2011 and 2014, the IDB Group directly financed about 1.1% of private investment in Uruguay (private gross fixed capital formation), primarily in the energy and agribusiness sectors (respectively 0.4% and 0.7% of total private investment), with a very significant foreign direct investment (FDI) component.[17]

2.2 The Bank's country strategy with Uruguay for the period 2010-2015 (document GN-2626)[18] focused on the following priority areas: (i) transport; (ii) energy; (iii) water, sanitation, and solid waste; (iv) science and technology; (v) social protection; (vi) education and job training; (vii) agribusiness; (viii) services exports; (ix) public management and finances; and (x) urban development and security.

2.3 During the effective period of the strategy up to the date of distribution of this document, 29 sovereign guaranteed (SG) loan operations were approved in an aggregate amount of US$1.9083 billion, including US$366.3 million approved under the Reallocation Program and US$50 million from the China Cofinancing Fund. Of these operations, three are policy-based loans (PBL) with a deferred drawdown option for a total amount of US$917 million.[19] The approvals were in the following sectors: service exports (49% of the approved amount, including the three PBLs), energy (15%), water and sanitation (9%), urban development (8%), public management (6%), transport (4%), agribusiness (4%), science and technology (3%), and education and job training (3%).[20] Two additional operations under the country strategy for 2010-2015, totaling US$111 million, are expected to be approved.

2.4 As for non-sovereign guaranteed (NSG) loans, 35 operations were approved for an aggregate amount of US$966.9 million.[21] The private sector windows primarily contributed to the energy (68%) and agribusiness (27%) sectors. In recent years, the Bank has noticeably expanded its presence in the Uruguayan private sector, complementing and reinforcing its activities with the government, by supporting large strategic investments in areas related to the energy matrix (wind and solar energy), the agroforestry industry, and agribusiness. Since most NSG operations

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[17] The total investment of projects that received IDB financing accounts for about 8% of total private gross fixed capital formation between 2011 and 2014, and the percentage is even higher if complementary investments by other project providers are included.

[18] Strategy in effect from December 2010 to December 2015.

[19] Of this total, US$366.3 million approved under the Reallocation Program was canceled in February 2015.

[20] The loan to Banco de la República Oriental del Uruguay (BROU) (UR-L1099) for US$125 million, aimed at financing productive infrastructure investment projects, was split between the energy and agribusiness sectors.

[21] Of these operations, 10 are SCF operations totaling US$914.4 million.

have been aimed at greenfield projects and investments in fixed assets, this financing can be measured against the flow of FDI into Uruguay. If all investments that have accompanied the NSG projects are taken into account, the Bank has facilitated investments of at least US$3.3157 billion, which represents almost 25% of FDI in the country in the period between 2011 and 2015.

2.5 As of July 2015, the portfolio in execution has 38 SG loans for US$1.8273 billion. Of this total, 35 are investment loan operations totaling US$1.2764 billion, of which US$679.8 million is pending disbursement, and 3 are PBLs for US$550.8 million with a deferred drawdown option. The main sectors comprising the active public sector portfolio are: export and investment promotion (31%); water, sanitation, and solid waste (18%); energy (16%); urban development and security (13%); science and technology (5%); agribusiness (4%); transportation (4%); public management and finance (4%); education and job training (3%); and social protection (2%).

2.6 The active private sector (NSG) portfolio is composed of 27 loans totaling US$842 million, including 8 SCF loans for US$795.5 million, 17 operations from the Inter-American Investment Corporation (IIC) for US$40.6 million, 1 Multilateral Investment Fund (MIF) loan under the Social Entrepreneurship Program (SEP) for US$1 million, and 1 Opportunities for the Majority (OMJ) loan for US$5 million. The portfolio is primarily concentrated in the energy (64%) and agribusiness (32%) sectors.

2.7 With regard to technical support, 33 nonreimbursable technical-cooperation operations and 1 investment grant are currently being executed in the public sector for a total of US$25 million. These operations finance a broad spectrum of activities, such as: strengthening of public entities, strategic sector studies (innovation, education and job training, water and sanitation), and support for improving the quality of social services. At the same time, 14 technical cooperation operations from the MIF are being executed for a total of US$11.2 million, focusing on agricultural sector development, entrepreneurship, financial inclusion, tourism development, and public-private partnerships (PPPs).

2.8 **Results achieved and in progress.**[22] Considering the results obtained in the framework of the country strategy for 2010-2015, four areas stand out for their transformational significance. In the first place, the Bank has been a key partner in bringing about an important change in the country's energy matrix.[23] The IDB Group has approved SG financing for a combined-cycle thermal plant and six NSG wind and solar energy projects that will help boost electric power generation capacity by 950 MW (35% of installed capacity in 2011). The Bank's intervention to support modifications to the regulatory framework envisaged for private investments in this area was a key factor in promoting such investments, including by attracting local, international, and multilateral lending institutions. In addition, the

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[22] The results achieved in the framework of the country strategy for 2010-2015 are described in greater detail in Annex III. They include results achieved during this period from the portfolio in execution as well as from approvals obtained during the period.

[23] By the end of 2015, Uruguay could be generating more than 90% of its electric power from renewable sources (depending on hydrology) and become one of the world's leading countries in terms of the percentage of electricity generated from wind power (28% of installed capacity). ("Energías renovables: Oportunidades de inversión" [Renewable Energy: Investment Opportunities], Uruguay XXI, 2014).

Bank has supported studies for development of the regasification plant and modernization of the Salto Grande binational hydropower plant.[24]

2.9 In the second place, the Bank has helped to foster business innovation and development of leading-edge technologies in the agribusiness sector.[25] The IDB Group has financed: (i) nearly 300 innovation projects with small and medium-sized enterprises (SME) through the National Research and Innovation Agency (ANII), finding that the beneficiary enterprises increase their spending in research and development three to four times more than the control group and that 20% of them introduce product innovations; (ii) the construction of a state-of-the-art pulp mill that involved the largest private investment in the country's history and is expected to boost pulp exports by US$700 million per year; and (iii) the construction of a sustainable agribusiness complex for milk powder production that aims to lead the powdered milk processing sector in Uruguay.[26]

2.10 In the third place, the Bank has supported broader use of new information and communication technologies (ICT) in: (i) schools, through Plan Ceibal, resulting in 100% of students in the basic secondary school cycle having laptops and their schools having computer equipment; (ii) health care, with nine public and private health institutions adopting electronic health records; (iii) budget management systems and improvements in electronic government;[27] and (iv) citizen security, by providing crime-prediction software for intelligent preventive policing.[28]

2.11 Lastly, the Bank has spurred the development of central urban areas of the capital. The intervention in the Goes neighborhood,[29] a rundown central area of Montevideo, focused on the Montevideo Agricultural Market, a property which, despite its deteriorated condition, helped spark a socioeconomic revitalization of this neighborhood. This intervention also included investments aimed at improving the physical space and urban facilities in the surrounding area, as well as a fund for housing improvement and community initiatives. The intervention not only revitalized and enhanced the social and commercial profile of the neighborhood

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[24] Punta del Tigre "B" Combined-Cycle Project (UR-L1070), Palmatir Wind Power Project (UR-L1080), Carape I & II Wind Power Project (UR-L1086), La Jacinta Solar Power Project (UR-L1092), Colonia Arias Wind Power Project (UR-L1103), Valentines Wind Power Project (UR-L1105), and Casa Blanca and Giacote Solar PV Project (UR-L1100). In addition, there is a line of credit to the BROU that includes a component for financing renewable energy projects (UR-L1099) and the private sector window is considering financing for the regasification plant (UR-L1045 and UR-L1095).

[25] Technology Development Program II (UR-L1030), Estancias del Lago (UR-L1059), Montes del Plata (UR-L1068).

[26] Some 20,000 tons of milk powder will be produced annually from an integrated dairy operation, which is the largest in the country and the region and will have more than 13,000 milking cows.

[27] Including 17 agencies using electronic recordkeeping systems and 74 government transactions that citizens can complete at least partially online.

[28] Plan Ceibal II: Support for Primary and Secondary Math and English Education (UR-L1093), Electronic Health Records in Public Hospitals in Uruguay (UR-T1091), MIF ATN/ME-10681-UR, Program to Support e-Government Management in Uruguay II (UR-L1065), Budget Management Strengthening Program (UR-L1098), and Integrated Local Management Program for Citizen Security (UR-L1062). In the context of these actions, the MIF played a key role in the pioneering stages of development of the software industry in Uruguay by supporting efforts to strengthen the sector's institutions and its presence in the global market.

[29] Through joint action by the MIF and the Fiscal and Municipal Management Division (ICF/FMM). Montevideo Agricultural Market as a Critical Element in the Socioeconomic Revitalization of the Goes Neighborhood (UR-M1030) and First Neighborhood Improvement Loan (UR-L1009).

but also mobilized private investments, generating 500 new housing solutions and job opportunities for area residents. The activity in the area has contributed to improved security in the neighborhood.[30]

2.12 A noteworthy aspect of the Bank's actions in this field and others is their crosscutting nature, with innovation promotion as a recurrent theme in all the different interventions. This is reflected in strong innovation-related additionality in the Bank's SG and NSG portfolio in various sectors, particularly in the aforementioned fields of renewable energy, state-of-the-art technology, scientific research, and use of ICT, for example in the areas of education and electronic government.

2.13 With regard to regional cooperation, the country is a leader in regional initiatives supported by the Bank, such as the youth development knowledge network, the regional framework to promote effective interventions for at-risk youth, the electronic health record network, coordination in the area of citizen security, exchanges on innovation issues, neighborhood improvement, decentralization, PPPs, and other issues.

III. PRIORITY AREAS

3.1 The objective of the Bank's country strategy with Uruguay for 2016–2020 is to support the national government plan with a view to achieving inclusive and sustainable growth in line with the Update to the Bank's Institutional Strategy for the period 2010-2020, as described below. Accordingly, the Bank proposes focusing on priority areas within **three strategic pillars** that will guide both SG and NSG operations: (i) **productivity and competitiveness**; (ii) **equity and social inclusion**; and (iii) **public sector management**.

A. Productivity and competitiveness

3.2 Bank interventions will be aimed at boosting productivity and competitiveness by: (i) promoting innovation; (ii) improving productive infrastructure; and (iii) supporting an integrated and coordinated policy for international positioning.

3.3 These three lines of action contribute to the following objectives of the Update to the Bank's Institutional Strategy: establish smart institutional frameworks; provide adequate knowledge and innovation ecosystems; improve regional infrastructure; insert firms into value chains; and converge integration policies and instruments.

3.4 In addition, with a view to boosting sustainable growth and productivity, the Bank will promote human capital development by means of interventions aimed at reducing social exclusion and inequality, as described under the following strategic pillar.

