

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

ARGENTINA

COUNTRY PAPER



CONTENTS

EXECUTIVE SUMMARY

A.	The Argentine economy in the past decade and challenges today.....	1
B.	The government's agenda	1
C.	The Bank's strategy objectives.....	2
D.	Strategy priorities for 2001-2003	2
E.	Items for a dialogue.....	3
F.	Consultation process for strategy development.....	3
I.	MACROECONOMIC BACKDROP AND DEVELOPMENT CHALLENGES	1
A.	The Argentine economy in the past decade	1
B.	Development challenges.....	4
1.	Building a more competitive production system.....	5
2.	Combating poverty.....	5
3.	Reform of the State.....	7
4.	Regional integration.....	8
C.	Prospects.....	8
II.	THE BANK'S COUNTRY STRATEGY	10
A.	Previous strategy and review of the Bank's portfolio.....	10
B.	The government's strategy	13
C.	Proposed 2001-2003 strategy and main lines of action.....	14
1.	The Bank's strategy objectives	14
2.	Principal strategy action areas.....	15
3.	Lending scenarios.....	26
4.	Studies.....	27
5.	Coordination with the Bank Group	27
6.	Cofinancing and interagency coordination.....	29
7.	Strategy monitoring mechanisms.....	30
III.	RISKS.....	30
IV.	AGENDA FOR A COUNTRY DIALOGUE.....	30

ANNEXES

Annex I	Bank action areas, 1996-2000
Annex II	The Bank's 2001-2003 lending program
Annex III	Matrix of Bank actions in Argentina, 2001-2003

ABBREVIATIONS

CSOs	civil society organizations
FONAVI	Fondo Nacional de Vivienda (National Housing Fund)
GDP	gross domestic product
IIC	Inter-American Investment Corporation
IMF	International Monetary Fund
JBIC	Japan Bank for International Cooperation
MERCOSUR	Southern Common Market
MIF	Multilateral Investment Fund
PRI	Private Sector Department
VAT	value-added tax

EXECUTIVE SUMMARY

A. The Argentine economy in the past decade and challenges today

- 1.1 Few Latin American nations have pursued economic reforms as sweeping as those carried through by Argentina in the past ten years. As its Convertibility Plan tamed hyperinflation the country launched a massive modernization program in the private and public sectors alike. Among the program's fruits were a more open economy, State reform with a heavy privatization component, higher business productivity, a more diverse export base, a bolstered financial sector, and rapidly developed ties with the other MERCOSUR members as tariffs were lowered across the board and trade barriers were removed. As the economy prospered, capital inflows swelled.
- 1.2 However, the performance of some economic and social variables over this same interval was more lackluster: (a) as the country modernized its production apparatus the unemployment rate rose sharply, hitting 17.5% in 1995; (b) the income distribution and poverty rates worsened; (c) the public accounts were frequently in the red: when the budget did balance in any given year it was thanks to privatization receipts; and (d) the economy was left more exposed to external shocks.
- 1.3 After four years (1991-1994) of robust **economic growth** Argentina was shaken by two external shocks, one in 1995 and another in 1998, each of them triggering a recession. The country bounced back quickly from the 1995 events but has yet to recover fully from the 1998 episode. In 1999 GDP was down 3.4%. Though final 2000 figures are not yet in, they are expected to depict flat growth or a slight downturn (-0.2%).
- 1.4 For Argentina to achieve what can be posited as its people's paramount objective—high, sustainable economic growth rates—it will have to rise to a series of **challenges** that fall into four main areas: (1) building a more competitive productive system; (2) fostering social progress by reducing unemployment, combating poverty, and enhancing distributional equity; (3) reform of the State, and (4) consolidating regional integration. The government is bringing a set of macro-economic and sectoral policies to bear as it pursues all four objectives simultaneously.

B. The government's agenda

- 1.5 The aim of the policies currently in place is to deepen ongoing reforms to achieve economic growth with social equity and solidify the public finances. They address such areas as social security reform, negotiation of a new federal tax revenue-sharing arrangement, health insurance reform, rules and standards to protect consumers, and putting the new telecommunications and ports regulatory frameworks into practice. A keynote of the government's strategy is a commitment to

erase the fiscal deficit at all levels of government in the medium term, steadily lowering the ratio of public debt to GDP. The government is endeavoring to shore up investors' confidence in Argentina through an IMF-coordinated international financial support package.

C. The Bank's strategy objectives

- 1.6 The Bank's strategy for the coming years will address the challenges outlined above, in line with the government's program and the Bank's Eighth Replenishment mandates and those ensuing from the Forty-first Annual Meeting of its Board of Governors. The objectives of the strategy are to continue to support: (i) **sustainable growth of the production sectors and productivity increases** by funding activities to help maintain an enabling environment for investment and competitiveness and build capacity in the government to promote productive and infrastructure projects; (ii) **poverty reduction and raising of living standards**, by supporting projects that will create jobs and provide broader access, better coverage, and higher quality of basic education, health, sanitation, and environmental services; (iii) **reform of the State and balanced fiscal accounts** to entrench gains achieved thus far, further decentralize government operations and make the workings of government more transparent, and strengthen institutions; and (iv) furtherance of the **regional integration** process.
- 1.7 With the above strategy goals in mind the Bank has devised a lending program, worked out in discussions with the country authorities, whereby it will support investments and reforms in the social sectors, infrastructure development, regional development, and other areas to help **revitalize the economy** and **create jobs**. This Bank-supported program is compatible with the offerings of other multilateral agencies as part of the financial support package for Argentina and the arrangement with the IMF approved recently by that organization's Board.
- 1.8 Along with loans, the proposed 2001-2003 operations program contains various other actions and facilities—technical cooperation, MIF and IIC funding—with private sector and civil society involvement. The aim is to achieve lasting improvements and yield the strongest possible impact in the sectors concerned.

D. Strategy priorities for 2001-2003

1. Activities to **raise productivity and enhance competitiveness** through financial and technical assistance to small and medium-sized enterprises (SMEs) and the agriculture, agroindustrial, and financial sectors; public- and private-sector infrastructure finance; regulatory framework improvements; capital market development, including the pension fund and insurance industries; and new technology development and dissemination programs.
2. Initiatives to **reduce poverty and raise living standards**, including targeting and strengthening of social programs; equity-enhancing activities and those

that involve and strengthen communities; employment and labor-intensive programs; more flexible labor conditions; a new management model for the health sector, and reforms in the education, housing, sanitation, and environmental sectors.

3. Actions to help **consolidate reform of the State and fiscal balance** at the national, provincial, and municipal levels, including reforms to rebuild an enabling environment for investment, strengthen public-expenditure management capacity, transparency, and efficiency, and make tax collection more efficient.
4. Actions to advance **regional integration**, such as macroeconomic coordination, dispute settlement mechanisms, infrastructure investment planning, regulatory framework harmonization, etc.

E. Items for a dialogue

- 1.9 The following are some key issues for the country dialogue: (i) the kinds of IDB operations that can help boost employment, spur economic growth, and improve the public finances; (ii) budgetary authorization for the use of Bank and counterpart resources; (iii) portfolio execution; (iv) modernization of public-sector operations and fiscal decentralization; (v) capital market improvements; (vi) the private sector's role in economic development; and (vii) regional integration.

F. Consultation process for strategy development

- 1.10 In order to develop the proposed strategy, in addition to the dialogue with government authorities, the Bank took into account the ongoing feedback it receives from various executing agencies as the portfolio is implemented, as well as the views of independent economists and civil society groups in the context of the programs and other activities (seminars, workshops) financed by the Bank.

ARGENTINA

Economic indicators

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Gross domestic product – Annual growth (%)										
Total GDP	-1.3	10.5	10.3	6.3	5.8	-2.8	5.5	8.1	3.9	-3.4
Agriculture, forestry and fisheries	8.4	4.3	-1.0	3.1	7.5	5.6	-1.2	0.5	10.3	1.6
Industry	-2.3	9.9	10.2	5.1	4.4	-7.5	7.3	10.2	11.3	-7.7
Construction	-16.1	25.4	16.9	11.2	5.8	-12.2	8.4	16.6	7.2	-8.3
Nonfinancial public sector – Percentage of GDP (%)										
Current revenue	20.4	20.3	20.9	21.2	19.5	18.6	16.9	18.7	18.9	18.5
Current expenditure	20.9	20.8	20.3	18.7	18.4	18.4	17.8	19.1	19.1	20.1
Balance (-Deficit)	-1.5	-0.5	0.6	1.2	-0.1	-0.5	-1.9	-1.5	-1.4	-2.5
Money and credit - Percentage of GDP (%)										
Domestic credit	21.1	20.9	20.4	24.0	25.8	26.6	26.9	27.7	31.0	33.0
Money supply (M1)	1.9	2.8	4.2	5.1	5.7	5.7	6.4	6.5	6.9	6.8
Prices										
Consumer prices (annual growth rate)	2,315.5	171.7	24.9	10.6	4.2	3.4	0.2	0.5	0.9	-1.2
Balance of payments - US\$ million										
Current account	4,552	-647	-5,521	-8,030	-10,992	-4,985	-6,521	-11,954	-14,372	-12,293
Trade balance	8,628	4,419	-1,396	-2,364	-4,139	2,357	1,760	-2,123	-3,117	2,175
Exports of goods	12,354	11,978	12,399	13,269	16,023	21,161	24,043	26,431	26,441	23,333
Imports of goods	3,726	7,559	13,795	15,633	20,162	18,804	22,283	28,554	29,558	25,508
Balance on services	-674	-1,599	-2,463	-3,221	-3,692	-3,326	-3,366	-4,178	-4,407	-4,095
Net income receipts	-4,400	-4,260	-2,393	-2,931	-3,567	-4,529	-5,331	-6,089	-7,375	-7,922
Net current transfers	998	793	731	486	406	513	416	436	527	507
Capital and financial account	-2,145	3,028	8,731	13,482	12,548	6,756	11,712	16,745	17,017	13,952
Change in reserves (- increase)	-3,121	-2,040	-3,264	-4,279	-685	82	-3,875	-3,293	-3,438	-1,201
External debt - US\$ million										
External debt	54,672	56,779	59,269	70,575	80,337	93,925	105,170	123,221	139,317	144,600
Actual debt-service payments	6,161	5,420	4,882	6,556	8,175	9,692	14,012	19,969	13,000	13,500

Sources: Ministry of Economic Affairs, Argentina. IDB Statistics and Quantitative Analysis Unit. IDB-OD1/RE1.