3.5 **Promotion of innovation.** Despite the recent economic growth, the gap between Uruguay's per capita GDP and that of the United States is greater today than in 1960. The reason for the lack of long-term convergence is the poor performance of total factor productivity (TFP). While TFP grew at an average annual rate of 1.3%

[30] This intervention was favored by synergies with the Integrated Local Management Program for Citizen Security (UR-L1062).

over the last 10 years,[31] contributing to economic growth, the country needs to accelerate productivity growth in the coming years, and above all make it sustainable, if it is to maintain a high rate of growth and avoid the diminishing returns that accompany physical and human capital accumulation. Firms become more productive when they introduce organizational improvements in management and technological improvements in products and productive processes, in other words, when they innovate. Uruguay invests 0.3% of GDP in innovation, compared with 0.7% of GDP for the region as a whole and 2.5% of GDP among OECD member countries. This gap is the result of two problems: (i) the highly disparate productive capacities of Uruguayan companies, as a result of which the critical mass of companies able to innovate is still small; and (ii) the relatively weak presence of knowledge-intensive sectors in the national productive structure.[32] These problems are rooted in limited business management and innovation capacities in domestic companies, as well as in these companies' low levels of coordination both within their value chains and with other actors in the national innovation system (e.g., universities, technology centers, etc.).

3.6 In terms of environmental factors, the existence of externalities and the low level of competition in some markets translate into a lack of incentives for companies to innovate and improve their productivity. In addition, restrictions on access to credit limit both the use of technology at existing companies and the ability of new, technology-based companies to scale their growth.[33]

3.7 The government plan for 2015-2020 proposes to strengthen innovation, science, and technology as a public policy to improve employment and income levels, social inclusion, and regional integration, as well as to integrate science and technology into the productive apparatus by creating a national competitiveness system.[34]

3.8 The Bank's country strategy will focus on activities to strengthen the regulatory framework and programs that foster innovation and technology-related entrepreneurship, as well as SME access to business development, technical assistance, and supplier development services and financing, with a view to

[31] According to central government calculations, TFP grew 2.9% between 2005 and 2014. The discrepancy is partly the result of an adjustment that is made to the explanatory variables in order to eliminate cyclical effects. In the IDB estimates, the capital stock is adjusted by its level of use.

[32] This remains true although innovation-intensive sectors have increased their share of the GDP, from 19% of GDP in 1997-1999 to 25% of GDP in 2009-2011. Yet the economic complexity of goods exports has remained more or less constant, and the goods export basket is still far removed from the more sophisticated product categories. Exports of ICT-intensive services (software) are an exception, due to the existence of a critical mass of human capital and sector-specific subsidies that have facilitated the development of a dynamic cluster of information technology companies (OECD, 2014).

[33] One in four local companies indicates that the lack of financing and the cost of financing are a constraint on innovation. In many cases, commercial bank loans do not reflect the borrower's needs or the risks associated with projects involving the use of innovative technology. Neither are there instruments favoring the development of a venture capital industry ("Sector Note: Competitiveness and Innovation," IDB, 2015).

[34] Bill sent to legislature in March 2015. The Uruguayan government wishes to move toward creating a national competitiveness system that promotes coordination among entities associated with the development of productive factors and helps the country to make strides in innovation, quality of human capital, and technology use. The national competitiveness system will seek to integrate the activities of various public entities with a view to putting forth coordinated objectives, policies, and strategies for international positioning of the economy, productive development, and science, technology, and innovation.

narrowing the productivity gaps. During the previous strategy period, the Bank positioned itself in the sector by supporting policies to improve the productivity of Uruguayan businesses, whether through science, technology, and innovation or productive development programs or in the form of medium- and long-term financing provided through Banco de la República Oriental del Uruguay (BROU).[35] Accordingly, the proposed activities in the sector are an opportunity to continue this process, consolidating the existing interventions to enhance their effectiveness on the basis of lessons learned, while strengthening the complementarity of the policies by supporting the new national competitiveness system. The Bank's work will prioritize coordination between the public and private sector windows so as to accelerate the launch of a venture capital industry.

3.9 The main risks identified include: (i) operational uncertainty at the agencies involved in implementing competitiveness and innovation programs since it may take some time for the reforms proposed by the national government to become institutionalized, which could be mitigated through an ongoing dialogue with the authorities on ICT issues; and (ii) insufficiently developed institutional capacity to implement innovative technical assistance and supplier development programs with extensive coverage as well as support instruments for challenge-based innovation, which will be mitigated by introducing institutional strengthening components into the agencies involved.

3.10 **Improvements in productive infrastructure.** The economic growth of the past decade, particularly in the agribusiness sector, has created pressure on the country's transportation and logistics infrastructure and services, especially the highway and rural road network, where Uruguay lags in terms of investment.[36] Despite a pronounced rise in demand, investments are needed in road improvement rather than in expansion of capacity (except for sections immediately adjacent to the Montevideo metropolitan area). The expenditures executed over the last two five-year periods have not been sufficient to prevent the road network from deteriorating under the weight of increased demand.[37] Since more than 92% of commercial freight in Uruguay is transported by road, poor road conditions have a significant impact on economic activity in the form of higher costs and reduced competitiveness for industrial enterprises. While the logistics performance index (LPI) has marginally improved since 2007, the gap with respect to OECD countries continues to be significant.[38] In view of the positioning of the ports of Montevideo and Nueva Palmira as a regional hub and their importance for the export sector, it is essential to maintain conditions that enable a sustainable expansion of port activity, taking into account the significant recent growth of transshipment cargo

[35] Technology Development Program II (UR-L1030), Program to Support Future Entrepreneurs (UR-L1071), Innovation Program for Productive Development (UR-L1069), Financial Program for Productive Development (UR-L1099), Estancias del Lago (UR-L1059), Montes del Plata (UR-L1068).

[36] According to the World Economic Forum 2014-2015, infrastructure limitations are the fifth most significant constraint on doing business in the country.

[37] The quality of highways has been deteriorating: In 2005, 50% of the country's highways were rated as in fair or poor condition, and the figure had risen to 55% in 2012 (DNV). IDB estimates indicate that approximately US$2 billion would be needed in the 2015-2019 period to upgrade road conditions enough to allow for proper economic management of the network.

[38] The LPI computed by the World Bank uses a scale from 1 to 5. This index climbed from 2.5 in 2007 to 2.7 in 2014.

headed to other markets. This requires continued investments in dredging of maritime and inland waterways and ports, as well as potential additional investments in berthing piers to accommodate more and larger cargo vessels. The railway sector, whose impact on logistics efficiency is limited by the small size of the country and the location of domestic production, is in need of continued investment in railways[39] and equipment but institutional strengthening above all. These investments should take resilience to climate change and sustainability issues into account. Furthermore, the relatively undeveloped capital markets and the lack of long-term financing are a barrier to investment in productive infrastructure in Uruguay.

3.11 The government plan for 2015-2020 proposes investing in transportation and logistics infrastructure, prioritizing maritime and inland waterway transportation and thus promoting ports and their accessibility, as well as freight railroad transportation; redesigning, developing, and maintaining the national and departmental road infrastructure as needed to maintain the production corridors; and creating the National Infrastructure System in order to steer the public and private investment process. Considering the high level of required investment in transportation and logistics infrastructure, the government expects the private sector to play a significant role in providing this funding. To this end, it plans to promote public-private partnerships (PPPs) as well as the use of financial instruments through the capital markets, which it has already done successfully in the past in this sector.

3.12 The country strategy will support Uruguay in improving the transportation (road, maritime and inland waterway, and railroad) and logistics network, with a focus on sector efficiency and taking resilience to climate change and sustainability issues into account. These actions will complement the support that the Bank has provided to improve freight infrastructure and logistics, primarily roads and maritime and inland waterways, develop a specific institutional framework for the logistics sector, and generate sector knowledge.[40] The Bank will continue to cooperate through SG loans, but also by promoting and supporting the development of institutional and market capacities for establishing PPPs and creating financing for public and private investment through the capital markets. For example, the Bank has identified the importance of helping to structure projects that meet the requirements for promoting PPPs, as well as looking into financial instruments that would address potential demand in this field.[41]

3.13 Due to contractual aspects related to the port agency and the Montevideo port operators, there is a risk that infrastructure will be developed without introducing operating models that enable the newly generated capacity to be used to the fullest extent. Likewise, if the investment in railway infrastructure is not accompanied by

[39] Railway rehabilitation works for US$200 million are currently underway. The amount needed to rehabilitate the remaining length of the active network is estimated at US$400 million.

[40] Road Infrastructure Program II (UR-L1067), which includes a component for institutional reform of the railroad sector; Supplemental Financing for the Port of Montevideo Modernization Program (UR-L1054); CVU Highway Program (UR-L1022); and Support for the Development of Freight Logistics ICTs in Uruguay (UR-T1066).

[41] In this regard, the work will build on the support provided by the Bank in designing and implementing the respective law by building capacity at the Corporación Nacional para el Desarrollo [National Development Corporation] and creating a PPP unit at the Ministry of Economy and Finance (MEF).

an organizational reengineering and the introduction of new regulatory and operational practices, the system will be unable to meet the forecast potential demand, such that an opportunity to develop this transportation mode will have been missed and expenditure will become inefficient. In both cases, the Bank can mitigate the risk by providing prior technical assistance to bring about the institutional development needed for successful execution of projects, and by carrying out activities to enhance institutional efficiency through the right combination of reimbursable and nonreimbursable resources.

3.14 The country's energy infrastructure has historically been characterized by dependence on imported energy and by the vulnerability of the electricity supply to hydrologic variability.[42] This has affected, among other things, the cost of energy in the country, which is higher than the average for the region, and particularly the cost of electric power, with its implications for the population and the competitiveness of the productive sector.[43] Since 2008, Uruguay has been promoting measures aimed at ensuring an energy supply, diversifying the energy matrix, and mitigating the sector's vulnerability to hydrologic variability, including a strong position in favor of renewable energy (wind and photovoltaic solar), construction of a combined-cycle gas plant and a liquefied natural gas (LNG) regasification terminal, and strengthening of regional electric interconnection. As indicated above, the Bank has been a key partner in these areas, supporting the financing of several of these projects.

3.15 The Bank will continue to support actions that help consolidate the diversification of energy sources and make use of their benefits, including private sector initiatives, focusing on renewable energy projects, measures to promote efficient energy use and minimize environmental impact, use of the natural gas available upon commissioning of the regasification plant,[44] and regional energy integration. The active portfolio in this area totals US$286.3 million in SG loans and US$530.5 million in NSG operations.[45]

3.16 Given the sector's rapid transformation, there are risks associated with efficient and integrated management of the electric system and natural gas, potential transmission capacity limitations in certain segments of the interconnected network in terms of dispatching the growing amount of wind energy (wind being an intermittent energy source), and the risk of missing opportunities to export energy using the available infrastructure. To mitigate these risks, it is important to accelerate the training of system agents, including the ability to forecast wind and

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[42] In 2010-2012, more than half of the energy supply was imported ("Energías renovables: Oportunidades de inversión" [Renewable energy: Investment opportunities], Uruguay XXI, 2014).

[43] For a medium-voltage industrial customer consuming 25 MWh/month, the cost in Uruguay is US$198/MWh (2013, including taxes), compared with prices ranging from (depending on the distribution company) US$90-139/MWh in Peru to US$155-210/MWh in Colombia, US$109/MWh in Chile (Chilectra), US$152/MWh in Brazil (Copel), and US$70/MWh in Ecuador (EEQSA) (CIER, 2013).

[44] The Bank is providing support on this matter through a nonreimbursable technical cooperation operation (UR-T1102).

[45] Punta del Tigre Combined-Cycle Project (UR-L1070), Palmatir Wind Power Project (UR-L1080), Carape I & II Wind Power Project (UR-L1086), La Jacinta Solar Power Project (UR-L1092), Colonia Arias Wind Power Project (UR-L1103), Valentines Wind Power Project (UR-L1105), and Casa Blanca and Giacote Solar PV Project (UR-L1100). In addition, there is a line of credit to the BROU that includes a component for financing renewable energy projects (UR-L1099).

water scenarios (including climate change adaptation issues), generate greater knowledge of the regional and international electric and LNG market, and identify and make critical investments, such as to reinforce the electric energy transmission and storage network. The Bank will help the Uruguayan government strike the right balance between addressing the country's energy efficiency requirements and making optimal use of energy resources, whether available or under development.

3.17 **Integrated and coordinated international positioning.** Uruguay's external sector has performed strongly in recent years with respect to exports and investments. This expansion process has involved significant changes in the sector's structure, leading to greater concentration in terms of both products and destinations, which constitutes a vulnerability for the future course of the economy.[46] Agricultural and agribusiness products accounted for 78% of goods exports in 2013. While this situation has been partly determined by exogenous factors such as the extraordinary boom in international agrifood commodity prices, it is imperative for the country to work to diversify its export basket through promotional efforts with a sector focus, coupled with strategic efforts to secure new export markets. At the same time, the country should improve market access conditions and pursue an active policy of attracting investments in strategic sectors. Furthermore, these actions should be supported by domestic public policies to create a favorable environment for ensuring that local production is consistent with the requirements of the international markets (for example, in terms of technical standards, human capital, innovation, etc.).

3.18 The principal guidelines of the new administration's policy in this area are: (i) to move forward on specializing and diversifying the productive and market structure (identifying sectors with greater potential for adopting technology, high productivity, and greater ability to create quality jobs); (ii) to provide continuity to policies designed to attract investments, focusing on sectors with high value added that create "new competitive advantages"; (iii) to minimize program fragmentation and dispersal of resources by creating a national competitiveness system; and (iv) to institutionalize use of the country brand.

3.19 The Bank's country strategy will focus on supporting implementation of a comprehensive and targeted policy to position the country globally while maximizing the local impact of those efforts. Accordingly, the strategy includes actions designed to reinforce the institutional structure of the external sector, improve international negotiation capabilities, and lock in reforms in trade facilitation and arrangements in border areas. As indicated in paragraph 3.8, support will also be provided for programs that promote innovation and technology-based entrepreneurship and seek to diversify the export basket and reduce vulnerability to climate change. At the same time, Bank actions will seek to improve export and investment promotion capacities, with a particular emphasis on post-investment services that facilitate upward movement in the value chain and

[46] Exports are increasingly concentrated in "new" products such as soybeans and pulp, which had practically no export share just one decade ago. In terms of destination markets, the most significant transformation is the substantial increase in China's share, from 4% in 2004 to 23% in 2013. With respect to FDI, the trend that began in the 1990s toward targeting natural-resource-intensive primary and industrial sectors has intensified. At the same time, MERCOSUR countries (particularly Argentina) have substantially increased their share of FDI in Uruguay, which in 2012 reached a record 47% of total FDI (Argentina's share being 38%).

maximize the local impact of investments. In addition, the strategy calls for selectively supporting the development of specific nontraditional sectors identified as strategically important for integrating the country into the global economy in the framework of the national competitiveness system, such as the global services sector. The Bank's experience in the country with supporting foreign trade management and global export services will serve as a foundation for designing and implementing new interventions in these areas.[47]

3.20 The main risk associated with implementation of the actions envisaged is the possibility of internal resistance to the proposed institutional changes, which could lead to a delay, or even a reduction in the scope, of the required institutional reorganization. The Bank will mitigate this risk through ongoing dialogue with the authorities so as to provide input that can be used for an effective design and implementation of the proposed reforms.

B. Equity and social inclusion

3.21 Within this strategic pillar, the Bank's interventions will be aimed at enhancing equity and achieving greater social inclusion by: (i) strengthening the human capital and employability of the population; (ii) supporting health care reform; (iii) improving habitat; and (iv) supporting the early childhood and youth segments of the most vulnerable population groups.

3.22 The interventions in these four priority areas are aligned with the following objectives of the Update to the Bank's Institutional Strategy for 2010-2020: eradicate extreme poverty, create a more redistributive fiscal policy, provide inclusive infrastructure and infrastructure services, and develop quality human capital.

3.23 **Strengthening of human capital and employability of the population.** Uruguay has made considerable efforts over the past decade to improve the learning conditions of the population, with an emphasis on equity and social inclusion. However, challenges persist at all educational levels but particularly in secondary schools, where despite net coverage gains, especially for children and adolescents in the bottom two income quintiles, there are problems in the form of grade repetition, low graduation rates, and poor quality. A full 35% of 17- and 18-year-olds did not complete the basic secondary school cycle, and 62% of 21- and 22-year-olds failed to complete the higher secondary school cycle (MEC, 2013).[48] The results of the PISA 2012 international test indicate that achievement levels in language, mathematics, and science have been stagnant since 2003 and that the quality gaps with respect to the educational systems in developed countries are not closing. Adolescents from the poorest groups are those most affected. Problems of coverage, low secondary school completion rates, and poor quality are associated with, among other things: widespread use of grade repetition as a student evaluation mechanism; encyclopedic curricular framework

[47] Foreign Trade Management Support Program (UR-L1015) and Program to Support Global Export Services (UR-L1060).

[48] There is evidence that dropping out of the educational system predisposes adolescents to have children earlier than their school-going peers (Varela Petito et al., 2012). Given the shortcomings of the childcare system, this primarily affects the employment possibilities of women. The launch of the National Integrated Care System (SNIC) should facilitate women's participation in the labor market.

and lack of coordination between cycles; low hourly load and large number of subjects per grade; high percentage of unlicensed, substitute, or interim teachers; excessive weight of seniority in the teaching profession; and a teacher management system that creates a high degree of dispersion and prevents proper planning.

3.24 Furthermore, the ratio of supply of training services (education and job training) to demand for skilled labor needs to be improved, considering the shortage of skilled labor in the workforce.[49] From an institutional standpoint, the National Institute of Employment and Professional Training (INEFOP) is a central agency focused on job training. It has significant public resources to invest in training, information, and guidance services, contributing to the country's productive development through its impact on individual skills and thus on the productivity of workers and businesses.[50] However, INEFOP is up against some challenges in terms of its coverage, relevance, and effectiveness. In particular, it should coordinate better with the private sector and its needs, shifting the focus towards a culture of work for development. This involves both employed and unemployed workers through the promotion of job training options and recognition of work experience.

3.25 The government plan proposes creating a long-term national education plan; continuing the wage improvement process; prioritizing the universalization of early childhood education for 3-year-olds; overhauling secondary education with a view to reducing the repetition rate by half; achieving universal school coverage for 15- to 17-year-olds; improving graduation rates in both (basic and higher) secondary school cycles; improving educational achievement; making progress in developing technological secondary education; and expanding the use of technology in education. In the area of job training, the priorities of the new administration are to strengthen the institutional framework for the professional training system and the national program for occupational certification (certification of job skills), linking and coordinating the management and actions of public institutions related to employment and job training, and implementing the Youth Employment Law approved during the previous administration.

3.26 The Bank has succeeded in positioning itself in the sector by supporting school infrastructure and teacher training and promoting interventions aimed at improving graduation rates, particularly at the secondary level.[51] In addition, the Bank supported from the outset the idea promoted by Plan Ceibal of expanding the use of new technologies in schools. This work will continue under the new strategy, with a greater emphasis on addressing the issues of school management and quality, while also focusing on social equity and gender equality, which are critical for raising productivity and creating more equitable growth. The Bank will continue to support interventions in education, particularly early childhood education in

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[49] According to an IDB survey of 801 businesses in 2012, 16% of businesses that were hiring were unable to fill all required positions. The most difficult categories to fill were for semi-skilled or trade workers (common in economies that are in the midst of a modernization process and require new skills) and professional and technical workers.

[50] According to its financial statements, INOFEP had an equity position of nearly US$100 million as of December 2013.

[51] Secondary and Technical Education and Teacher Training Support Program (UR-L1050) and Plan Ceibal II - Support for Primary and Secondary Math and English Education (UR-L1032).

relation to increased enrollment of three-year-olds, and preschool, secondary school, and technical and vocational school, as well as interventions aimed at strengthening the institutional and management tools available to emphasize job training.[52] In this field, access to the formal labor market will also be strengthened through Bank support for implementation of the recently enacted Financial Inclusion Law (Law 19.210), aimed at facilitating access to services currently beyond the reach of the most vulnerable population segment, particularly young people and women.[53]

3.27 Interventions in early childhood education, as well as those associated with Plan Ceibal, carry a low risk because there is political consensus as to their importance and priority status. In contrast, interventions to support secondary education and better management of the system entail a higher risk because there is as yet no consensus from the actors involved. Furthermore, the institutional context of Uruguayan education is complex, characterized by an autonomous National Public Education Administration (ANEP), the agency that guides and manages public education and has the authority to formulate and implement educational policies at the preschool (ages 4 to 5), primary school (ages 6 to 11), and secondary school (ages 12 to 18) levels, as well as with respect to teacher training. This makes implementing any type of action or program a very complex proposition. With regard to job training, the biggest risk is that the institutional weakness of INEFOP, the agency responsible for implementing public policy in this field, will impair its ability to address private sector demand in a timely manner. A related risk is the content of INEFOP's training programs. The Bank can be a strategic partner for the national government and help mitigate these risks by providing technical assistance towards the fulfillment of a common agenda supported by a majority of the country's political actors, as is already occurring in the area of job training.

3.28 **Support for health care reform.** A reform of the Uruguayan health care sector was launched in 2007 with the objective of achieving universal access to comprehensive health care.[54] The model has been highly successful,[55] but there are challenges in terms of the long-term sustainability of efficiency standards, continuous improvement of service quality, and consolidation of a medical care model focused on the first level of care. Low budgetary allocation to primary care[56] and a predominance of medical visits at specialized levels in comparison with primary-level visits are a sign that the primary care level needs to be strengthened from both a technical and a budgetary standpoint. Another major innovation under the reform is the risk-adjusted capitation payment that the National Health Fund (FONASA) transfers to the providers. At present, the capitation value is determined by age and gender and is periodically adjusted for inflationary factors. International experience shows that the progressive inclusion of other factors in adjusting the

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[52] The World Bank has focused on supporting primary education in recent years.

[53] Implementation of this law complements a series of financial regulatory and oversight initiatives that the Bank has been supporting (Program to Strengthen the Financial Services Superintendency, UR-L1052).

[54] The national health system went from having approximately 725,000 members (22% of the population) at the start of the reform to having 2,400,000 members (68% of the population) in 2014.

[55] Out-of-pocket expenses fell from 56.5% in 2006 to 35.5% in 2012 (WHO, 2013).

[56] Of the total ASSE budget, only 12% is allocated to the primary care networks while 30% is allocated to the central level of care ("Sector Note: Health," IDB, 2015).

capitation (e.g., accessibility, disability, socioeconomic level, provider scale) inhibits the creation of inefficiencies because providers with higher-risk populations become defunded and others with lower-risk populations become overfunded.[57]

3.29 The government plan seeks to lock in the achievements made under this reform. It proposes to strengthen stewardship of the system under the leadership of the Ministry of Public Health (MSP); prioritize certain health programs (childhood, noncommunicable chronic diseases, sexual and reproductive health, mental health, accident prevention, dental health); move toward changes in the health care model in line with the demographic and epidemiologic profile of the population, promoting the first level of care and strengthening the Integrated Health Services Networks (RISS); boost the leadership role of the State Health Services Administration (ASSE) and the Integrated Network of Public Health Providers (RIEPS); develop a strategic plan for health care workers; and fine-tune the financing mechanisms that can allow the National Integrated Health System (SNIS) to remain sustainable.