I. MACROECONOMIC BACKDROP AND DEVELOPMENT CHALLENGES

A. The Argentine economy in the past decade

- 1.1 Few Latin American nations have pursued economic reforms as sweeping as those carried through by Argentina in the past ten years. As its Convertibility Plan tamed hyperinflation the country launched a massive modernization program in the private and public sectors alike. Among the program's fruits were a more open economy, State reform with a heavy privatization component, higher business productivity, a more diverse export base, a bolstered financial sector, and quickly developed ties with the other MERCOSUR members as tariffs were lowered across the board and trade barriers removed. As the economy prospered, capital inflows swelled.
- 1.2 However, the performance of some economic and social variables over this same interval was more lackluster: (a) as the country modernized its production apparatus the unemployment rate rose sharply, hitting 17.5% in 1995; (b) income distribution and poverty rates worsened; (c) the public accounts were frequently in the red: when the budget did balance in any given year it was thanks to privatization receipts; and (d) the economy was left more exposed to external shocks.
- 1.3 After four years (1991-1994) of robust **economic growth** Argentina was shaken by two external shocks, the first in 1995 and the second in late 1998. In 1995 the "tequila effect" prompted a massive capital exodus and domestic activity declined, but ultimately the economy rallied. The initial trigger for the second shock was the spillover from turmoil in Southeast Asia and Russia in mid-1998; after Brazil devalued the *real* in early 1999 the situation became even more serious. Throughout the rest of the year Argentina's external accounts suffered, with declining terms of trade and the dollar's appreciation against European currencies and the yen. The result was negative GDP growth in the final quarter of 1998 and first three quarters of 1999.
- 1.4 Toward the end of the year (September 1999) the country glimpsed signs of a turnaround, but in 2000 its economic performance was once again lackluster, with flat or slightly negative (-0.2%) growth figures. The external picture was mixed: prices for Argentina's leading export commodities (including oil) climbed, as did export sales to Asia, and the Brazilian market picked up. However, Federal Reserve interest-rate hikes and a steady appreciation of the dollar impacted Argentina negatively, its economy and domestic demand remaining sluggish despite efforts by President Fernando de la Rúa who had taken office in December 1999. The 0.3% decline in GDP in the fourth quarter of 1999 was gentler than preceding-quarter drops; estimates for 2000 are for a 0.2% downturn. Industrial growth was -0.7% in 2000 (compared to -7.7% the previous year) but the mining sector grew by 11.6%. The falloff in gross fixed investment was less pronounced than in 1999.
- 1.5 The right conditions for boosting **employment** are still not in place. Between October 1999 and October 2000 the unemployment rate climbed from 13.8% to

- 14.7%, meaning some two million people without jobs. Another two million are underemployed. Compounding the problems in the formal labor market are the ranks of unregistered workers that have swelled in the past ten years to account for nearly 40% of the active workforce. According to studies based on National Statistics and Census Bureau numbers, 72% of the jobs created from 1990 until early 2000 were informal ones, marking a 50% rise in this form of employment. In other words, most of these new jobs give workers no benefits or labor rights and pay nothing into the social security system.
- 1.6 As the economy expanded in the 1990s, **social inequality worsened**. Between 1990 and 1999, GDP growth was matched by a 57% increase in the income gap, and the concentration of income increased twice as fast as it had from 1975 to 1990. In 1990, according to official figures, the poorest 10% of the population received 2.15% of total income; by 1999 this segment was receiving only 1.5% of the total. Meanwhile, the share of the wealthiest decile rose from 33.6% to 36.7%. In Buenos Aires, the highest per capita income region of the country, the income gap increased by 127% in the 1990s.
 - 1.7 In 1999, against a backdrop of recession, the **public accounts** worsened considerably, showing a US\$7.156 billion deficit. Driving the shortfall was a combination of steady increases in spending in the 1990s and declining tax revenues. The 1999 deficit was up 86.9% from 1998, 40% over the IMF target, and equivalent to 2.5% of GDP. Factoring in the provincial deficits, the consolidated shortfall was 4.1% of GDP.
 - 1.8 To remedy this state of affairs the new administration, backed by a new IMF arrangement, adopted aggressive fiscal policies on the tax and spending sides alike. The picture brightened during the first half of 2000, the US\$2,374.8 million deficit falling below the US\$2.69 billion agreed on with the IMF for that period. This can be attributed mostly to spending cutbacks and extraordinary revenues owing to the moratorium, advance income-tax payments, debt-bond swaps, etc. Given the sluggish economy, however, there was no rise in regular tax revenues. When the country posted a deficit again in July and August it became evident that the IMF targets would have to be adjusted.
 - 1.9 As Argentina's economy languished in 2000 the global financial markets became worried about the nation's ability to honor its external-debt obligations, and the country-risk premium soared. In these circumstances, resolute action was needed to buttress confidence in the country. The government adopted a firm growth-oriented economic strategy to secure local and foreign investors' confidence, speed up productivity improvements, and continue to make the economy more competitive. A central element of the strategy is continuation of the convertibility scheme, in a series of economic policy initiatives that bespeak the country's resolve to solidify its fiscal accounts in the medium term and expand on and pick up the pace of

structural reforms, modernization, and trade liberalization. The IMF is backing the government's program.

- 1.10 The aim of the policies currently in place is to deepen ongoing reforms. These include social security reform, a federal agreement on transfer payments to the provinces and negotiation of a new federal tax-revenue sharing arrangement, deregulation and redistribution of health insurance system resources to enhance health-care quality and make for more equitable coverage, and provisions to protect consumers and put the new telecommunications and ports regulatory frameworks into practice. A keynote of the government's strategy is a renewal of its commitment to erase the fiscal deficit at all levels of government in the medium term, so as to steadily lower the ratio of public debt to GDP. Two highlights of this program to put the fiscal accounts in order are a freezing of primary expenditure by the federal government and deficit-running provincial governments to 2000 levels and the strengthening of structural fiscal reforms, notably those pertaining to tax administration and the social security system. Targets for the national public deficit worked out with the IMF are US\$6.6 billion for 2000; US\$6.5 billion for 2001; US\$4.85 billion for 2002, US\$3.3 billion for 2003, US\$1.7 billion for 2004, and zero deficit in 2005.
- 1.11 In late December, following fast-track negotiations, Argentina announced the terms of the IMF-headed financial support package, which immediately shored up confidence in the country. Agencies participating in this financial support package are the IMF with US\$13.7 billion, the IDB with US\$2.4 billion in loan commitments and the World Bank with US\$2.5 billion, the Spanish government with a US\$1 billion loan, private commercial banks who will put up US\$10 billion via debt instruments, private pension funds with US\$3 billion (through purchases of government securities), and US\$7 billion in debt swaps. The government's plan is to resort to the financial support funds as a precautionary arrangement but adhere to the overall objective of accessing the international and domestic markets, which will supply the bulk of the Treasury's borrowing requirement.
- 1.12 Though some **provinces** have brought in fiscal adjustments in recent years the 1999 aggregate provincial deficit was 87% higher than in 1998 and their combined debt stock was up 16.5%. This had direct repercussions on the national public accounts and on local governments' prospects for carrying out their mandates. In 1999, current revenues were down but operating expenditures increased (continuing the early-1990s trend) as did interest payments. Capital projects had to be shelved. The provincial deficit that year stood at 1.6% of GDP. According to the forecasts, the deficit will edge down to 1.2% of GDP in 2000.
- 1.13 The **external accounts** have improved since the fourth quarter of 1999, chiefly because export growth has outpaced increases in imports. Rising world prices for various commodities, including fuel, and higher volumes (e.g. sales to Brazil and soybean shipments) are responsible for the surge in exports; the sluggish economy

explains dips in imports. The 2000 forecast is for a trade surplus of close to US\$2.49 billion, a considerable improvement over the US\$770 million deficit the previous year.

- 1.14 The magnitude of the country's **public debt stock** (35.6% of it owed to creditors in Argentina) and mounting debt-service costs are a constraint for government action, since they make it more difficult to use fiscal policy to recharge the economy, combat unemployment, and redress social inequities. Approximately 80% of the debt is at medium or long term; 56.7% of it carries fixed rates of interest. Bonds account for the lion's share (71.3%) of the debt. Loans represent 20% of total debt: 63.9% of the outstanding balance is owed to international institutions, 17.3% to official agencies, 15.2% to commercial banks, and 3.6% to other creditors. In 2000, interest on the debt equaled 16.5% of aggregate revenues of the consolidated public sector.
- 1.15 Between 1991 and 1999 Argentina's external debt (most of it public-sector borrowings) climbed from US\$57 billion to US\$144.6 billion. The external debt-to-GDP ratio rose from 28.4% to 51%. This drove up the debt service (interest and principal payments) from 73% of exports annually, on average, in 1996-1998, to 97% of exports in 1999. Commitments actually paid off during those intervals equaled 61.1% and 57.9%, respectively, of exports. Estimates from the most current data available put the country's December 2000 debt stock at US\$150.4 billion.

B. Development challenges

- 1.16 To help understand circumstances in Argentina this paper identifies two **kinds of challenges** to economic and social progress. The **first** set has to do with managing economic and social objectives that are both priorities. In other words, part of the country's stress stems from efforts to resolve different kinds of problems when the remedies are at least partly at odds. The two preeminent challenges of this kind are outlined below.
- (i) **Narrowing the public deficit and reenergizing the economy.** Given the current state of affairs in Argentina, measures intended to erase the fiscal deficit at all levels of government in the medium term need to go hand in hand with moves to recharge the economy and combat poverty. Underlying the measures worked out with the IMF in December 2000 is the premise that lasting fiscal balance hinges largely on a return to a higher growth path.
 - (ii) **Enhancing competitiveness and lowering unemployment.** Argentina needs to expand on and enhance its efforts to boost private- and public-sector productivity. Putting the economy back on a growth path will be the key to making certain that private-sector modernization and reform of the State do not create an

environment that, in the short or medium term, could thwart Argentine society's other important objective, which is to lower unemployment and even out the income distribution.

- 1.17 The **second** kind of challenges involves the attainment of specific objectives. If Argentina is to achieve its posited core objective—high, sustainable economic growth rates—it will have to rise to a series of challenges that fall into four main areas: (1) making the production system more competitive; (2) fostering social progress by reducing unemployment, combating poverty, and narrowing the income gap; (3) reform of the State, and (4) strengthening regional integration.

1. Building a more competitive production system

- 1.18 Argentina still has a long way to go to make its goods and services sectors more competitive. The initiatives outlined below would propel economic growth and help secure a solid foothold for the country in the global marketplace.

- a. **Cultivating competitiveness.** The key to a more competitive economy is a combination of actions including: (a) sector and regional programs to disseminate technology and continue with ISO 9000 type quality improvements; (b) infrastructure investment; (c) management and technical training for SMEs; (d) moving off-book activities into the formal sector; and (e) improving foreign-trade policy and environmental conservation. One challenge on this front is to come up with ways of funding such endeavors and achieving efficiency gains in institutions working in these fields.
- b. **Policy integration.** One step in boosting competitiveness is to develop tie-in policies in many different spheres of the nation's business. For instance: (a) labor reform, apart from helping to create jobs, spurs businesses to become more competitive so they can reduce relative labor costs without lowering wages; (b) initiatives to make the financial system run more efficiently will attract investors and bring down production costs in every sector; (c) measures to encourage informal businesses to move into the mainstream economy will give them—assuming they are viable—access to tools for development; and (d) more effective regulatory frameworks will create an enabling environment for heightened business productivity.

2. Combating poverty

- 1.19 According to official statistics, approximately 30% of Argentina's urban dwellers are living in poverty and of this total, some three million do not earn enough to cover their basic nutritional needs. Lowering the unemployment rate, narrowing the income gap, and alleviating poverty are no easy task even for the more advanced nations, much less for Latin America. Attesting to the tough challenge facing Argentina is the fact that the aforementioned three indicators worsened precisely

during the era of strongest economic growth starting in 1991. With the country's unsteady growth figures today the task is even more formidable. Some requirements for tackling this challenge are discussed in the following paragraphs.