3.30 The Bank's work in the country will focus on supporting the SNIS in strengthening stewardship capacities in the health care sector, with an emphasis on efficiency- and results-based management, and in implementing actions to improve the quality of care. Accordingly, the Bank will support the MSP, the National Board of Health, and the ASSE in strategic areas such as improving information for monitoring the health system, expanding the electronic health record system,[58] perfecting the capitation payment model, and strengthening the first level of care and integrating it with the specialized care levels. In recent years, the Bank has supported the country by helping to improve the quality and efficiency of the health system, primarily through technical cooperation operations[59] the outcomes of which create a basis for designing and implementing the new interventions in these areas.

3.31 In the case of support to the MSP, one risk could be the difficulty of accessing the information needed to carry out a quality diagnostic assessment. However, the commitment of the authorities to strengthen the MSP in its stewardship role is sufficiently strong as to consider this risk to be low. No significant risks are discernible with regard to the support for perfecting the capitation risk adjustment, since the MSP technicians and providers can handle the information involved, and the Bank would be working together with the MSP and the Ministry of Economy and Finance (MEF). With regard to improving the resolution capacity of the first level of ASSE, a potential risk would be a directional change in the institution entailing a shift in strategic priorities in favor of another care model. However, given the consensus around this agenda, the risk is perceived to be low. For all

57 International studies indicate that capitation adjustments based only on age and gender capture a limited percentage of the variability in health expenditures. In the experience of other countries, risk adjustments have also been initially based on these two factors, since they are the most objective factors to measure, but additional risk factors have been incorporated as the systems have been fine-tuned. This has been the path followed by Holland, Germany, Israel, Finland, and Australia; and in the Latin American context, Colombia and Chile are also making some progress in this direction ("Sector Note: Health," IDB, 2015).

58 As of March 2015, 42% of professionals at ASSE's first level of care had made an entry in the electronic health record system ("Sector Note: Health," IDB, 2015).

59 Electronic Health Record System in Public Hospitals in Uruguay (UR-T1091), MIF ATN/ME-10681-UR, and e-Government Management Project in the Health Sector (UR-L1082),

these potential risks, the main mitigation measure would be ongoing technical support from the Bank aimed at providing evidence and better conditions for decision-making.

3.32 **Habitat improvement.** According to census data as of 2011, approximately 15,760 households (1.4% of total households) have a quantitative housing deficit[60] and 42% of households have a qualitative housing deficit (problems with construction materials, lack of water or sanitation, overcrowding). These results show that the main housing problem faced by Uruguayan households is not an insufficient number of housing units but rather the country's housing infrastructure or quality conditions in a broader sense. In addition, the rate of home ownership in Uruguay is lower than would be expected from demographic characteristics and international comparisons, and furthermore there are major inequalities based on income level.[61] The reason for this is that in recent decades, the Uruguayan market has been characterized by a difficulty of access to housing solutions. Both the absence of long-term credit and housing policy issues are contributing factors to this situation, and the result is a stock of lower-quality homes, which has exacerbated the qualitative deficit, as well as demand pressure on the rental market, which creates negative repercussions on household income. Lastly, the sustainable development paradigm has been making inroads in the country's institutional structures, which is where the prospects for resilient housing may lie.[62] Also, Uruguay has vast housing policy experience, which in recent years has focused on diversifying the strategies for addressing housing access. These strategies include actions which, while not specifically identified with resilience, can fit in the framework of this concept and can incorporate instruments for achieving greater sustainability levels and fostering resilience to climate change.

3.33 The government plan consolidates the lines of work pursued over the past 10 years and sets programmatic objectives that include eliminating housing emergency situations; implementing housing and habitat policies targeting all population groups; optimizing intensive use of the housing stock and improving the habitat by creating a better urban infrastructure, including efficient use of energy and water; expanding water and sanitation coverage; and strengthening the public financing system to make housing affordable for low-income groups.

3.34 Continuing the work that the Bank has been doing in the country during the past two decades on improving neighborhoods and access to basic services, primarily

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[60] Quantitative deficit is understood to refer to the volume of habitable housing units that would allow each household to live under its own roof. In other words, it is assumed that every family would like to have its own home and not live together with other families.

[61] Uruguay has one of the lowest home ownership rates in Latin America, the fifth lowest rate in the region after Bolivia, Colombia, the Dominican Republic, and Honduras. Furthermore, the home ownership rate in the top two income quintiles as a proportion of the home ownership rate in the bottom two income quintiles is 172%, well above the equivalent figure in other countries in Latin America, which is less than 130% (OECD, 2014).

[62] Certain elements of this aptitude for resilience could be attained when a home's appropriate orientation is achieved for any given location based on design and when the home is also equipped with, among other things, thermal and insulating materials, energy-efficient lighting, solar energy systems, and efficient water heaters.

water and sanitation,[63] the new country strategy will promote: (i) mechanisms to enhance the development of low-income housing and urban environments; (ii) improvement and revitalization of informal neighborhoods on an integrated basis, considering not only access to services such as water and sanitation but also the public environment and public spaces; (iii) exploring innovative avenues, such as experimentation with resilient housing; (iv) in view of the success of the Goes neighborhood intervention model described in Section II, the Bank will pursue integrated urban initiatives that lead to better use of existing infrastructure in other central areas of Montevideo or other cities; and (v) strategies to improve integrated solid waste management, including cleanup service optimization and adequate final disposal solutions throughout the country.

3.35 The main identified risks are a potential change in government priorities due to the reduced fiscal space and the limited capacity of departmental governments to support processes of change. To mitigate these risks, the Bank will develop a strategy for communicating its own experience in these areas, while also attempting to maintain a dialogue with municipal, departmental, and national sector authorities on the advantages of its implementation.

3.36 **Support for the early childhood and youth segments of the most vulnerable population groups.** The absence of intergenerational equity in Uruguay becomes evident when comparing the rate of poverty for the entire population (9.7% in 2014) with the rate of poverty in children under the age of six (20.4%).[64] This is a result of higher birth rates in the poorest households,[65] leading to a concentration of children in these households: close to 50% of children under the age of six live in households in the lowest quintile. As indicated above, these inequities persist in other stages of life, creating sharp inequalities in terms of completion of education cycles by income level. Moreover, in 2014, the percentage of 15- to 29-year-olds in the lowest income quintile who were functionally disengaged (not attending school or working outside the home) was 22% in the case of men and 41% in the case of women. This gender disparity is basically due to the high percentage of young women who work doing household chores (22% of all 15- to 29-year-old women in the bottom income quintile do not study and only work in the home).

3.37 The national government intends, among other things, to formulate and/or reinforce policies and programs to support specific protection paths, focusing on key stages in the life cycle (childhood, youth, and old age). In this regard, the government has designated policies on early childhood as a national priority for the social sustainability of the country. In addition, the government intends to create a National Integrated Care System (SNIC)[66] aimed at providing care for (temporarily or permanently) dependent population groups, including children, senior adults, and individuals with disabilities, with an especially strong component of social

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[63] First Neighborhood Improvement Loan (UR-L1009), Neighborhood Improvement Program II (UR-L1084), Montevideo Sanitation Programs (UR-L1005 and UR-L1063), Integrated Sanitation Programs for Ciudad de la Costa (UR-L1017, UR-L1075, and UR-L1081), Drainage and Environmental Sanitation (UR-L1069), Ciudad de la Costa-West Area Sanitation Project (UR-L1094).

[64] The indigence rate in 2014 was 0.3% for the total population and 0.9% for children under the age of six.

[65] While the average number of children under 14 years of age in households in the bottom quintile whose heads of household are younger than 50 is 1.7, in the top two quintiles the average is 0.4 (ECH, 2013).

[66] Bill sent to the legislature in March 2015.

assistance services. The understanding is that the growing deficit of care in the country jeopardizes the wellbeing of the population, limits the exercise of rights, and constitutes a factor of inequality insofar as access to care services depends on purchasing power and is based on unpaid work by women.[67] For example, while 95% of three-year-olds from households in the top quintile attend some type of educational center, the equivalent figure in the bottom quintile is just 44%.

3.38 The Bank's country strategy will continue to support the Uruguayan government in its social protection policy based on the universalization of rights under principles of gender equity and equality and diversity. With a view to closing the access gaps for the poorest and most vulnerable groups, the Bank will focus its interventions on early childhood, particularly children 0 to 3 years of age as a window of opportunity for the development of cognitive and socioemotional capacities, and on youth, in both cases within the most vulnerable population groups. To this end, the Bank will support: (i) the creation of a comprehensive early childhood protection system, with an emphasis on building care pathways and defining quality standards in terms of service provision and measurement of results, including steps to mitigate adolescent pregnancies and monitor women from the most vulnerable groups during pregnancy;[68] (ii) expansion and improvement of interventions focused on childrearing guidelines for the care of children 0-24 months of age, and expansion of quality coverage at day care centers for children 24-36 months of age; (iii) improvement of multisector and integrated youth policies and interventions, with an emphasis on quality expansion of specialized programs for adolescents and youth at risk; and (iv) operational launch of the SNIC, with an emphasis on support for the design and regulation of actions, as well as on the production of knowledge on cost-effective service models.

3.39 The multitude of sectors responsible for providing child and youth services and participating in various intersectoral deliberative bodies entails the risk of failure to reach decisions within the required time frames. This risk will be mitigated by attempting to maintain awareness of the agreements with the government and planning support activities in collective settings with the participation of the entities involved to look at progress with implementation. In addition, as in any process of change, there is a risk that it will be difficult for the technical teams to adapt to the new practices and new care protocols that provide for higher quality standards. The Bank's extensive experience in early childhood issues and past support in building care pathways throughout the life cycle (in various countries), as well as the international consensus on the importance of measuring the success of these interventions, are advantages when it comes to holding a sectoral and political dialogue that can lead to agreements for implementation.

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[67] See Bases Programáticas Tercer Gobierno Nacional del Frente Amplio 2015-2020 [Programmatic Bases of the Third Frente Amplio National Government Administration 2015-2020]. The types of child care mentioned in the document include: expanding maternity and paternity leave; universalizing early childhood care, with a focus on coverage for one- and two-year-olds; and universalizing public day care for three-year-olds.

[68] The Bank has been supporting this issue by financing coordination platforms and knowledge development for the formulation, planning, and monitoring of public policies aimed at consolidating the integrated early childhood protection system (UR-T1101).

C. Public sector management

3.40 The Bank will support the country in the process of improving public sector management through: (i) greater efficiency in public institutions; and (ii) strengthening of urban and departmental management.

3.41 The interventions in these priority areas are aligned with the following objectives of the Update to the Bank's Institutional Strategy 2010-2020: create a more redistributive fiscal policy; strengthen the capacity of the State; and establish smart institutional frameworks.

3.42 **Greater efficiency in public institutions.** In the last decade, Uruguay has introduced improvements in public sector management and has had success in mobilizing resources and reducing inequality. However, the relatively high tax ratio (27%)[69] and elevated public spending (over 30% of the GDP) mean that, going forward, any improvements in social indicators will have to come primarily from a more efficient use of already available public resources. Data envelopment analysis studies show that there is room to improve the efficiency of expenditures in sectors that account for the largest share of public spending, such as health and education.[70] In addition, there is room to intensify coordination and management of citizen security policy.[71]

3.43 The objectives of the new administration include achieving modern, effective, and efficient public management. To this end, the proposal is to simplify formalities and enable online processing, and to implement electronic government solutions. In addition, there are plans to strengthen the role of the public offices responsible for evaluating the quality of investment projects and expenditure, and to expand the use of performance indicators and management commitments to the entire public sector, including State-owned enterprises. With regard to citizen security, the national government intends to deepen the organizational reform of the National Police with a focus on knowledge-based management and applied intelligence, develop a new educational curriculum for police training, and consolidate a new management model for correctional institutions.

3.44 Against this backdrop, and relying on the Bank's active portfolio in support of better public sector management,[72] the country strategy will support the strengthening of key institutions that can play a stewardship role in areas such as health, education, budget, the environment and climate change, agriculture, and electronic government, promoting planning, coordination of sector policies, interaction between different levels of government, and results-based management with the core objective of enhancing the efficiency of spending. There are also plans to

[69] In 2013, this ratio was 25.4% in the United States, 20.2% in Chile, and 34.1% on average in the OECD member countries.

[70] See "Sector Note: Strengthening of Public Management and Finances," IDB, 2015.

[71] For example, while 70% of crimes are committed between 6:00 p.m. and 6:00 a.m., Montevideo's 25 police precincts deploy the largest number of police officers between 6:00 a.m. and 2:00 p.m. ("Sector Note: Citizen Security," IDB, 2015).

[72] Program to Support E-Government Management in Uruguay II (UR-L1065), Integrated Local Management Program for Citizen Security (UR-L1062), Institutional Capacity Program for the Ministry of Economy and Finance (UR-L1074), e-Government Management Program in the Health Sector (UR-L1082), Budget Management Strengthening Program (UR-L1098), Program to Modernize Public Financial Management (UR-L1089), Program to Support Agricultural Public Management (UR-L1016).

conduct better monitoring of the performance of State-owned enterprises. With regard to investments, support will continue to be provided for the implementation of a National Public Investment System, which is considered a critically important tool for coordinating and monitoring public investment at both the central and the departmental levels.

3.45 In the area of citizen security, the high costs of insecurity and the cross-sector approach needed to address this problem require a major effort to improve the quality of expenditure and the mechanisms for coordination and leadership of the sector. To this end, the Bank will strengthen the capacity to analyze crime phenomena on a comprehensive and scientific basis and will support the implementation of innovative and cost-effective evidence-based interventions, with an emphasis on police efficiency to reduce the rate of robbery, and a holistic approach to youth violence and violence against women.

3.46 The most significant risks associated with the proposed actions have to do with the natural resistance to change and to reforms in the area of public administration, as well as with certain management capacity weaknesses in the public administration. To mitigate these risks, the projects and support activities to be implemented should include significant change management and training components.

3.47 **Strengthening of urban and departmental management.** Uruguay has undertaken a major decentralization process in recent decades. Since 1996, it has been moving toward greater administrative, fiscal, and political decentralization. However, the challenge involved in this process is to clearly define the functions of the various levels of government. While there is a certain amount of clarity and transparency in how the central government determines the allocation and execution of expenditures, the same cannot be said of the second and third levels of government (departmental and municipal governments), the latter having been created by the Political Decentralization and Citizen Participation Law of 2010. This lack of clarity in assigning responsibility for specific functions becomes more problematic considering that municipios have been established on only a fraction of Uruguayan territory, specifically 20%, covering 71% of the country's total population. In rural areas or towns with fewer than 1,000 residents, less than half of the population is municipalized. An example of the problems that result from the lack of clarity in the definition of roles of the various government levels can be seen in the provision of basic services such as waste management and sanitation.[73]

3.48 The main guidelines of the government plan in this area are to: (i) deepen democracy at all levels of government; (ii) consolidate the institutional frameworks of municipios; (iii) move forward on legal modifications regarding departmental and municipal governments; and (iv) develop regionalization as a line of action that can lead to a more efficient use of resources.

3.49 The Bank will support the Uruguayan government in fostering regional development and fiscally responsible decentralization consistent with the

[73] Responsibilities for the execution and maintenance of sanitation services through conventional networks are clearly assigned: the National Sanitation Works Administration is responsible for providing these services in the country's interior and the Municipality of Montevideo is responsible for the department of Montevideo. However, there is no clear allocation of responsibilities among the various government levels with regard to vacuum truck services. As a result, the provision of these services is uneven across different Uruguayan cities and towns, and there is a great deal of price disparity.

socioeconomic and demographic characteristics of the country's regions. It will do so by providing technical support for the definition of powers, responsibilities, and fiscal regulations of the various government levels, as well as by helping to build subnational government capacities in areas such as fiscal management, waste handling and management, urban transportation, rural roads, housing, and sanitation services, coordinating with the relevant State-owned enterprises as appropriate. The interventions will be supported by the Bank's experience in Uruguay in this area.[74]

3.50 Decentralization processes are complex political and economic processes that require agreements between multiple sectors of society. In the particular case of Uruguay, any change in the transfers or powers of departmental governments must be preceded by a series of consensuses. As a mitigation measure, the strategy calls for supporting the Office of Planning and Budget (OPP)[75] to reinforce the technical arguments in favor of an efficient and effective decentralization, while taking fiscal and management sustainability considerations into account. In the area of provision of services to the population, actions would also be coordinated with the relevant national entities.

D. Crosscutting areas of action

3.51 **Gender equality.** Given the aforementioned gender equality gaps,[76] the Bank will pay particularly close attention to gender issues in interventions aimed at strengthening of human capital and employability, habitat improvement, support for the early childhood and youth segments of the most vulnerable population groups, and implementation of the National Integrated Care System (SNIC), whose actions will have an impact in terms of reducing gender inequalities. In the particular case of violence against women,[77] the Bank's support will be aimed at, among other things, strengthening the institutional capacities to improve interagency coordination, simplifying grievance procedures and other formalities, and providing a broader public array of victim support and offender treatment services. In addition, the Bank will support activities to disseminate information and raise social awareness about this issue.

3.52 **Climate change.** With an urban population highly concentrated along the country's 680-km coastline, Uruguay is very vulnerable to the impacts of climate change. In addition, it is estimated that the long-term impact of climate change will be adverse for the main sectors of the economy (agriculture, energy, and tourism), especially considering that the country is experiencing extreme events of growing intensity. In

[74] Subnational Development and Management Program (UR-L1038).

[75] The Uruguayan Constitution assigns OPP the responsibility of assisting the executive branch in formulating development plans and programs, as well as planning decentralization policies.

[76] Higher female unemployment rates and greater proportion of individuals not attending school or working outside the home among women in the poorest population groups. In addition, the gender equality index prepared by the World Economic Forum (2014) ranks Uruguay in 82nd place among 142 countries, one of the worst rankings in Latin America. The worst subindex is that of political empowerment, where the country is ranked in 112th place.

[77] The data show that 69% of women above the age of 15 have experienced gender-based violence of some sort (psychological, economic, sexual, or physical) at some point in their lives, and that close to one out of every two women who have been in a relationship have experienced domestic violence from their partner or ex-partner at some point in their lives (2013 National Survey on the Prevalence of Gender-based and Generational Violence).

this context, climate change adaptation and mitigation elements will be incorporated into initiatives aimed at fostering innovation, developing a policy for participation in the global economy, improving productive infrastructure, improving habitat, and developing better public sector management. These elements include investing in climate-resilient infrastructure in transportation, energy, and housing, promoting renewable energy, and reducing the vulnerability of sectors affected by climate. With regard to the sustainable management of natural resources and climate change, the Bank's support will target the development of multisector strategies, providing an integrative vision aimed at protecting the various sectors involved. The strategies include short-term steps to alleviate the most urgent needs (such as those arising from droughts or floods), as well as medium-term measures such as the development of plans for sustainable management of natural resources. In addition, special emphasis will be given to greater water security[78] by promoting integrated water resources management at the national level through various strategies and programs. In particular, in the near term, the Bank will promote actions in watersheds aimed primarily at the provision of water for human consumption and the continuation of irrigation development projects.

IV. LENDING FRAMEWORK

4.1 The nonfinancial public sector financing needs for the 2016-2020 period are projected at US$13.179 billion. The Bank anticipates SG approvals of approximately US$1.8 billion for the country strategy period, with a larger share of approvals in the first years of the period. These approvals include a significant proportion of investment loans, as well as a balanced combination of PBLs with and without a deferred drawdown option (see Annex IV).

4.2 Under this scenario, total disbursements for the 2016-2020 period are estimated at US$1.309 billion, with an average of US$101 million in annual net flows. Thus, Uruguay's debt with the Bank over this period would on average be roughly equivalent to 3.6% of GDP and about 5.4% of total public debt.

V. COUNTRY STRATEGY IMPLEMENTATION

5.1 **Consolidation of institutional capacity.** Uruguay has stood out for its reasonable levels of institutional legitimacy and stability, transparency, and low perceived corruption. The World Bank's governance indicators place Uruguay among the highest-ranked countries in Latin America. Since there are no major challenges in issues of integrity, the associated risks are low. With respect to the preceding five-year period, the following milestones are notable: (i) partial implementation of results-based management, particularly in relation to the budget cycle; (ii) creation of a new Integrated Financial Information System (SIIF) incorporating technological and functional changes; (iii) creation of a Superintendency of the National Internal Audit Office for the public sector; (iv) preparation of a strategic development plan for the Tribunal de Cuentas de la República [State Audit Office], and procurement and implementation of an Integrated Audit Control System (SICA) and an audit

[78] Conservation of water resources in terms of both quantity and quality. The Bank has been supporting this issue through the technical cooperation operation UR-T1076, "Plan for Integrated Water Resources Management (IWRM) Adaptation to Climate Change in Uruguay".

manual; (v) introduction of a modern legal framework for public procurement and creation of the State Procurement Agency (ACCE); (vi) and implementation of a government procurement portal and the master registry of providers (RUPE).

5.2 As a result of this institutional capacity, Bank portfolio projects have generally been executed satisfactorily, having achieved their respective objectives without requiring significant changes or extensions.

5.3 **Operational implementation modality.** The operational programming actions to be implemented by the Bank during the country strategy period will include a balanced combination of investment instruments and unrestricted funds. The Uruguayan government's requests for unrestricted funds will be considered in the financial contribution sequence set forth in Annex IV. In addition, the Bank will seek flexibility in the use of the financial instruments available to ensure that they are adapted as well as possible to the characteristics and needs of the interventions to be supported, taking into account the demand for results-based project disbursements. It should be noted that following approval of the Update to the Institutional Strategy, the Bank has created a working group to conduct an institution-wide analysis of the currently available set of financing instruments.