- a. **Unemployment.** Much of the explanation for worsening poverty levels and social gaps lies in the country's unemployment and underemployment figures. For years, high unemployment and underemployment rates have been hobbling government attempts to improve social indicators. In fact, the jobless figure started to climb in 1991 when the economy was rallying and the government launched the modernization process. As the country set about dismantling protectionist barriers and speeded up its privatization program the production system had to quickly come up with productivity improvements, an effort to which the surge in capital-goods imports over that period can attest. The industrial sector is a telling example: between 1991 and 1996 its output climbed 30% but 20% of its workforce lost their jobs. Apart from this structural unemployment, the recession since 1998 has dampened job prospects.

Along with the labor code reform approved in May 2000, the training and infrastructure investment programs the government has unveiled, many of which the Bank is helping to fund, are improving conditions in the labor market and equipping the productive system to compete. However, the economic authorities understand that there can be no substantive reduction in unemployment unless the country can post considerably higher-than-forecast GDP growth in the next three years.

- b. **Social spending.** The best strategy in both an unemployment and a full-employment scenario to combat poverty and improve the income distribution is to spur investment in sectors like health, education, nutrition, housing, sanitation, environmental protection, and social advancement that will provide proportionally more benefits to lower-income segments of the population. Hand in hand with such investments would be wage and tax policies concordant with a sustainable increase in real income of the poorest. A backdrop of development with stability clearly would facilitate the task. The Argentine government has demonstrated its intention of adopting such a strategy, albeit at a relatively slow pace given the current constraints (notably on the fiscal side) and weaknesses in institutions operating in this area.

As well as finding viable avenues for funding social expenditure the country will need to bolster national, provincial, and municipal agencies that administer social programs. Though Argentina's per capita social expenditure is the highest in Latin America, equivalent to 18% of GDP, its rising poverty rate bespeaks an inefficient use of resources. This priority challenge is something for the entire nation to address, since inequities can trigger instability, as occurred with the hyperinflation of the late 1980s.

3. Reform of the State

1.20 Reform of the State is intended to achieve the outcomes discussed below.

- a. **Public accounts.** Fiscal deficits can destabilize the economy and make it difficult for government agencies to do their job. One reason for the lackluster results of various measures in recent years is the lack of flexibility in public spending, which handicaps efforts to put resources to more efficient use and thereby pare government expenditure. Further reforms of the State, taking in the pension system, would enable the government to lower spending and improve the quality of public services. Achieving true fiscal balance will mean, along with State reform, realizing such aims as: (a) a return to a high economic growth path and increased domestic consumption; (b) continuity in moves to modernize the tax administration, to significantly curb tax evasion; (c) approval of a more sustainable federal pact in terms of apportioning resources and functions among different agencies; and (d) faster reform of the State and fiscal adjustment in the provinces and municipalities. The point of reference for adjustments to the public finances is the 1999 Fiscal Responsibility Law.
- b. **Public-sector performance.** Despite impressive inroads made on many elements of the State reform process, some remaining weak points in the administrative apparatus are impairing the quality of government services. Public agencies feel little sense of commitment or accountability and the desired level of transparency is proving difficult to achieve. Thus, much remains to be done in this sphere, which includes civil service performance.
- c. **Provinces and municipalities.** Action still is needed on various fronts in the provinces and municipalities to adjust the public finances and revamp government administration. Until satisfactory results are achieved in those areas, reform of the State at the national level will be hobbled. The upcoming discussions on a new Federal Tax Revenue-Sharing Law will be an opportunity to come up with incentives to the provinces for such improvements. One challenge posed by the new revenue-sharing scheme will be to build capacity in provincial governments to collect taxes falling within their purview. The more the provinces can boost own revenues and rely less on federal funds, the faster the national government will be able to achieve lasting improvements in its fiscal accounts. The federal government has offered support mechanisms to provinces that bring in programs to strengthen their finances.
- d. **Pension system.** The pension system still accounts for fully 40% of the deficit. There is, as yet, no sound apparatus in place for a system of coexisting private pension funds and national and provincial public plans, making these services less than effective. With the new pension reforms unveiled in December 2000 the government plans to speed the system's return to a solid financial footing and improve instruments to cover more of the population.

- e. **Regulation.** Argentina has put through sweeping privatization and concession programs in the public transportation, communications, water and sanitation, and electric power sectors. However, regulation of these industries needs to be improved, both to assure service quality and keep rates affordable so as not to push up the “country cost”. Financial-services regulation and oversight also needs a boost, to create an environment more conducive to saving and more attractive to investors.

4. Regional integration

- 1.21 Argentinians understand that MERCOSUR is the surest avenue to an open economy, since most of the improvement in the foreign trade/GDP ratio since 1991 is attributable to intraregional trading. Integration also is essential for diversifying the country’s export base. While primary commodities predominate in sales to the rest of the world, manufactures such as automobiles, petrochemicals, and capital goods head the list of shipments to MERCOSUR. Thus, regional integration could be a strategic factor in industrial-sector recovery.
- 1.22 The surge in trade since the 1991 signature of the Treaty of Asunción could create the false impression that the most important integration moves are now complete. In fact, it is clear that work is needed on a series of important preconditions such as macroeconomic coordination, structuring of institutions, harmonization of member-state laws and regulatory frameworks, infrastructure integration, and sector-specific development programs. The new government has announced its intention to push for MERCOSUR’s revitalization. As was evident in recent negotiations involving NAFTA, the European Union, and the World Trade Organization, MERCOSUR also can be a vehicle for bolstering negotiating capacity in dealings with other regions and multilateral accords. This is vital for achieving such aims as moving into hitherto-closed markets in industrial economies.

C. Prospects

- 1.23 The IMF-coordinated international financial support package put together last December is a decisive step in boosting investment in Argentina and domestic consumption. Though increased export sales will be fundamental for the dynamic of the Argentine model, the impact of any such improvement on economic growth will be tempered by the fact that exports contribute 10% of GDP and have little effect on tax intakes.
- 1.24 Since there had been little change in investment and consumption figures by late 2000, GDP growth that year will likely come out to -0.2%. Though this will do nothing to trim the deficit, the fiscal measures and reforms the government has brought in can be expected to tighten its control over the public accounts. The infrastructure plan also will spur economic growth in the medium term, thanks to

US\$20 billion in capital spending called for over five years, the bulk of it privately funded.

	1999	2000	2001	2002	2003
GDP – Real change (%)	-3.4	-0.2	2.5	3.8	4.3
Balance of payments (US\$ billion)					
Current account balance	-12.4	-9.9	-9.8	-9.8	-10.1
Trade balance	-2.2	1.1	1.8	2.7	3.7
Exports	23.3	26.3	28.7	32.1	35.8
Imports	-25.5	-25.2	-27.0	-29.3	-32.1
I. External debt (US\$ billion)	144.6	150.4	156.0	161.9	167.8
II. Fiscal balance/GDP (%) ^{1/}	-4.2	-3.6	-3.1	-2.2	-1.4

Sources: Ministry of Economic Affairs, IMF, FIEL, IDB-REI/ODI.

^{1/} Consolidated public sector.

- 1.25 Though gradual improvements in **employment** can be expected as growth picks up in 2001, this is unlikely to make significant inroads into the unemployment problem since the very increase in employment could mean a larger pool of workers in the market (workforce participation rate). Labor-code reforms will not be enough, in and of themselves, to make a significant difference in unemployment over the next three years, though they will make it easier to find work in a growing economy. Additional considerations here are the continuing fiscal adjustments in the provinces and municipalities and the need for the production system to become even more competitive—neither of which do much for job creation. Given this panorama, lowering the poverty rate will require extremely effective government programs during this transition period.
- 1.26 As for the **balance of payments**, despite promising signs in external markets, Argentina's recent trade surpluses, and moves to diversify export products and markets, no significant reduction in the current-account deficit is likely in the coming years, considering among other factors net interest payments to foreign creditors. In this context, the performance of capital flows will be crucial to allay concerns on the external front. According to the forecasts, capital-account balances will be healthy enough to offset current-account deficits ranging from 3.1% to 3.3% of GDP in the next few years.
- 1.27 The MERCOSUR member states will continue to seek solutions to the bloc's difficulties and to harmonize their nations' economic policies. One milestone was the May 2000 agreement with Brazil with a plan for coordinating fiscal-deficit, public-debt, and inflation targets. In the years ahead, MERCOSUR members will be focusing more and more on coordinating and aligning their policies, programs, and reporting systems.
- 1.28 Prospects in the **financial sector** are promising, following five years of stringent adjustments. Deposits were up 12% in 2000, the strongest showing since mid-1998.

A series of government decisions will have a considerable impact on this sector: deregulation of the personal loan market will spur competition for consumer credit business and thereby bring down interest rates, and converting Banco Nación to a State corporation will make its operations more transparent and efficient.

- 1.29 **In conclusion:** The government does not have much room to maneuver in public-policy implementation because it is bound by parameters of its exchange rate and monetary policy, the fiscal situation, public-sector debt levels, and the fact that the political parties backing the government do not have a majority in Congress. Nevertheless, the government has been seizing the opportunities it does have and is resolutely deploying its economic policy instruments. The financial support program arranged in late 2000 will bolster those efforts. Consequently, the real effect of decisions taken to revitalize the economy will likely be felt from 2001 onward (see Table I-1), helping to step up the fight against poverty.

II. THE BANK'S COUNTRY STRATEGY

A. Previous strategy and review of the Bank's portfolio

- 2.1 The Bank's 1999-2006 strategy for Argentina pursued operations with the following objectives: (i) deepen and consolidate modernization of the State, taking in the provinces and municipalities; (ii) raise productivity and make the economy more competitive; and (iii) reduce poverty and raise the living standards of Argentinians by giving them jobs and increasing the coverage of basic services.
- 2.2 According to a review of completed and ongoing operations by reference to the above-mentioned strategy, keynotes of the portfolio are a **preponderance of operations to help finance reform of the State** (chiefly a US\$2.5 billion financial emergency operation), a **sustained effort to increase Bank activity at the subnational level**, and some **innovative social-sector projects**. Argentina also made considerable use of the private-sector window¹ to fund improvements in services formerly delivered by the State.
- 2.3 Funding to help Argentina contend with emergencies, in the form of one loan for a climate-related (flood) emergency and one finance sector operation (structural adjustment and strengthening of banking-system safeguards), accounted for 38% of Bank approvals for the country between 1996 and 2000.

¹ Argentina's is the most diversified of the borrowing member country portfolios.

- 2.4 Given the magnitude of Argentina's economy, the **impact**² of the Bank's loans has more to do with their targeting, innovative nature, and catalytic effect than with the amount of funding *per se*. Some Bank support highlights are a pioneering initiative to build emergency-preparedness capacity in natural-disaster management agencies; a standby loan to strengthen banking-system safeguards; operations to improve the quality of government operations (including programs in some provinces); comprehensive assistance to vulnerable groups, with heavy community input, and development of a network of institutions to give these groups readier access to social services; institutional adjustments to draw maximum benefit from pension reforms, modernization of the State, labor market reform, and social development; and broader access and coverage of credit and nonfinancial services for SMEs. See Annex I for details.
- 2.5 The main **obstacles** for timely loan execution are implementing agencies' institutional weaknesses, a lack of familiarity with Bank procedures (largely owing to turnover in executing unit staff) and, more recently, the government's fiscal adjustment program and low budget authority levels for use of Bank and counterpart funds, given the size of the portfolio (see paragraph 2.11).
- 2.6 The chief **lessons learned** can be grouped into those relating to project *preparation* and those having to do with project *execution*. Important lessons for the *preparation* phase are: (a) in parallel with loans, offer other actions and instruments—technical cooperation, MIF, PRI, and IIC support—in partnership with private enterprise and civil society, to maximize an operation's impact on the sector and make it sustainable; (b) ensure that beneficiaries and executing agencies have genuine input as an operation is being designed, to instill a sense of ownership; (c) in the case of direct loans to provincial governments, foster from the very beginning of the preparatory stage interfaces between the executive and legislative branches to structure an overall frame of reference for reforms of the State so they will be viable and lasting; and (d) when designing and costing new operations with subnational governments and the social sectors, build in longer average implementation periods to take account of such factors as provincial or municipal borrowing statutes, a lack of familiarity with procedures for international borrowings, and executing agencies' institutional shortcomings.
- 2.7 Future efforts during the project *implementation* stage should include: (a) keeping the same counterpart technical team for a minimum length of time, to afford continuity in operations execution; (b) institutionalizing the Bank's training offerings for executing agencies in the areas of procurement, disbursements, and financial statements; and (c) continuing the practice of periodic portfolio reviews to pinpoint and head off problems, with the participation of executing agencies and representatives of the Cabinet Office Chief and the Ministry of Economic Affairs.

² Since many of these operations are still under way, their full impact will only be felt in the medium and long term.

2.8 Between 1996 and 2000 the Bank approved 42 operations for Argentina totaling US\$7,345.2 million (net of cancellations)³—26 investment loans for US\$3,658 million, four sector loans worth US\$3,219.2 million (special structural adjustment program, strengthening banking-system safeguards, provincial pension system, and support for fiscal balance and social-sector management), eight private-sector “A” loans for US\$463.1 million, and four Project Preparation Facility operations totaling US\$4.9 million. The bulk of this funding supported modernization of the State (financial adjustment program, provincial reforms) and programs to reduce poverty and raise living standards (urban development and social protection and management). The following table breaks down the portfolio by the strategy objectives mapped out in the 1996 country paper (document GN-1951-2).

Project approvals 1996-2000 (US\$ million)				Active loans (US\$ million)				
Objective and sector	Nº.	Amount	%	Nº.	Amount	%*	Disb. *	%
Modernization of the State	12	3,808.2	51.8	12	3,527.3	41.9	2,457.4	59.3
Enhancing productivity and competitiveness	12	1,203.6	16.4	12	1,498.3	17.8	597.6	14.4
Poverty reduction	18	2,333.4	31.8	20	3,388.5	40.3	1,088.8	26.3
Total	42	7,345.2	100.0	44	8,414.1	100.0	4,143.8	100.0

*Net of cancellations. Disbursements at 31 December 2000.

2.9 On average, Bank approvals in 1996-2000 came to US\$1.47 billion a year. The highest figure was in 1998—US\$3,843 million, most of it for loans for structural adjustment and strengthening of bank-system safeguards and to aid in the flood emergency. The lowest approval figure was US\$454 million in 1999.

2.10 The Bank’s **active loan portfolio** in Argentina (including private-sector “A” loans) currently stands at US\$8,414.1 million. At 31 December 2000, US\$4,143.8 million (49.4%) had been disbursed.⁴ The portfolio consists of 41 investment projects (one of them regional and four PRI operations) and three sector loans.⁵ In value terms, 41.9% of the loans are assisting in modernization of the State, 40.3% in social-sector operations, and 17.8% in projects or programs in the production sectors. Other ongoing operations are a US\$22 million export line of credit, 28 nonreimbursable technical-cooperation projects (some of them regional) totaling US\$50.5 million, 22 MIF operations for US\$36.7 million and six Small Projects for US\$2.8 million in all.

³ The original amount was US\$7,346.2 million.

⁴ If sector loans are excluded the figure drops to 41.8%.

⁵ The US\$500 million standby loan to help strengthen banking-system safeguards gives the system access to funding in the event of a financial crisis.

2.11 Moves to trim the fiscal deficit have had an impact on the portfolio: 12 Bank-funded projects have been affected by spending restrictions and their implementation progress at 31 December 2000 is rated **unsatisfactory**. For eight of them, prospects of achieving their objectives are **doubtful** and one operation is **unlikely** to fulfill its aims. Progress on the others is rated **normal**. Specific action plans were worked out during the periodic portfolio review meetings to deal with project delays. These include loan reformulations or adjustments, extensions, midterm reviews, administration missions, concentrating the execution of several projects of any one ministry within a single executing unit, workshops with executing agencies, and partial cancellations. Performance of the four active PRI projects has been satisfactory; they are unfolding as planned, adhering to the original timetable.

2.12 The following table sums up the status of operations in the portfolio by reference to their **implementation progress** and **achievement of development objectives**.

Strategy objective	Implementation progress	Achievement of development objectives				
		Very likely	Likely	Doubtful	Unlikely	Total
Deepen and consolidate modernization of the State and extend the process to provinces and municipalities	Highly satisfactory					
	Satisfactory		9			9
	Unsatisfactory		1	1	1**	3
Enhance productivity and national competitiveness	Highly satisfactory					
	Satisfactory		7	1		8
	Unsatisfactory			1		1
Reduce poverty and raise living standards	Highly satisfactory					
	Satisfactory	1	10			11
	Unsatisfactory		3	5		8
TOTAL*		1	30	8	1	40

* Does not include four PRI projects.

**Administration of justice project—cancelled, but advanced funds still to be accounted for.

B. The government's strategy

2.13 As was noted in paragraph 1.10, the government's policy aims are to deepen ongoing reforms to spur economic growth with social equity and solidify the public accounts. To achieve these core objectives it is focusing on such areas as enhancing competition, social security reform, negotiating a new federal tax revenue-sharing arrangement, health insurance reform, consumer protection standards, and putting the new telecommunications and ports regulatory frameworks into practice. A keynote of the government's strategy is a commitment to erase the fiscal deficit at all levels of government in the medium term, steadily lowering the ratio of public debt to GDP. The government is endeavoring to restore investors' confidence in Argentina through an IMF-coordinated international financial support package. Some of these initiatives are outlined below.

- 2.14 Two pillars of the nation's **economic revitalization** policy are the National Housing Plan and the 2000-2005 Federal Infrastructure Plan, calling for some US\$20 billion in investment. A large share will fall to the private sector, which will finance, build, operate, and maintain the projects. An Infrastructure Fund is being set up for this purpose. Other important elements of the economic renewal strategy are: (a) making the production system more competitive; (b) boosting national saving to pay for mounting investment needs, to ease the external debt burden; and (c) tax mechanisms to spur investment and exports. To help the economy compete in the global marketplace the government will try to steadily lower costs, raise productivity, carry through structural reforms, and improve the regulatory framework.
- 2.15 The central aim of the **social equity enhancing** policy is to combat unemployment and poverty. The government's main tool for improving employment levels, the Labor Reform Law passed by the Congress in May 2000, is designed to facilitate job creation, provide incentives for workers to move into the formal workforce, improve working conditions and job stability, and make the production system more competitive. Elements of the labor reform are: (a) decentralization of collective agreements; (b) repeal of clauses that permitted unlimited collective-agreement renewals; (c) creation of arbitration and mediation services; (d) review of collective agreements that can jeopardize companies' financial health; (e) lengthening the probation period for new hires; (f) simpler worker-registration procedures; and (g) workers' right to information on their company. Poverty-reduction aims are to strengthen the safety net for the neediest and implement the Solidarity Plan, at an estimated cost of US\$200 million, to help 400,000 families classed as unable to satisfy basic needs.
- 2.16 The government's moves in the **fiscal area** are intended to cut spending and boost revenues. In December 1999 it brought in a tax reform package and wrote spending cutbacks into the 2000 budget. In 2000 the authorities announced a new round of budget cuts, including the lowering of civil service salaries, and stepped up efforts to curb tax evasion. One aim of the pension reform approved in December 2000 is to reduce expenditures in the pension system, broaden its coverage, and make for a more equitable distribution of benefits, as well as fostering competition and efficiency in the private system. The national government has placed renewed emphasis on the issue of **provincial government** finances, having signed an agreement with the provinces to govern federal-provincial fiscal relations until 2005 and lay the foundations for the future Federal Tax Revenue-Sharing Act.

C. **Proposed 2001-2003 strategy and main lines of action**

1. **The Bank's strategy objectives**

- 2.17 The Bank's strategy for 2001-2003 will address the challenges outlined above, in line with the government's agenda and the Bank's Eighth Replenishment mandates

and those ensuing from the Forty-first Annual Meeting of its Board of Governors. Its strategy aims are to continue offering support for: (i) **sustainable growth of the production sectors and productivity increases**, by funding activities to help maintain an enabling environment for investment and competitiveness and build capacity in the government to promote productive and infrastructure projects; (ii) **poverty reduction and a rise in living standards**, by supporting projects to create jobs and provide broader access and better coverage and quality of basic education, health, sanitation, and environmental services; (iii) **reform of the State and fiscal balance**, to build on initiatives already under way, further decentralize government operations and make the workings of government more transparent, and strengthen institutions; and (iv) deepen **regional integration**.

- 2.18 With the above strategy goals in mind the Bank has devised a lending program, worked out in discussions with the country authorities, whereby it will support investments and reforms in the social sectors, infrastructure development, regional development, and other areas, with an emphasis on **spurring economic growth and creating jobs**. This Bank-supported program is compatible with the offerings of other multilateral agencies as part of the financial support package for Argentina and the IMF arrangement approved recently by that organization's Board (see breakdown of the lending program by strategy focus in Annex 2). With these measures, in the **base-case lending scenario**, average annual Bank approvals in 2001-2003 (US\$1.42 billion) would be down slightly from the 1996-2000 average of US\$1.47 billion (see chapter II, section C(3)).
- 2.19 The proposed 2001-2003 lending program (including PRI and IIC loans) is rounded out by other facilities—technical cooperation and MIF operations—that will involve the private sector and civil society, to help make certain that the effort will be sustainable and maximize impacts on the respective sectors. The use of new flexible lending instruments will be determined as new operations are identified. Intensive use of Project Preparation and Execution Facility (PROPEF) will be sought, in particular for the preparation of sector operations. In the past, Argentina has been the top user of the PPF (Project Preparation Facility), with US\$12.1 million approved as of February 2001. Moreover, since Argentina has traditionally been very open to new processes, it is expected to make good use of the innovation loan facility. The government has not requested use of the multiphase program loans, but opportunities for use of this facility may emerge over the medium term.

2. Principal strategy action areas

a. Sustainable growth of the production sectors and productivity increases

- 2.20 **SMEs:** Microenterprises and SMEs still face barriers to access to credit and nonfinancial services. Since the gap is particularly serious in provinces in the

interior, action is needed to support local productive development. A rigid labor market and high nonwage costs are softening business profits. Some approved operations have yet to be implemented because of institutional weaknesses, shortfalls in funding for project execution, shifting priorities, or a combination of these factors.