5.4 **Use of country systems.** The use of financial management and control (budget, accounting, treasury, internal audit, and external control) subsystems has grown in recent years and is projected to reach 65% by the end of the 2010-2015 period. Ongoing support is being provided for the development of financial management systems, primarily increased use of the national accounting system through greater incorporation of the SIIF's accounting module in projects with external financing and validation of other systems that do not go through the central government administration. With regard to the government procurement system, the information system is being used, along with shopping (as an abbreviated bidding method). Once the results of the MAPS (Methodology for Assessing Procurement Systems) diagnostic assessment are made available, which will occur in 2015, an action plan will be implemented that looks for opportunities to improve the system with a view to consolidating a broader agenda for use of the other subsystems (individual consulting and national competitive bidding).

5.5 **Lessons learned.** Worth noting is the positive experience of capitalizing on the synergies arising from public- and private-sector window collaboration to develop an operational relationship with private sector clients. The most salient example is in the field of renewable energy, where this collaboration has led to significant growth in the level of business activity related to wind and solar energy. The incorporation of these new technologies, aside from helping to diversify the country's energy matrix, has made it possible to advance in the area of innovation by creating new providers of wind and solar generators. As an additional benefit, this collaboration has consolidated a public-private participation approach to a vital service such as electricity. This will undoubtedly be treated as a successful public-private precedent, to be replicated in other sectors, such as the road sector.

5.6 A second lesson is also related to the operational boost derived from cross-sector and interagency collaboration. In this regard, three cases are worthy of note: (i) the urban renovation intervention in the Goes neighborhood, described above; (ii) scaling of support for entrepreneurship development through technical support for strengthening the business incubator at the Laboratorio Tecnológico de

Uruguay [Technology Laboratory of Uruguay] and the creation of Programa Emprender, which has provided technical support for developing business plans as well as seed capital for businesses with growth potential, leading to the inclusion of entrepreneurship support as public policy by the ANII as crystallized in the Program to Support Future Entrepreneurs; and (iii) development of electronic health records in support of the Federación Médica del Interior [Inland Medical Federation] for deployment in its network of hospitals and clinics, and a pilot test at two ASSE hospitals, then scaled to other hospitals, culminating in the public policy reflected in the e-Government Management Program in the Health Sector, aimed at implementing a platform extending to the entire sector, including mutual entities. This coordination effort was crowned by the creation of the Regional Network for the Development of Electronic Health Records, in which Uruguay is a founding member and promoter.

5.7 In this context, it has been identified as important for the Bank to examine a possible systematization of information on this type of experience in order to strengthen the Bank's programmatic and operational work, particularly in the design of new programs, thus generating lessons for the country as well as for the region in general. In the context of project preparation, special attention will be paid to the monitoring and evaluation arrangements and methods to be used, with a view to assuring the quality of the information that is to serve as the basis for such evaluation.

5.8 **"Two-way" knowledge transfer.** Uruguay is important for the Bank not only as a partner for development but also as a provider of knowledge and experience to the rest of the region. Accordingly, the Bank will support the implementation of South-South projects, channeling the public policy knowledge and experience acquired by the country to the rest of the region.[79] In addition, given the characteristics of Uruguay as a small, middle-income country, it may be important for the Bank to support projects that incorporate experiences from outside the region, for example in the areas of technological development and domestic violence. In this context, the Bank will design a country-specific knowledge agenda with the Uruguayan government and other key local sectors, consolidating implementation mechanisms such as the local knowledge networks and including mechanisms aimed at systematizing the outcomes achieved as a result of the Bank's work in the country.

5.9 **Private sector.** The plan is to continue to increase the number and amount of NSG operations. The synergies, additionality on innovation issues, and complementarity between public sector and private sector projects will be essential for creating a greater impact on the development of IDB Group interventions in the coming years, particularly in fostering the use of public-private partnerships in transportation and energy infrastructure. The support of NSG operations will be of key importance in promoting credit access for businesses and capital market growth, as well as in continuing to support the production and export sectors so as to achieve greater efficiency and productivity and development of value chains.

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[79] The Uruguayan International Cooperation Agency (AUCI) has in recent years vigorously promoted a South-South cooperation strategy that has included various initiatives with Bank support through CT/INTRA, the Regional Public Goods Program, and exchange missions between countries in the region and Uruguay.

Similarly, this support can be extended to new areas such as habitat and health improvement.

5.10 **Donor coordination.** The IDB maintains ongoing relationships with the main multilateral and bilateral agencies active in Uruguay. From a sector standpoint, it is worth noting the joint work carried out in areas such as citizen security, education, and neighborhood improvement. The Bank has led bilateral and multilateral lending in Uruguay, acting as a catalyst (e.g., channeling grants for electronic health records with funds from Japan), leveraging projects through co-financing (for example, Ciudad de la Costa sanitation and Punta del Tigre combined-cycle gas plant jointly with CAF and other agencies, and an innovation program jointly with the China Cofinancing Fund),[80] and acting in coordinated fashion to maximize the efficient allocation of resources (e.g., in education, the Bank focuses on early and secondary education while the World Bank focuses on primary education). The Bank will continue to maintain these relationships, with the concomitant opportunities to act as catalyst in the above-indicated areas, and will deepen its coordination arrangements with CAF in areas of infrastructure such as energy, transportation, and water and sanitation.

VI. RISKS

6.1 **Macroeconomic risks.** The country has been characterized by its robust macroeconomic performance and has reinforced its resistance to external shocks.[81] However, some vulnerability factors persist in the Uruguayan economy. The main macroeconomic risks are associated with the future path of the region's economy, which coupled with slower growth in China could dampen both exports and foreign investment in Uruguay. In addition, a further decline in commodity prices or an increase in interest rates in the United States could adversely impact growth in the coming years. In any of these scenarios, the country has the financial soundness and external liquidity levels needed to cover its short-term payment obligations to external creditors. However, there is a certain degree of uncertainty as to how this may affect the central government's financing needs and, consequently, the Bank's financing in the coming years. Accordingly, greater use of fast-disbursing funds (PBLs) is a possibility. The Bank will conduct periodic monitoring of the macroeconomic situation through the macroeconomic safeguards framework.

6.2 **Implementation risks.** The new government administration has identified a reform agenda that includes changes in the educational system, institutional changes,[82] and a deeper health sector reform. There is a risk that, given the size and the political and institutional complexity of these initiatives, the difficulty in implementing them will affect the Bank's program in those areas. In this regard, the country strategy and the interventions it calls for are designed to be consistent with the government agenda and acknowledge the importance of having flexible

[80] UR-L1094, UR-L1070, and UR-L1096.

[81] The Uruguayan government has been active in managing debt, reducing the degree of debt dollarization and extending its maturity profile. In addition, the government has accumulated liquid assets and has secured contingent lines of credit to address global financial market shocks. The BCU has raised its level of reserves, which should enable it to cover a large part of its annual foreign currency needs.

[82] For example, by creating the National Competitiveness System.

programs that can be adjusted to reflect potential changes in the government's needs and requirements. At the same time, as indicated in Section III, the Bank will provide technical support and dialogue with the authorities to accompany any required monitoring and mitigation action.

MAIN SOCIAL AND ECONOMIC INDICATORS

	2010	2011	2012	2013	2014
Real GDP growth (%)	7.8	5.2	3.3	5.1	3.5
GDP (US$ billions)	40.285	47.962	51.385	57.525	57.461
Per capita GDP (US$)	11,860	14,054	14,997	16,722	16,638
Per capita GDP (US$ PPP)	16,235	17,723	18,638	19,679	20,262
Gross capital formation (% GDP)	19.9	19.3	22.7	22.9	21.5
National savings (% GDP)	17.0	18.2	18.2	18.3	17.3
Unemployment rate (%)	7.0	6.3	6.3	6.5	6.5
Inflation (%)	6.9	8.6	7.5	8.5	8.3
Exchange rate (Ur$/US$)*	19.9	20.0	19.2	21.5	24.3
Real effective exchange rate** (January 2006=100)	94.0	92.4	86.4	86.8	94.8
Current account (% GDP)	(1.8)	(2.9)	(5.2)	(5.2)	(4.6)
Balance of trade (% GDP)	1.6	0.2	(2.5)	(2.1)	(1.3)
Financial and capital account (% GDP)	2.6	8.7	12.2	8.1	6.7
Foreign direct investment (% GDP)	5.8	5.2	4.9	5.3	4.8
NFPS overall balance	(0.4)	(0.4)	(2.4)	(1.9)	(2.7)
NFPS primary balance	2.0	2.0	(0.1)	0.5	(0.4)
Public sector overall balance (% GDP)	(1.1)	(0.9)	(2.7)	(2.3)	(3.3)
Public sector primary balance (% GDP)	1.9	1.9	(0.2)	0.4	(0.5)
NFPS debt (% GDP)	44.2	43.4	45.6	41.5	42.7
Consolidated public sector debt (% GDP)	59.3	56.3	60.6	57.6	58.5
International reserves (US$ billions)	7.656	10.302	13.605	16.281	17.555
Population (millions)	3.40	3.41	3.43	3.44	3.45
Poverty (% total population)	18.5	13.7	12.4	11.5	9.7
Extreme poverty (% total population)	1.1	0.5	0.5	0.5	0.3
Gini coefficient	0.43	0.40	0.38	0.38	0.38

* December
** Adjusted by the CPI of Argentina

MACROECONOMIC AND SOCIAL CONTEXT

1. **Since 2003, the Uruguayan economy has posted twelve years of growth, averaging 5.0% per year from 2003 to 2014.** This growth is due in large part to a higher labor force participation rate and high investment levels, which made a positive contribution to physical and human capital growth. At the same time, the favorable performance of productivity also helped drive economic growth.

2. **In 2014, GDP grew 3.5% and per capita GDP reached US$16,640, one of the highest levels in Latin America.** However, the economy has slowed in recent years, and forecasts for 2015-2016 point to growth rates ranging from 2% to 2.5%. This expected weakening comes on slower growth in the economies of important trading partners such as Argentina, Brazil, and China, appreciation of the bilateral exchange rate with Brazil, a decline in commodity prices, and a more restrictive monetary policy.

3. **Reducing the inflation rate is one of the main macroeconomic policy challenges.** The annual inflation rate was 8.3% in 2014. Inflation has been exceeding the upper limit of the BCU target range (3%-7%) since 2011. Low unemployment together with real wage growth in a context of indexed wages could partially explain the rise in consumer prices. Inflation expectations for 2015 remain stable but high (9%).

4. **The fiscal deficit posted in 2014 was 3.5% of GDP.** This represented a deterioration of 1.2 percentage points with respect to 2013 and was the largest deficit recorded since the 2002 crisis. This deterioration of the fiscal accounts is primarily due to an increase in current expenditures, with investments remaining practically unchanged.

5. **Despite a certain degree of deterioration in public finances in the last year, the country has adequate debt sustainability indicators and manageable financing needs.** Total consolidated public sector debt at year-end 2014 was 58% of GDP, while net debt was 21% of GDP, the lowest level in 15 years. In addition, the profile of Uruguay's public debt has improved in recent years as a result of the implementation of an appropriate debt management strategy. The authorities have succeeded in improving the profile of liabilities, reducing the proportion of debt denominated in foreign currency to 47% of total central government debt and extending the average maturity to 15 years. At present, Uruguay has investment grade status among the major rating agencies.

6. **The central government is well positioned to weather a shutdown of the international credit markets.** It has contingent lines of credit with multilateral institutions for approximately US$2.167 billion (IDB: US$550 million). In addition, as of October 2015, the central government had liquid assets equivalent to 6.4% of GDP. These resources should be sufficient to cover all debt amortization and interest payments by the central government scheduled for 2016.