- 2.21 Action lines: Support initiatives to: (a) **provide readier access to credit and nonfinancial services**, including support for foreign trade; (b) promote the creation of **reciprocal guarantee companies** and specialized credit-rating agencies; (c) help **remove obstacles** to competitiveness gains; (d) spur **development of local production**, particularly in the less advanced regions; (e) implement market **globalization and diversification programs**, particularly at the provincial level; and (f) promote **technology development programs** and their dissemination, to make businesses more competitive and develop industry.
- 2.22 **Infrastructure**: Argentina has some serious physical infrastructure gaps, the result of years of scanty investment and maintenance. Even with the privatizations of the 1990s the country's installed capacity is insufficient in some sectors, especially to handle mounting demands as the regional integration process advances. Though considerable strides have been made in improving electricity, telecommunications, port, and rail freight services, in some instances (transportation, telecommunications) no legal or regulatory framework was devised at the start of the privatization process to assure good-quality service and protect consumers' rights. Enforcement of regulations is one issue calling for special attention in some provinces.
- 2.23 Action lines: (a) public and private **basic infrastructure project finance** (transportation, energy), particularly in the less advanced provinces, to lower costs and make Argentine products more competitive; support for the set-up of the Infrastructure Fund warrants special attention here; (b) **regulation**: strengthen national and provincial compliance monitoring agencies to help redress distortions, make decentralized spending more efficient, heighten competition in the marketplace, and protect consumers; develop enabling regulatory frameworks for private infrastructure investment, including support for tourism development; and (c) support the **diffusion of clean technologies** and development of renewable resources. The private sector will be given a prominent role in supporting public investment and as borrowers.
- 2.24 **Financial sector**: The finance sector has made substantial, albeit uneven, progress. Argentina's capital market is still underdeveloped and further reforms are needed in the pension and insurance industries, notably to bolster regulatory and oversight systems. There are still serious problems in the banking system as far as broad availability and cost of financial services and credit are concerned, particularly for small businesses and those operating in remote or poor regions of the country.

- 2.25 Action lines: (a) **development of the capital,⁶ pension, and insurance markets**, strengthening their regulation, supervision, and organization and better equipping them to boost investment capital and savings; (b) **rationalization of public-sector participation in local and international financial markets**, particularly on the part of subnational governments, to be able to pay for long-term investments; and (c) continue supporting Argentine efforts to **strengthen and develop the banking system** by adopting and maintaining regulatory and oversight systems to ensure that banks are financially sound, efficiently run, and profitable and that they broaden their client base. This could include privatizing national, provincial, and municipal banks where indicated.
- 2.26 **Agriculture sector**: Studies on the provinces show development gaps in some parts of the country, particularly rural areas. Some unresolved problems are small farmers' rudimentary technology and trade and business know-how and the loss of natural capital as soil fertility and water quality deteriorate.
- 2.27 Action lines: (a) **comprehensive rural development programs** that involve local communities closely in shaping a common strategy to come up with cross-sectoral initiatives; one feature of such programs (targeting chiefly small-scale producers) should be productive and social investments to help diversify production and make it more profitable, and also diversify the employment base, reduce poverty, and stem the exodus from the countryside; (b) **sustainable technological, industrial, and business development of key agricultural and agribusiness chains**, by way of support for sectoral policy initiatives and funding for productive and infrastructure projects that encourage private-sector involvement and efficient natural-resources management; (c) **promotion of agricultural and agroindustrial exports**, through technical and financial assistance to adopt modern marketing systems; and (d) **decentralization**, building technical and financial capacity in provincial and municipal agencies that work in the agriculture and agribusiness sector, to involve them more directly in developing the sector.

⁶ The Region is working with PRI to map out a capital market development strategy.

Projects under way	US\$ million*		Lending program	US\$ million
	Approved	Disb.		
795/OC-AR National road corridors	278.0	220.9	AR-0263 Road and rail transp. safety	100.0
802/OC-AR Technology moderniz.	81.7	69.8	AR-0266 Finance sector program	500.0
899/OC-AR Provincial agric. development	125.0	47.4	AR-0269 Infrastructure Fund	TBD
962/OC-AR Port modernization	104.0	20.2	AR-0241 Agric. competitiveness prog. PROCOM	100.0
989/OC-AR Business restructuring	100.0	17.9	AR-0268 Support rural communities PROCOR	5.0
1118/OC-AR Flood emergency	300.0	166.1	AR-0199 Tourism development	25.0
1201/OC-AR Technol. moderniz. II	140.0	12.6	AR-0240 Provincial rural services PROSAP II	100.0
1044/OC-AR Alto Paraná project PRI	60.0	42.7	AR-0279 Production devt. Prov. Río Negro	100.0
1146/OC-AR Trenes de Bs.Aires PRI	75.0	-	AR-0281 Sector program support competitiveness	500.0
1188/OC-AR Puente Rosario Victoria PRI	33.1	-	AR nn Restructuring agric. production	TBD
1294/OC-AR Border cross./integr.corrid.	200.0	-	SUBTOTAL	1,430
1263/OC-AR Autom. transport. safety PPF	1.5	-	PRI AR-nn Wind energy Chubut	14.6
TOTAL	1,498.3	597.6	PRI AR 0258 Aeropuertos de Argentina	75.0
			PRI AR-0236 Córdoba highway	50.0
			PRI RG-0054 BR-AR power grid	75.0
			PRI AR-nn Latin America transportation logistics	75.0
			TOTAL	1,719.6

*Net of cancellations. Disbursements at 31 December 2000.

MIF operations program	US\$ million	TC operations program	US\$ million
Quality certification system	2.0	TC Provincial SME development	0.1
Strength. provincial power industry regulators	1.0	TC Strength. overland integration Argentina-Chile	0.8
Technology Center creation. Loss minimization	2.0	TC Formulac. Infrastructure Fund loan	0.8
Regulat. info. technol. (Regional)	2.0	TC Inst.-strength. air transportation	0.8
Local economic development	2.5	TC Efficient energy services strategy	0.1
Accelerator microenterprise competitiveness	0.8	TOTAL	2.6
Devt. of microleasing for micro and small enterprises	2.0		
Internal competitiveness	2.5		
TOTAL	14.8		

b. Poverty reduction and raising of living standards

- 2.28 **Employment:** Training and retraining services in Argentina and facilities to assist the unemployed are spotty, not of the best quality, and not always available when and where needed. Most of the jobless form part of the informal sector, so they have no unemployment or health insurance and no pension plan. Given the modest GDP growth forecasts for 2001 and the fiscal shortfall it will be difficult to put through job-creation policies. Implementation of the new labor code approved in early 2000 will help modernize the labor market and ease rigidities to help lower employers' labor costs. However, for this to have any effect on employment numbers the country needs steady increases in investment, particularly on the private sector's part.
- 2.29 Action lines: Support reforms to make labor-market conditions more flexible and create jobs, and smooth the interplay of supply and demand in the job market. The Bank will deliver this support through funding for: (a) projects offering **incentives to private investment** (infrastructure, housing, removing barriers to credit, reducing nonwage labor costs); (b) **vocational training**; (c) development and

implementation of **employment and labor-intensive programs** with the aim of shrinking informal-employment figures; and (d) seminars and other events as forums for **discussion of these reforms**. None of these measures could be expected to have an impact in the short term. In December 2000 the Bank approved a quick-disbursing project to help **implement the labor code** and lend support in other areas.

- 2.30 **Social safety net:** Even with the arrangements in place to shield “protected social programs” from spending cuts, the budget-trimming required by the fiscal adjustment is affecting a number of programs that serve low-income Argentinians. Though program targeting has improved considerably in recent years, progress still needs to be made in terms of creating and maintaining indicators of spending efficiency and implementing a system to identify the cost of social services, since many of the country’s programs do not collect the kind of information needed to gauge how effectively they are delivering benefits. Some have no information on beneficiary numbers or per-beneficiary cost. There are a plethora of social protection programs with heavy administrative costs but lackluster results. The government is already taking steps to consolidate these.
- 2.31 Action lines: Continue to work with the government to develop and operate social protection programs—the fight against poverty, Pro-Huerta, fiscal balance and social management—within the constraints of the fiscal adjustment, the aim being to achieve better targeting and more efficient spending. To this end: (a) continue to support the adoption and improvement of **targeting and integration mechanisms** (SISFAM—Master System for Identification and Registration of Families Eligible for Social Programs and Services, and SINTyS—Taxpayer and Social Services Identification System); (b) support the improvement of the **impact assessment systems** to gain a more accurate idea of program outcomes; (c) support the **elimination of overlaps and duplications** in the different social programs through coordination, consolidation, and restructuring; (d) fund studies to identify specific methodologies and systems to measure the **efficiency of expenditures and cost of social services**; and (e) support **equity enhancing and community participation and community development** activities in urban and rural areas in the design, execution, and supervision of social programs.
- 2.32 **Education:** Though Argentina has restructured much of its education system and quality is improving, reforms to enhance the quality of **primary** education are not yet complete in all provinces. Other problems still to be remedied are the low 33% **secondary school** completion rate, the lack of a cost-recovery system in **post-secondary education**, the fact that many provinces do not have the money or technical capability to implement the law mandating ten years of compulsory basic general education, and the teaching hours and leave system that makes for inefficiencies in teacher performance and administrative costs, particularly in secondary schools.

- 2.33 Action lines: Continue furnishing support to the national and provincial governments to improve primary and secondary education. Specifically: (a) provide **institution-strengthening for provincial governments** so they can better plan, execute, and track education-improvement programs and to manage the sector's human resources more efficiently; (b) support the **implementation of programs targeted** to the poorest schools and to students at greatest social and educational disadvantage, to improve the earnings prospects of the very poor; (c) **promote strategies** that seek **internal-efficiency improvements in the education system** to reduce dropout and repeater rates, particularly in secondary schools; and (d) support **implementation of polymodal secondary education** by expanding infrastructure, adapting the curriculum to new marketplace demands, providing teacher training, and using information technology to enhance teaching methods.
- 2.34 **Health**: The public's satisfaction with health-care quality does not reflect the magnitude of health spending (7% to 10% of GDP—one of the highest figures in Latin America). Health care and access to health services is far from uniform. Preventive health care is scarce; health units are inefficient and have little autonomy. There is no capacity for targeting services or recouping their cost and no basic health-care package, particularly for low-income mothers and children.
- 2.35 Action lines: Support provincial efforts to realign human resources and health-care delivery structures as part of a new model that will entail: (a) **enhancing the efficiency and quality of the labor-sponsored obras sociales health plans** by (i) adopting family health models and more effective care management systems, and (ii) introducing financial incentives in fee-for-service systems, to improve care delivery; (b) completely **decentralizing public services** to the provinces and municipalities; (c) **converting public hospitals** to self-managed facilities; (d) **targeting services** to the neediest groups and organizing services in line with client needs and preferences; (e) **progressively integrating the obras sociales plans** into the prepaid care system and **developing a common regulatory framework** to oversee competition strategies between the two arrangements, consumer protection and advocacy mechanisms, and quality assurance and accreditation of companies and *obras sociales* in the sector (minimum acceptable standards); and (f) **progressive restructuring of provincial obras sociales** into health-sector organization and funding agencies in the provinces and **gradual transformation of provincial health ministries** into regulatory and public-health agencies.
- 2.36 **Housing**: There still are some problem areas in government-financed schemes like the National Housing Fund (FONAVI). Funded from fuel-tax proceeds and administered by Provincial Housing Authorities, FONAVI lends at subsidized interest rates. Its loans are not closely targeted and a high percentage of them are in arrears. The country's shantytowns with no basic infrastructure, many of them in floodprone areas, show that low-income housing programs still have considerable work to do.

- 2.37 Action lines: Help: (a) **build a consensus** on a policy that can help ease the shortage of low-cost housing in Argentina; (b) finance housing-system reform, notably the **National Housing Plan**; and (c) fund new **slum rehabilitation** programs to install basic infrastructure and regulate property titles, and thereby shrink the stock of substandard housing.
- 2.38 **Municipal development:** As the decentralization process advances, more and more social and other services are being passed down to local governments. Moreover, it is the municipalities that feel the pressure for good-quality, affordable city services and are responsible for creating an enabling environment for economic activity.
- 2.39 Action lines: Advance and consolidate the decentralization process and further strengthen local governments in such areas as: (a) **transfer to municipalities of a range of city services** that, by their nature, should be delivered by local governments; (b) fostering **partnerships among conurban municipalities** to identify shared problems that may lend themselves to common solutions by virtue of economies of scale or externalities; (c) **efficient spending**; (d) **local revenue generation**; (e) **fiscal discipline**; and (f) **capital market access**.
- 2.40 **Water and sanitation:** This sector's **regulatory, tariff, and institutional framework** does nothing to prize efficient service delivery or meaningful private-sector participation. A large share of the population has no piped water or sewer hookups; sewage treatment and disposal is a particular problem. In part this is because private concession operators have trouble securing funding, and the financial and efficiency problems of provincial and municipal utilities and cooperatives make it hard for them to become self-sustaining or expand their services. There are weaknesses in the sector's regulatory agencies, few of which are independent. Furthermore, in the concession areas it has been difficult to add low-income and rural households to the customer rolls because there is as yet no clear policy on expanding utility services to those segments of the population.
- 2.41 Action lines: (a) **reorganization of the sector:** strengthen incentive mechanisms to attract private investment to the sector and expedite the process; continue to participate in activities required to privatize utilities and make them more efficient; (b) **social development:** help devise systems to expand service to low-income urban households without jeopardizing providers' chances for self-sufficiency, and support the creation of self-sustaining systems in rural areas; and (c) **private sector:** continue to support moves to strengthen regulatory agencies, to give private enterprise an incentive to enter and remain in the water and sanitation sector and deliver quality services.
- 2.42 **Environmental management:** Many Argentine provinces lack a solid environmental management apparatus and agencies with authority and capacity to monitor and enforce environmental regulations. The federal environmental management system is complex and difficult to implement. Because environmental

- standards are not duly enforced and there are too few effective prevention and mitigation programs, the country's natural resources are deteriorating, particularly surface and ground water resources. The prime aims of environmental-sector management should be to improve quality of life, particularly in urban centers, by enhancing air and water quality, managing solid waste and industrial effluent, and so on. In rural areas, work is needed to preserve environmental quality, especially watershed protection, soil management, and wildlife conservation, impacting particularly the quality of life of indigenous populations and the poor.
- 2.43 Action lines: (a) **institutional development**: continue actions to develop and bolster the legal framework and federal and provincial environmental management and compliance monitoring agencies; (b) **environmental protection**: assist the national and provincial governments with initiatives to improve air and watercourse quality, conserve soil and wildlife, protect watersheds, and develop and manage an environmental information system to publicize successful experiences.
- 2.44 **Women in development**: Argentina's female unemployment rate has risen more quickly than the rate for men, as have underemployment numbers for women. The imbalance has worsened in recent years as more and more women join the workforce. Moreover, women's earnings are 75% of men's. Most low-income women work in the informal sector or domestic service (53%), with no benefits and thus no safety net. Poor women need more job opportunities and incentives to train in nontraditional fields that will bring them higher pay and benefits. Women breadwinners are particularly vulnerable and in need of special support.
- 2.45 Action lines: There are many opportunities for Argentina's investment program to tackle the problems and most pressing needs of women, particularly if: (a) **gender considerations** are built into poverty-reduction and employment programs, and (b) social programs, particularly those targeted to vulnerable groups, take into consideration the serious problems of **women heads of household**. Key elements here are efforts by the National Council on Women and the provincial offices to make sure gender issues are duly addressed in the different sector ministries' work and help steer sector policies and strategies in areas that are priorities for women. The institution-strengthening components of the Federal Program for Women (loan 1133/OC-AR) are crucial in this regard.
- 2.46 **Civil society**: Argentina's civil society organizations (CSOs) are advocates for a vast array of causes—environmental protection and the rights of women, consumers, and children, to name a few. According to Justice Ministry data there are 78,392 registered CSOs in the country, 65.6% of them based in the central region.⁷

⁷ City of Buenos Aires and provinces of Buenos Aires, Entre Ríos, Santa Fé and Córdoba.

2.47 Since the Bank's Eighth Replenishment, Argentine CSOs have become much more involved in the design and operation of the country's social projects. Among these are programs to help children and youth at risk and other vulnerable groups, the Federal Program for Women, and various technical-cooperation projects for CSO institution-strengthening. The Argentina Country Office has a Civil Society Advisory Board, one of whose terms of reference is to help come up with ways of involving CSOs in Bank operations in the country.

2.48 Action lines: The Bank will continue to support initiatives to: (a) **build closer relations between government and CSOs**, particularly agencies with poverty reduction and environmental management missions; (b) make CSOs **financially sustainable**, and (c) improve the **sector's organization and dissemination of CSO activities**.

Table II-4 Support for poverty reduction and raising of living standards				
Projects under way	US\$ million		Lending program	US\$ million
	Approved	Disbursed		
552/OC-AR Water supply Bs. Aires- Aguas Argentinas	97.5	74.4	AR-0176 Education program	600.0
760/OC-AR Resettlement Yacyretá	130.0	14.9	AR-0243 Pro-Huerta	27.0
797/OC-AR Reconquista River cleanup	150.0	112.2	AR-0262 Rosario slum rehabilitation	43.0
830/OC and 932/SF-AR Municipal social investments	210.0	145.4	AR-0272 Comprehensive plan to combat poverty	TBD
845/OC-AR Basic education reform	300.0	274.0	AR-0273 Mod. Educ.Mgt. Prov Bs.Aires	350.0
857/OC-AR Rural sanitation VI	200.0	159.9	AR-0274 National Housing Program	600.0
940/OC-AR Slum rehabilitation	102.0	18.1	AR-0245 Yaboti reserve	9.0
1021/OC and 996/SF-AR Assistance to vulnerable groups	33.0	10.9	AR-0236 Water and sewers Bs. Aires Azurix PRI	52.0
1031/OC-AR Productive/employment support	370.0	188.9	AR-nn Water Greater Bs. Aires PRI	50.0
1059/OC-AR Matanza Riachuelo basin cleanup	250.0	3.6	SUBTOTAL	1,721.0
1060/OC-AR Reform nonuniv. higher education	82.5	8.0	MIF Coop. social/labor relations	2.5
1068/OC-AR Investments in major cities	260.0	9.0	SP Diversif. agric.-sugarcane prod.	0.6
1111/OC and 1008/SF-AR Children and youth at risk	20.0	3.5	TC Provincial environmental standards	0.2
1133/OC-AR Federal Program for Women	7.5	1.0	TC Labor-intens.envir.amelioration	0.4
1134/OC-AR Prog. support water sector reform	250.0	5.4	TC Develop. Yaboti reserve project	0.2
1164/OC-AR Municipal reform and development	250.0	8.7	TC Ins.diag.compre. fight against poverty	0.8
1182A/OC-AR Equity investment Aguas Argentinas PRI	75.0	40.0	TC Support for Natl. Council on Women	0.1
1187/OC and 1193/OC-AR Primary healthcare reform	101.0	0.5	TC Azurix project Bs Aires	0.2
1192/OC-AR Global credit micro and small enterprises	100.0	10.4	TC SMEs in local development	0.1
1295/OC-AR Fiscal balance and social management	400.0	-	TC Creation 20 family support centers	0.3
TOTAL	3,388.5	1,088.8	TOTAL	1,726.4

*Net of cancellations. Disbursements at 31 December 2000.

c. Reform of the State and fiscal balance

2.49 **Reform of the State**: The challenge today is to help solidify public-sector reforms by supporting moves to: (a) improve fiscal performance by designing sound fiscal-federalism instruments and institutions; (b) deepen pension reforms; (c) improve the workings of the financial markets; (d) give the public sector better regulatory

- tools; (e) step up the adoption of modern management technologies; (f) lower the “country cost”; and (g) improve the performance of the central government and its agencies by bringing in a simple benchmarking system to track and assess performance, accountability, and outcomes.
- 2.50 Action lines: Continue assisting government efforts to revamp the State apparatus and make it more efficient, particularly actions to: (a) **deepen pension reform**; (b) support **reforms to help rebuild an attractive environment for foreign investment** (mediation and arbitration, intellectual property rights, regulatory frameworks); (c) forge consensus regarding the proposed new **revenue-sharing** scheme (see paragraph 2.16); (d) **enhance public-policy management and public-sector performance and transparency** through institution-strengthening and reforms seeking more efficient procurement and tendering systems and more autonomous operation of public institutions; (e) **strengthen the national accounting and finance system** by improving government audits, strengthening the General Audit Office and making its operations more transparent; (f) build capacity in the central and provincial governments for **census data gathering, national accounting, and economic and social statistics**; and (g) design and implement crime and violence prevention policies to help improve citizen security.
- 2.51 **Fiscal balance**: An important focus of the country’s economic authorities will be the commitment to balance the federal and provincial public accounts in the medium term—this being the cornerstone of the special financial support program mentioned in chapter I. A narrower deficit will mean a better country credit rating and hence a lower cost of capital, all of which will help put the economy back on a growth path.
- 2.52 Action lines: Assist with: (a) actions to help **balance the national and provincial fiscal accounts** by widening the tax base and simplifying the tax and public revenue system, and further strengthen the Federal Public Revenue Administration (AFIP), and (b) projects to **make tax collection more efficient and rationalize public spending**. The Bank can help alleviate the provincial debt situation by funding priority projects in provinces that have already taken steps to improve their debt profile and debt management.
- 2.53 **Decentralization**: Substantial progress has been made on decentralization over the past four years, notably on the spending-responsibility side. Between 1995 and 1999 Argentina’s subnational governments (provinces and municipalities) accounted for 47.7% of the nation’s aggregate public spending and 80% of social expenditure—the highest percentages in the region after Brazil. But decentralization of expenditure was not accompanied by genuine decentralization of taxing authority to the subnational governments, which brought in only 18.3% of the country’s overall tax revenues over that same four-year span. The federal government reserved responsibility for legislating, collecting, and enforcing the heavy-yield taxes (VAT, income tax, etc.) whose revenues it then shares out. The municipalities and

provinces are not institutionally equipped to handle all their new responsibilities, with little sharing or cooperation between the national and provincial governments on taxation matters. Though tax receipts have risen appreciably, tax evasion is still a problem. There is no incentive in the revenue-sharing arrangement for raising funds locally or expending them efficiently—with the ensuing impact on the consolidated fiscal deficit.

2.54 Action lines: (a) help **find spheres for local taxation** with a view to further decentralizing taxation authority to the provinces and municipalities; (b) foster **institution-strengthening and human resources training and development projects** for the national and subnational governments so they can devise and coordinate productive projects with the private sector; (c) strengthen **management capacity** and achieve greater **fiscal discipline, transparency, and spending efficiency**; and (d) support government actions to **build consensuses** by way of seminars, discussion forums, etc., on proposed reforms, including the revenue-sharing system and development of instruments to aid in that process. Particular focuses of support will be vertical cooperation between the provinces and the national government and the provinces' and municipalities' capacity to act in these areas.