7. **The current account deficit contracted in 2014 after expanding in 2013.** The current account deficit in 2014 was 4.6% of GDP, lower than in 2013 (5.2%). In part, the high deficit recorded in the last two years reflects higher imports of capital goods associated with a new pulp mill (Montes del Plata) and a weaker

balance of services due to lower tourism revenues, particularly from Argentina, and a rise in outbound tourism.

8. **Capital inflows weaken.** Capital inflows represented 6.9% of GDP in 2014, after having reached 10.3% of GDP in 2013. Nonetheless, FDI remains at the level of previous years (4.8% of GDP) and accounts for over half of capital inflows. It may be said that capital inflows have not experienced any major reversals despite the changes in the international context.

9. **International reserves at the BCU currently represent 30% of GDP.** In addition to financing the current account deficit, the capital inflows have made it possible to accumulate a high level of reserve assets. The current reserves balance would be sufficient to cover slightly more than one year of imports or the short-term liabilities and current account balance.

10. **The incidence of poverty in 2014 was 9.7% of the country's total population, 0.8 percentage points less than one year earlier.** The indigence rate was 0.3% of the country's total population. At the same time, there was an observable reduction in inequality as measured by the Gini coefficient, which in 2014 was estimated at 38.1. The government's assistance plans, and especially the robust performance of the labor market, have lifted thousands of people out of poverty in recent years. Moreover, these factors, together with the reforms implemented in the health and tax systems, led to an improvement in the distribution of wealth.

11. **Poverty primarily affects the youngest members of the population, and school-age children in particular.** In 2014, 19% of children under the age of 12 lived below the poverty line. Moreover, poverty is primarily urban. There is a greater proportion of people living in poverty in Montevideo (13%) and in towns with fewer than 5,000 inhabitants (9%) than in the countryside (3%).

12. **The unemployment rate remains close to historic lows, averaging 6.6% in 2014.** However, high unemployment rates persist among young people under 25 years of age (19%). This problem is even more pronounced in the case of women, with an unemployment rate of 24% in the same cohort.

13. **Among young people, the school attrition rate is high and not improving**. Among 15- to 17-year-olds, 79% report attending an educational institution, while among 18- to 24-year-olds, the percentage is 38%. Socioeconomic inequalities are significant, showing that the school attrition process begins earlier among those from lower-income households. While 66% of 15- to 17-year-olds from the lowest income quintile attend an educational institution, the percentage is 97% for the equivalent cohort from the highest income quintile.

MAIN RESULTS IN THE FRAMEWORK OF THE COUNTRY STRATEGY 2010-2015

The main results include the following:[83]

1. Transport

(i) Improvement of the port infrastructure through the construction of a new jetty in the port of Montevideo, resulting in a 12% increase in berth space.

2. Energy

(ii) Financing of a combined-cycle natural gas plant that will help expand electricity supply capacity by 530 MW;

(iii) Increase in power generation capacity through the financing of six energy development programs using renewable energy (420 MW).

3. Water, sanitation, and solid waste

(iv) Expansion of sanitation coverage in the metropolitan area, benefitting 50,000 inhabitants;

(v) Support in preparing Uruguay's first national plan for integrated management of water resources;

(vi) Increase in water supply for rural communities, with service newly provided to 4,283 households.

4. Science and technology

(vii) Increase in private investment in research and development through the financing of 210 SME innovation projects, 33 projects to generate and strengthen scientific and technological services for SMEs, and 54 strategic innovation projects;

(viii) Health management improvements, with nine public and private health institutions adopting the use of electronic health records;

(ix) Creation of new jobs through help in creating over 100 enterprises, strengthening over 140 enterprises through mentorships, training, or some type of technical assistance, and providing access to credit to 34 new enterprises.

5. Social protection

(x) Support for improving the living conditions of the most vulnerable population groups, such as children and adolescents, through access to a basic package of

[83] Includes results achieved during the 2010-2015 period from the portfolio in execution as well as expected results from approvals obtained during this strategy period.

social services for 64.6% of vulnerable households with members under 18 years of age, and formulation of a strategic early childhood plan for 2015-2020.

6. Education and job training

(xi) Improvements in secondary school infrastructure and teacher training, with 306 secondary school classrooms built and equipped, and 2,125 secondary school teachers and 740 secondary school principals trained in working with adolescents and youth;

(xii) Expanded use of new technologies in schools as promoted by the Ceibal Plan, with the result that 100% of basic-cycle secondary school students have laptops and their schools have computer equipment.

7. Agribusiness

(xi) Strengthening of the agribusiness sector through greater use of technology in the sector, resulting in 100% of the national herd identified and registered in the Animal Identification and Registration System, which ensures the traceability of cattle in Uruguay;

(xii) Greater diversification of the export sector through: (i) construction of a new pulp mill and associated ports, including Uruguay's largest biomass-fired power plant, which entailed the largest private investment in the country's history and contributes approximately US$700 million in additional annual exports; and (ii) development of an integrated dairy project with US$65 million in expected annual exports, including a system of free-stall dairy facilities and a powdered milk plant, as well as thermal energy generation from biogas;

(xiii) Greater use of technology in the sector, with 2,861 small rural producers adopting the use of new technologies.

8. Service exports

(xiii) Increase in services exports through: tailored training programs (finishing schools) for 60 service-exporting companies, reaching 2,029 individuals; international promotion actions, with 52 events abroad and 19 events in Uruguay; tourism promotion, focusing on alternatives to sun and sand destinations.

9. Public management and finance

(xiv) Improvements in central government management, resulting in lower VAT evasion and in numerous advances in electronic government, including use of electronic recordkeeping systems by 17 agencies and the ability of citizens to complete 74 government transactions at least partially online;

(xv) Creation of a legal and regulatory framework for public-private partnerships.

10. Urban development and security

(xvi) Improvement in the living conditions of the urban population through the provision of basic infrastructure and community facilities for 20 informal neighborhoods;

(xvii) Improvements in citizen security through the implementation of a solution-oriented community policing model in three precincts, training for 500 police officers with the support of world-class academic centers, and provision of crime-prediction software for intelligent preventive policing.

INDICATIVE FINANCING FRAMEWORK[84]

Nonfinancial Public Sector Financing Needs (US$ millions)

	2015p	2016p	2017p	2018p	2019p	2020p	Total 2016-2020	Average 2016-2020
USES	**3,775**	**2,420**	**3,100**	**3,006**	**3,465**	**3,429**	**15,419**	**3,084**
Interest payments	1,237	1,222	1,285	1,340	1,414	1,486	6,748	1,350
Amortizations	2,538	1,197	1,814	1,666	2,051	1,943	8,671	1,734
SOURCES	**3,775**	**2,420**	**3,100**	**3,006**	**3,465**	**3,429**	**15,419**	**3,084**
Primary balance	-54	106	268	448	699	720	2,241	448
Multilateral disbursements	241	274	395	591	504	385	2,149	430
IDB	*126*	*143*	*207*	*309*	*264*	*201*	*1,123*	*225*
Debt issues in local or international markets*	4,200	1,800	2,200	1,700	2,000	2,100	9,800	1,960
Use of assets (reduction of reserves)	-800	200	200	200	200	200	1,000	200
Other	*188*	*40*	*36*	*67*	*62*	*24*	*229*	*46*
FINANCING NEEDS	**3,829**	**2,314**	**2,832**	**2,558**	**2,766**	**2,709**	**13,179**	**2,636**
(as % GDP)	**7.0%**	**4.4%**	**5.3%**	**4.6%**	**4.7%**	**4.5%**	**4.7%**	**4.7%**

Figures estimated by the authors based on IDB, MEF, BCU, and IMF

* Includes bank debt of State-owned enterprises.

Projected Sovereign Guaranteed Debt Flows and Rations for the Total Public Sector

	2014	2015p[2]	2016p	2017p[3]	2018p	2019p	2020p	Total country strategy 2016-2020p	Average 2016-2020p
Approvals (US$ millions) [1]	393	608	382	500	260	210	198	1,800[2]	
a. Loan disbursements to the TPS (US$ millions)	166	167	204	272	329	284	221	1,309	262
b. Repayment of principal (US$ millions)	99	111	122	138	178	181	184	802	160
c. Net flow of loans to the TPS (a-b) (US$ millions)	67	56	81	134	151	103	37	507	101
d. Interest and fees (US$ millions)	64	63	59	57	53	54	57	281	56
e. Net cash flow (c-d) (US$ millions)	3	-7	22	77	98	49	-20	225	45
TPS debt with the IDB									
US$ billions	1,651	1,707	1,788	1,922	2,073	2,176	2,213		2,035
% TPS multilateral debt	50%	52%	51%	51%	51%	51%	51%		51%
% TPS debt	4.9%	4.8%	4.9%	5.2%	5.5%	5.7%	5.7%		5.4%
% GDP	2.9%	3.1%	3.4%	3.6%	3.7%	3.7%	3.7%		3.6%
TPS multilateral debt/TPS gross debt	10%	9%	10%	10%	11%	11%	11%		11%
TPS multilateral debt/TPS external debt	17%	19%	21%	22%	22%	23%	22%		22%
TPS gross debt/GDP	58%	65%	69%	69%	67%	66%	65%		67%

Note: The flow of funds table does not take loans to the private sector into consideration.

TPS = Total public sector

(1) The annual approval amounts are indicative and subject to availability of Bank resources.

(2) As part of the approvals for 2015, US$250 million is expected to be approved in December under the country strategy for 2016-2020.

(3) As part of the approvals for 2017, approval is expected for a US$250 million PBL, which would presumably be disbursed in 2018 and 2019.

Sources:

Approvals and disbursements of SG operations: estimates based on a preliminary dialogue with the country.

IDB debt and net flows: IDB Finance Department/Finance Data Mart, and authors' own calculations.

IDB/multilateral debt is assumed to remain constant during the strategy period.

Total public debt: projections developed by the authors based on estimates of financing needs.

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84 The first table refers to the nonfinancial public sector (NFPS), and the second refers to the total public sector (TPS).