2.55 Support for the provinces will take the form of **direct loans** (such as the operations with the provinces of Córdoba and Buenos Aires) or **national loans** benefiting groups of provinces. In direct lending operations the aim will be to promote adoption of an **overall reform framework** to enable governments to quickly take needed measures to improve their operation, making sure that **such initiatives are concordant with national policies**. The Bank also would support these efforts by organizing training workshops on institution-strengthening issues for selected provinces.

Projects under way	US\$ million*		Projects identified	US\$ million
	Approved	Disb.		
826/OC-AR Reform State financial management	47.0	41.7	AR nn Sector program support provinces	500.0
925/OC-AR Preinvestment II	25.0	10.0	AR-0247 Citizen security	100.0
979/OC-AR Support Prov. of Buenos Aires	350.0	322.7	AR-0261 National Census and Nat.Accts.	59.0
1034/OC-AR Instit. support AFIP	96.0	66.0	AR-0264 AFIP strengthening II	95.0
1103/OC-AR Support Prov. of Mendoza	80.0	-	AR-0232 Prog.support regional development	20.0
1107/OC-AR Support Govt. City of Buenos Aires	200.0	10.2	SUBTOTAL	774.0
1163/OC-AR-1 Structural adjustment	2,000.0	2,000.0	MIF Intellectual Property Rights Center	1.7
1163/OC-AR-2 Strength. bank system safeguards	500.0	5.0	MIF Venture capital fund	5.0
1206/OC-AR Inst.strength. foreign trade policy	5.0	-	MIF Regulatory framework tourism concess.	1.8
1082/OC-AR Administration of justice **	1.8	1.8	TC Trading standards GMOs	0.2
1279/OC-AR Inst.strengthening MRECIC	7.5	-	TOTAL	782.7
1287/OC-AR Moderniz.State, Prov. of Córdoba	215.0	-		
TOTAL*	3,527.3	2,457.4		

*Net of cancellations. Disbursements at 31 December 2000.

** Loan cancelled; advances to be accounted for.

d. Regional integration

- 2.56 Since Argentina's transactions with its MERCOSUR partners make up 30% of its foreign trade, that common market plays a prominent role in the country's development strategy. Hence, the aim of many government and private-sector actions is to make the most of Argentina's membership in this trade accord. Sharing a border with each of the expanded MERCOSUR's member states, Argentina is well situated to head up the process of improving access to border crossings—an important goal, since over 60% of traded goods are hauled overland and very few crossings are paved. New infrastructure outlays are essential to make transportation safer and bring down operating costs if Argentina and the region are to become more competitive. Though highway-improvement investments fall largely to the public sector there are a variety of arrangements whereby private enterprise can be brought in at the construction, operation, and maintenance stages.
- 2.57 Action lines: The Bank can do a great deal to help advance the integration process by way of: (a) support for **actions to coordinate infrastructure investment planning** in the region and public and private investment project funding (gas pipelines, roads, ports, electric power transmission systems and airports) and (b) **technical assistance and other facilities to achieve closer integration**, such as support for macroeconomic coordination, institution-strengthening, dispute settlement mechanisms, alignment of laws of the member states, common regulatory frameworks, regional industrial restructuring, export development, and investment promotion programs. Particularly important are programs to help small and mid-sized businesses prospect for export, investment, and joint-venture opportunities with their MERCOSUR partners.

3. Lending scenarios

- 2.58 The **base-case scenario** envisages average annual approvals of US\$1.42 billion in 2001-2003, down slightly from US\$1.47 billion in 1996-2000. This scenario focuses more strongly on programs to reduce poverty and enhance competitiveness, with some specific initiatives for modernization of the State, particularly in the provinces.
- 2.59 The **high scenario**, with more investment loans, would raise the average to US\$1.75 billion. The triggers for this scenario, in the absence of disruptive external factors, would be better performance of the Argentine economy's general indicators and fulfillment of commitments in terms of economic policy and reforms agreed in the context of the IMF-headed financial support program. These circumstances would help continue the downward trend in country risk that began to emerge in the last weeks of December 2000. This would help bring down the cost of capital and rekindle economic growth, with a positive impact on demand for new investments and on fiscal deficit reduction. Another trigger would be more satisfactory portfolio performance. This scenario provides for US\$2 billion in quick-disbursing sector

loans, by virtue of the Bank's participation in the aforementioned financial support program.⁸

- 2.60 Argentina's share of borrowing-country indebtedness to the Bank was 15.1% in 1998 and 1999 and 14.8% in 2000. Under the **high** scenario for 2001-2003 its percentage would climb to 16.6% in 2001 and hold at 17.4% in 2002-2003, as the following table illustrates.

Table II-6					
Exposure ratios					
High scenario					
(percentages)					
	1999	2000	2001	2002	2003
Debt to IDB/IDB portfolio (< 18%)	15.1	14.8	16.6	17.4	17.4
IDB debt service ^{1/} /External public debt service ^{3/} (<30%)	3.9	4.5	4.4	10.2*	11.0
Multilateral debt service ^{2/} /External public debt service ^{3/} (<50%)	8.3	10.4	10.8	23.2*	24.6
IDB debt service/G&S exports (<8%)	3.2	3.6	3.4	7.1	7.0
External public debt service/G&S exports	81.5	79.6	77.9	69.4	63.9
^{1/} Principal and interest payments.					
^{2/} Excluding debt to IMF.					
^{3/} Based on unofficial preliminary IMF forecasts.					

*Repayment begins on emergency loan 1163/OC-AR-1.

4. Studies

- 2.61 In 1999 the Bank completed a study on the new face of Argentina's industrial sector. In 2000 it published two sector-specific studies, one on the banking industry and the other on the pension system, along with regional studies on various topics.

5. Coordination with the Bank Group

- 2.62 **Multilateral Investment Fund (MIF):** The MIF has been very active in Argentina, with 26 operations totaling US\$44.5 million. The average disbursement rate at 31 December 2000 was 43.2%. Three are regional operations (US\$2 million in all).
- 2.63 The MIF has targeted four areas in its support for private enterprise: (i) expansion of private-sector activity, particularly in the water and sanitation sector in various regions; (ii) establishment of commercial dispute resolution mechanisms; (iii) improvements in human-resources productivity, including job skills certification and better occupational health conditions; and (iv) development of micro and small agricultural, industrial, and service businesses by broadening access to capital and to training and business services.

⁸ US\$400 million in funding was approved in 2000 for a sectoral program to support achievement of fiscal balance and social spending.

- 2.64 A number of regional projects are benefiting Argentina in two areas: (i) development of microenterprises and small businesses, giving them readier access to technical assistance and training services, and (ii) greater access for small businesses to investment funds in the technology and environmental areas.
- 2.65 To help spur productivity gains the MIF will focus on innovative projects that can yield lessons for other countries in the region. General focuses of MIF support include: heightening the competitiveness of small businesses, including local-level actions, through technology development and adoption of production quality standards; helping small businesses move into export markets; improving training and credit services for microenterprises, and building local technical capacity in the area of intellectual property.
- 2.66 Two issues falling under reform of the State are intellectual property and competition safeguards. Argentina is eligible for support in three areas in the regional sphere: training in energy-sector regulation, support for information-technology sector regulation, and regional venture capital funds that would benefit small Argentine companies.
- 2.67 **Technical cooperation and Small Projects:** As FSO local-currency availabilities for technical cooperation have dwindled, the use of **trust funds** (TC-Funds), notably the Japan Special Fund, has become very important. There are 15 prospective operations for TC-Funds support in 2001-2002 totaling US\$5.2 million.
- 2.68 **Inter-American Investment Corporation (IIC):** Since it began operating in 1989 the IIC has approved 26 operations for Argentina worth US\$148.2 million. At 31 December 2000 it had 16 operations under way in the country totaling US\$74.6 million—US\$69.6 million in loans plus US\$5 million in equity investments. The bulk of this funding went to the financial services, manufacturing, agroindustry, grain and oilseeds, and mining sectors.
- 2.69 In 2000 the IIC focused heavily on new project promotion and identification, particularly in the larger Argentine provinces. Its country strategy in 2001-2003 will look to: (i) direct loans; (ii) innovative deals with a strong development impact, and (iii) capital market opportunities.
- 2.70 Given the size of the IIC's portfolio in Argentina (where most of its current operations are concentrated), few new approvals are slated for 2001-2003. Priority will go to projects to expand existing companies and structuring deals of a size that would lend themselves to loan syndication. The IIC will continue to handle smaller projects via its lines of credit with Banco de Galicia y Buenos Aires and Banco Río de la Plata, the latter facility having been approved in November 1999.

6. Cofinancing and interagency coordination

- 2.71 **International Monetary Fund (IMF):** In early 2000 Argentina signed a US\$7.4 billion three-year standby arrangement with the IMF. Having achieved agreed targets, it became eligible in March 2000 for 53% of the planned first-year drawings. The following December, as was noted in chapter I of this paper, the country wrapped up negotiations for an adjustment to the current arrangement, backed by a Supplemental Reserve Facility (SRF) program. This gives Argentina access to a total of US\$13.7 billion in IMF funding: US\$11 billion under the standby facility and US\$2.7 billion from the SRF. Drawings are contingent on the country's attaining agreed fiscal, debt, and structural-reform targets.
- 2.72 Execution of the Bank's **current portfolio** and the investment projects in the **lending program** are likewise tied to achievement of the above-noted targets because of their impact on public spending: they could affect the availability of counterpart resources as well as authorizations for externally-funded outlays.
- 2.73 **World Bank:** The IDB and the World Bank have traditionally coordinated their support in Argentina, with complementary financing in priority areas and some cofinanced operations (provincial bank privatization, pension system, provincial agricultural development, structural adjustment, and strengthening of the banking system). The two organizations will continue this approach in future, with a heavier emphasis on complementary lending and occasional cofinancing.
- 2.74 The World Bank's gradual reduction of its Argentina lending program will take average annual approvals from US\$1.5 billion in FY97-FY00 to US\$1.16 billion for FY01-FY03 in the high lending scenario. In future it will be targeting its support to provincial reforms, enhancing public-sector performance, social-sector reforms, and improving services for the poor, particularly in rural areas (see details in the matrix in Annex 3).
- 2.75 **Japan:** Japan has supplied Argentina with US\$3.2 billion for development projects in recent years in the form of operations cofinanced with the IDB and bilateral direct loans. Four of these projects totaling US\$637 million were cofinanced with the Bank (investment sector loan, multisector credit program, Reconquista River cleanup, and AES Paraná). The Export-Import Bank of Japan contributed funding for the provincial bank privatization program (US\$800 million) in concert with the IMF, World Bank, and IDB.
- 2.76 In its cofinancing strategy with Argentina the Japan Bank for International Cooperation (JBIC) targets infrastructure and production-sector projects and private-sector development. For 2000 it envisaged support for the Border Crossing and Integration Corridors project. Because of Argentina's high income level it is not eligible for JBIC soft loans.

- 2.77 **Other agencies:** The European Investment Bank has furnished US\$208 million in funding for projects involving highway corridors, natural gas, and water and sanitation for Aguas Argentinas. The bulk of its assistance goes to the private sector. The European Commission provides consulting services on a nonreimbursable basis.

7. Strategy monitoring mechanisms

- 2.78 The following will be the chief means of monitoring the Bank's strategy: (i) benchmarks against which to measure progress on the strategy's implementation and development impact (see Annex 3); (ii) annual programming missions to come up with operations that pursue the strategy objectives; (iii) annual portfolio reports; and (iv) midway through the cycle, a specific strategy-monitoring mission.