COMMENTS ON THE COUNTRY PROGRAM EVALUATION FOR URUGUAY 2010-2015

OVE's recommendations in the CPE	Management's response	Incorporation into the country strategy 2016-2020
Recommendation 1: Increase the multisector focus of the country strategy and the Bank's program in general. The country is making efforts to adopt this focus in such areas as competitiveness and social policy. In this regard, the Bank should structure the new strategy, and ultimately its operations and analytic work, around crosscutting issues that leverage possible synergies among different sectors of the Bank.	**Agree.** Bank Management is updating the current country strategy guidelines to replace those now in force, which were approved by the Board of Executive Directors in 2009 (document GN-2468-6). The update will address recommendations made by the Board of Executive Directors, clients, OVE, and Management, including the importance of offering an integrated vision (multisector and crosscutting) to address development challenges, which means moving away from segmented visions through individualized sectors. Management will submit the proposal to update the country strategy guidelines to the Board of Executive Directors in the fourth quarter of 2015. Currently, four country strategies are being prepared under this new focus (BO, BR, CO, JA) and will be submitted to the Board of Executive Directors for consideration in 2015 and 2016. However, the country strategy with Uruguay 2016-2020 is not part of these pilots, and so is being prepared under the current country strategy guidelines. Regardless, the new strategy will be conceived and designed around three major areas of strategic focus, to be implemented through multisector focuses that will necessarily involve crosscutting issues, particularly in the areas of competitiveness and social policy being promoted by the government. This multisector, crosscutting focus will leverage synergies among the different areas and sectors in both the public and private sector windows of the Bank.	See Section III, on Priority Areas, which sets out three strategic pillars that will steer operational activity and promote a crosscutting multisector focus in the Bank's work in Uruguay.
Recommendation 2: Balance the need for contingent financing with investment and technical assistance. To implement this recommendation, the Bank could consider: (i) developing parameters that help define the makeup of the lending envelope (contingent and investment resources), to respond more effectively and efficiently to the country's needs. For this, the strategy should also incorporate different lending scenarios allowing flexibility based on the management of	**Agree.** During dialogue for preparation of the new country strategy, the Bank has made it clear to the Uruguayan authorities that a balance needs to be maintained between the need for contingent financing and the need for investment in development projects in programming. Analysis of regional and global economic conditions and how they could affect the Uruguayan economy indicate that the greatest risks may arise during the first two years of implementation of the new strategy. As such, the Bank has reached preliminary agreement with the government on a front-loaded operations program that would mix contingent financing with investment operations during the first two years. Moreover, hybrid instruments may be introduced over the course of the period for the design of operations to address the country's needs more efficiently and	See Section IV, on the Financing Framework, and Annex IV and paragraph 5.3. The eventual definition of parameters will require an institution-wide analysis, which is beyond the scope of this country strategy.

OVE's recommendations in the CPE	Management's response	Incorporation into the country strategy 2016-2020
program and country risks; and (ii) using contingent financing supplemented with investment and technical assistance, for example through hybrid lending instruments, in areas where a role can be played in catalyzing reforms.	effectively. This approach to determining the lending envelope (front-loading and loans with deferred disbursement option) takes the possibility of a crisis setting into account, so alternative scenarios were not considered necessary in this instance, on the understanding that the relevant risks of the program and the country are adequately addressed.	
Recommendation 3: **Deepen the analysis and cost estimates for infrastructure projects.** The Bank could consider supporting the country through: (i) deeper and more detailed analysis of the estimated costs of works prior to tenders in order to minimize **design problems**; and (ii) the systematic incorporation of the possible impact of **exogenous variables** such as the exchange rate and price of inputs in their cost estimate models.	**Agree.** OVE's point about cost overruns on several infrastructure projects and the need to address this issue through better analysis in the design of this type of projects is well taken. To address this, the Infrastructure and Environment Sector (INE) is already using a cost estimate methodology developed specifically for infrastructure projects that factors in price and exchange rate fluctuation, as well as endogenous variables analyzed in the historical context of similar Bank-financed projects executed by the contracting institution. The methodology has already been used in the rural roads program in Paraguay, the highway program in São Paulo, and basic sanitation and urban transportation programs in Uruguay.	Aside from its institution-wide implications, this recommendation is already being implemented in the relevant programs in Uruguay.
Recommendation 4: **Design a knowledge strategy with the country.** Explore lending mechanisms to support the design of an agreed strategy with the government that contains at least two major lines of work: (i) an advanced, prospective knowledge agenda specific to the new and complex issues Uruguay faces as an upper-middle-income country, to offer the country attractive solutions and products; (ii) an agenda to systematically capture and document the outcomes and lessons of lending and technical assistance operations (e.g., evaluations of innovative pilots), in order to learn lessons for the country and the region as a whole.	**Agree.** Two-way knowledge transfer activities are being considered as part of implementation of the new country strategy for 2016-2020, given Uruguay's importance for the Bank not only as a development partner but as a provider of knowledge and know-how for the rest of the region. Thus, the Bank will support the implementation of South-South cooperation projects, to channel that knowledge and experience in public policy and best practices toward the rest of the region. The Bank has been working with the Agencia Uruguaya de Cooperación Internacional [Uruguayan International Cooperation Agency] (AUCI) for the past few years on a South-South cooperation strategy through several different initiatives financed through CT/INTRA and the Regional Public Goods Program. The Bank also plans to support Uruguay, as a small, middle-income country, through activities/projects that incorporate know-how from outside the region, such as in the areas of technological development, elder care, and domestic violence. The work to prepare the country strategy for 2016-2020 has yielded a substantial store of knowledge that will lay the foundation for developing an important agenda for the pooling of experience with the authorities during that time. Building on this will be the	See paragraphs 5.7 and 5.8.

OVE's recommendations in the CPE	Management's response	Incorporation into the country strategy 2016-2020
	promotion of local development networks to strengthen linkages with academia, the private sector, and local civil society in different areas of specialization such as local development, innovation, citizen security, and social safety nets.	
Recommendation 5: **Explore the use and development of new lending and financial instruments tailored to the country's specific needs that allow its debt strategy to be supported and that reduce the transaction costs for the Bank and the country.** The options to explore include, for example: (i) deepening the use of programmatic lending instruments; (ii) a new results-based lending instrument; (iii) an "umbrella" lending instrument, for example, to support various institutions in a common thematic area (e.g., institution-strengthening); (iv) innovative financial instruments (e.g., swaps, insurance, local currency financing).	**Agree.** During implementation of the new country strategy for 2016-2020, special attention will be paid to the identification of lending instruments to finance the agreed operations programs, so that they can best address the specific features of the operations and the country's needs in terms of flexibility, rapid response, and lower transaction costs. The range of instruments to be used will include not only new instruments created as a result of institutional decision-making through consultation and approval by the Board of Executive Directors, but current instruments (investment loans of various types, policy-based loans, hybrid, guarantees, etc.) under lending arrangements such as conditional credit lines for investment projects (CCLIPs), programmatic loans, swaps, etc.	See paragraph 5.3, although the institution-wide implications of this recommendation are beyond the scope of this country strategy.
Recommendation 6: **Move in the direction of greater flexibility in the annual programming process.** Explore new mechanisms for progress toward a multiyear or ongoing operations programming process, in order to make annual allocations and operation design more predictable in Uruguay, and more in line with the country's multiyear budget.	**Agree.** Management is fully aware of the Bank's need to be able to conduct multiyear programming processes, particularly in countries like Uruguay that approve five-year budgets. Such programming would be more predictable and flexible, particularly for new governments taking office. VPC has no objection to moving toward a multiyear allocation of resources. However, this entails substantial changes in the Bank's current policies on financial resource management. In particular, it would require amendment of the Income Management Model (IMM) and the Long-term Financial Projections (LTFP). At any rate, this has less to do with the specific case of Uruguay, and more with an institutional change to be proposed by Management under the right circumstances and approved by the Board of Executive Directors.	This is a recommendation of institution-wide application that would require an analysis that is beyond the scope of this country strategy.

COUNTRY STRATEGY: DEVELOPMENT EFFECTIVENESS MATRIX

In August 2008, the Board of Directors approved the Development Effectiveness Framework (document GN-2489) to increase the evaluability of all Bank development products.
The Development Effectiveness Matrix for Country Strategies (DEM-CS) is a checklist of the elements that are necessary to evaluate a country strategy. It is based on the evaluation criteria developed by the Evaluation Cooperation Group of the Multilateral Development Banks in the "Good Practice Standards for Country Strategy and Program Evaluation."

COUNTRY STRATEGY:

STRATEGIC ALIGNMENT *(measures two dimensions: (i) the degree of consistency between the strategy objectives and the country's development challenges, on one hand, and the government priorities and plans, on the other; and (ii) the use of a blend of products (financial, knowledge, and technical assistance) to attain the proposed objectives and identify other donor agencies and their areas of action):*

Consistency with strategic objectives: The country strategy proposes working in priority areas around three strategic pillars: (i) improve productivity and competitiveness by promoting innovation, improving productive infrastructure, and supporting an integrated and coordinated policy for international positioning; (ii) promote equity and social inclusion by strengthening the human capital and the employability of the population, supporting health care reform, improving habitat, and supporting the early childhood and youth segments of the most vulnerable population groups; and (iii) strengthen public management by supporting greater efficiency in public institutions and strengthening urban and departmental management. These areas are aligned with the development challenges identified by the Uruguayan government and contribute to the structural and regional challenges identified in the Update to the Bank's Institutional Strategy for 2010-2020, specifically the challenges of social exclusion and inequity, low productivity and low innovation, and limited economic integration. The identified areas are the result of fifteen sector analyses and the growth assessment.

Product blend and participation of other donors: The country strategy calls for the use of various Bank instruments, such as sovereign guaranteed operations, non-sovereign guaranteed operations, and technical cooperation operations. The country strategy succinctly takes into consideration the interventions of other multilateral donors such as the World Bank and the CAF.

EFFECTIVENESS *(measured as the extent to which the country strategy is expected to achieve its objectives based on a review of four dimensions: (i) the quality of the diagnostics supporting the Bank's action in each line of work; (ii) the quality of the results matrix accompanying the strategy; (iii) the use and strengthening of country systems; and (iv) the analysis of the financing framework)* ***:***

Dimensions of effectiveness	%
I. Sector diagnostics	
- Identifies the main problems based on empirical evidence	100%
- Identifies the main beneficiaries	100%
- Identifies and assesses factors contributing to the problems identified	100%
- Presents the policy framework and a sequence of events for Bank intervention	100%
- The diagnostics match the objectives presented in the strategy	100%
II. Results matrix	
- Expected outcomes are clearly defined	100%
- Indicators are outcome-based and SMART	89%
- Indicators have baselines	100%

Fifteen sector notes were presented as part of the strategy . All of them are the result of sector diagnostics.
-100% of the notes clearly identify the main problems in the sector based on empirical evidence.
-100% of the notes identify the potential beneficiaries in each area of intervention.
-100% of the notes identify or assess the factors contributing to the problems identified.
-100% of the notes present the policy framework and a sequence of events for Bank intervention.
-In 100% of the notes, the issues raised match the Bank's strategic objectives.

Results matrix : The results matrix contains 16 strategic objectives for Bank action, 19 expected outcomes, and 19 indicators to measure advances toward the proposed objectives.

- 100% of the strategic objectives have clearly defined expected results.
- 89% of the indicators are outcome-based and SMART; the remaining 11% are not suitable for measuring the expected outcome or require greater specificity.
- 100% of the indicators have baselines.

Country systems : There are updated diagnostics for all financial management subsystems. For procurement, a diagnostic assessment using OECD/MAPS technology is in the final stages of preparation. There are planned actions to strengthen some of the financial management subsystems (accounting and reporting, and external control) and procurement subsystems (procurement methods and implementation of MAPS assessment recommendations). Regarding the use of country systems, the budget, treasury, accounting and reporting, external control, internal audit, procurement information, and shopping subsystems will be used, along with partial use of national competitive bidding.

Financing framework : The strategy contains an analysis of the country's financing needs and provides a projected scenario for sovereign guaranteed lending. Specifically, the country strategy forecasts approvals of sovereign guaranteed operations for approximately US$1.8 billion for the strategy period, with the expectation of a larger approval amount during the first years of strategy implementation.

RISKS *(measures three dimensions: (i) identification of factors that affect or might affect attainment of the proposed objectives; (ii) definition of mitigation measures; and (iii) monitoring mechanisms):*

The strategy identifies the risks associated with Bank participation in each of the strategic sectors and identifies mitigation measures. It also identifies general risks associated with the country's macroeconomic situation and implementation risks, identifying mitigation measures and monitoring instruments in both cases.