III. RISKS

- 3.1 The success of the strategy proposed here is directly contingent on Argentina's progress toward the economic targets agreed to in the IMF-led financial support program. One possible risk is that the economy might take longer than expected to pick up, with everything this would entail for the fiscal accounts, investment, employment, and portfolio execution. The government then would have to rearrange investment priorities to be able to tackle the most pressing needs. A second risk is that the institutional apparatus might not be equipped to satisfy all the operations' technical and timing requirements. To avert problems in this regard, institution-strengthening components have been provided for as needed. A further risk has to do with how quickly the provincial deficits can be trimmed, given the implications for future direct lending to the provinces.

IV. AGENDA FOR A COUNTRY DIALOGUE

- 4.1 The following are some key issues proposed for the country dialogue: (i) kinds of IDB operations that can help improve employment levels, spur economic growth, and strengthen the public accounts; (ii) budgetary authorization for the use of Bank and counterpart resources; (iii) portfolio execution; (iv) modernizing the workings of government and fiscal decentralization; (v) capital market development; (vi) the private sector's role in economic development; and (vii) regional integration.
- 4.2 Among the proposed vehicles for this dialogue are (i) issue-specific studies, (ii) seminars with Bank staff or external consultants, and (iii) specific dialogue missions.

BANK ACTION AREAS, 1996-2000¹

Modernization of the State, including provinces and municipalities:

- Consolidation of public-sector budget, administrative and financial reforms and improvements in the quality of information available on the workings of government.
- Improving revenue collection efficiency by strengthening fiscal management for tax and customs compliance enforcement.
- Self-sustaining municipal development by achieving greater tax, financial, and operations efficiency and enabling capital-market access.
- Enhancing the quality of services by way of concession arrangements or privatization's of public utilities.
- Strengthening financial-sector safeguards.

Spurring productivity and competitiveness:

- Delivery, with private-sector involvement, of essential infrastructure services required by the production sector (rehabilitation, expansion or construction of roads, ports, storage depots, electricity and gas systems, etc.).
- Actions to achieve sustainable growth in agricultural and agribusiness production.
- For SMEs, expanding access and availability of credit and nonfinancial services to spur competitiveness through business realignment and technology development programs.
- Support for business development with integrated export growth and quality enhancement measures.
- Pioneering moves to build emergency preparedness capacity in natural-disaster management agencies.

Poverty reduction and raising of living standards:

- Initiatives to cushion the impact of economic adjustments on the social sectors.
- Comprehensive assistance for vulnerable groups, with heavy community involvement and development of an institutional network to make it easier for these groups to obtain social services.
- Urban development with job-creation potential, to improve living conditions in low-income urban households.
- More vocational training and job counseling to put larger numbers of poor young people to work.
- Increase in coverage and efficiency of health, education, and sanitation services and environmental and natural-resources management.
- Improvement of social-sector management.

¹ Many operations are still under way. Their full impact will be felt in the medium and long term.

ARGENTINE REPUBLIC
2001-2003 LENDING PROGRAM
(US\$ MILLION)

	RS ¹	PLS ²	CDP ³	Status
PROJECTS 2001-A				
AR-0262 Slum rehabilitation Ciudad Rosario		43		Approval slated first half 2001
AR-0266 Finance sector program⁴			500	Profile I
AR-0280 Sector program to support provinces⁴	500			Idea
AR-0176 Education program		600		Profile I
AR-0232 Program of support for regional development	20			Profile I
TOTAL 2001 A	520	643	500	1,663
PROJECTS 2001-B				
AR-0261 Prep National Census and National Accounts	59			Profile II
AR-0243 Pro-Huerta project		27		Profile II
AR-0247 Citizen security	100			Profile I
TOTAL 2001 B	159	27		186
PROJECTS 2002				
AR-0267 Tourism development			25	Idea
AR-0281 Sector program to support competitiveness⁴			500	Idea
AR-0274 Housing sector program⁴		500⁵		Idea
AR-0273 Modernization education and management Prov. Buenos Aires		350		Idea
TOTAL 2002		850	525	1,375
PIPELINE				
AR-0272 Comprehensive plan to combat poverty		TBD		Idea
AR-0263 Road and rail transport safety			100	Profile I
AR-0264 Strengthening AFIP II	95			Profile I
AR-0245 CTR Sustainable management Yaboti Reserve		9		Profile I
AR-0268 Support for rural communities- PROCOR			5	Idea
AR-0269 Infrastructure Fund			TBD	Profile I in preparation
AR-0241 PROCOM agricultural competitiveness program			100	Profile I
AR-0279 Development of production Prov. of. Río Negro			100	Idea
AR-n/n Restructuring agricultural production			TBD	Idea

	RS¹	PLS²	CDP³	Status
AR-0240 Provincial Agriculture Services (PROSAP II)			100	Profile II
TOTAL PIPELINE	95	9	405	509
GRAND TOTAL	774	1,529	1,430	3,733
Percentage	20.7	41.0	38.3	100%

¹ RS: Consolidate reform of the State.

² PLS: Reduce poverty and raise living standards.

³ CDP: Make domestic production more competitive.

⁴ The four operations in bold are part of the Bank's contribution to the Special Financial Support Program coordinated by the IMF. Added to the program to support fiscal balance and social management, approved in December 2000, they total US\$2.4 billion. These resources are earmarked to finance public-sector reforms.

⁵ May include a US\$100 million- US\$150 million investment component.

**MATRIX OF BANK ACTIONS IN ARGENTINA
2001-2003**

GOVERNMENT ACTIONS AND POLICIES	THE BANK'S STRATEGY	PROPOSED BANK ACTIONS	OTHER AGENCIES (US\$ million)	BENCHMARKS TO MONITOR GOVERNMENT AND BANK ACTION
Sustainable economic growth and increased competitiveness				
<ul style="list-style-type: none"> - Make the productive system more competitive and efficient, chiefly by way of the Competition Plan, support for SMEs, and the Labor Reform Law. - Spur exports. - Develop alternative public-infrastructure finance sources (Infrastructure Fund). - Revamp the telecommunications industry regulatory framework. - Strengthen the financial system. - Spur local capital, pension, and insurance market development. 	<ul style="list-style-type: none"> - Fund activities that can help maintain an enabling environment for investment and competition and also build government capacity for promoting productive and infrastructure projects. 	<ul style="list-style-type: none"> - Foster competitiveness through operations to help make public and private service delivery more efficient (AR-0281: Sector program to support competitiveness; TC: SME development at provincial level). - Support initiatives to bolster businesses' export capacity (AR-0241: PROCOM agricultural competitiveness program; AR-nn: Restructuring agricultural production). - Help solidify and develop the financial and banking system, capital market, pension fund and insurance industries (AR-0266: Finance sector program). - Infrastructure improvement, rehabilitation, and expansion (energy, transportation, etc.) with public and private financing (PRI, AR-nn: Chubut wind energy; AR-0258: airports in Argentina; AR-0236: Córdoba highway; RG-0054: BR-AR electric interconnection; AR-nn: Latin American Logistics; TC: Strengthening of Argentina-Chile overland integration; institutional strengthening of air transport; energy efficiency services strategy). 	<p>World Bank (WB):</p> <ul style="list-style-type: none"> - Support for infrastructure that can lower logistical costs, with private financing. [private infrastructure financing; support for sustainable fisheries (\$5); rural infrastructure for the poor (\$75); urban infrastructure (\$250)] 	<ul style="list-style-type: none"> - Government - Renewed economic growth, with GDP growth rates of 2.5%, 3.8% and 4.3% in 2001, 2002 and 2003 respectively. - 28% increase in exports between 2000 and 2003. - Improved financial system performance indicators with lower interest rates. - Bank - Funding for expansion of public and private installed infrastructure capacity, in particular startup of Infrastructure Fund. - Improvement of infrastructure in 33 airports awarded under concessions. - Expansion of electric energy export capacity to Brazil by 1000 MW. - Lowering of the informal employment rate in the productive sectors, by simplifying the job registry system (uniform system for registration of employment contracts). - Fostering of SME productivity increases.

GOVERNMENT ACTIONS AND POLICIES	THE BANK'S STRATEGY	PROPOSED BANK ACTIONS	OTHER AGENCIES (US\$ million)	BENCHMARKS TO MONITOR GOVERNMENT AND BANK ACTION
		<ul style="list-style-type: none"> - Support creation and operation of the Infrastructure Fund (AR-0269: Infrastructure Fund; TC: Infrastructure Fund loan formulation). - Promote transportation safety (road, air, rail) (AR-0263: road and rail transport safety). - Various operations to help develop the production sectors at the provincial and local level. (AR-0268: support for rural communities—PROCOR; AR-0240: provincial agriculture services—PROSAP II; AR-0279: development of production Prov. of Río Negro) - Regulatory frameworks for infrastructure (various operations). - Tourism development (AR-0199). 		<ul style="list-style-type: none"> - Enhanced capacity in the financial system for investment promotion. - Amendments to Pension Law submitted to Congress to enhance transparency, simplification, and competition in the private pension administration market. - At least 25% of the claims of local enterprises against the National Reinsurance Institute (INDER) settled.
Poverty reduction and raising of living standards				
<ul style="list-style-type: none"> - Employment: Labor Reform Law, Emergency Employment Program, Permanent Productive Employment Plan (municipal), <i>Trabajar</i> Program. - Municipal development: Major urban agglomerations. - Consolidate social assistance programs (Plan to Combat Poverty, particularly the Solidarity Plan). - Make the social security system more equitable and sustainable (pension reform). 	<ul style="list-style-type: none"> - Support projects to create jobs and improve access, coverage, and quality of basic education, health, sanitation, and environmental services and make spending more efficient. 	<ul style="list-style-type: none"> - Support for social reforms, including housing sector (AR-0274: national housing program), the Plan to Combat Poverty (AR-0272: comprehensive plan to combat poverty; AR-0243: Pro-Huerta; SP: agricultural diversification for sugarcane growers; TC: intensive environmental improvement and manpower; TC: formulation of Yabotí Reserve project; TC: institutional diagnostic assessment of comprehensive plan to combat poverty; TC: establishment of 20 family support centers; TC: support for National Women's Council), and projects in education (AR-0176: education 	<p>WB:</p> <ul style="list-style-type: none"> - Health sector reforms [comprehensive health project (\$150)]. - Improvement in services for the poor [social safety net program 6 (\$250); social reform (\$300); social safety net 5 (\$30); rural poverty program 	<ul style="list-style-type: none"> - Government - Better targeting of population segments living in extreme poverty, taking services to 400,000 families with unmet basic needs by the end of 2005. - Passage of the Pension Reform Law to improve pensions for low-income groups. - Expansion of basic utilities infrastructure coverage (water and sewers) and improved quality control and efficiency of services.

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<ul style="list-style-type: none"> - Services for children in need (<i>Identidad</i> plan). - Ease the housing shortage—National Housing Plan. - Health-care reform (PAMI, for retirees). - Strengthen environmental management. 		<ul style="list-style-type: none"> program; and AR-0273: modernization of education and management, Prov. Bs. Aires), sanitation (water and sewerage Azurix and Water, Greater Bs. Aires), slum rehabilitation (AR-0262: Rosario), and environment (AR-0245: Yabotí Reserve; TC provincial environmental regulations). - Support for SISFAM to improve targeting of social spending and make it more efficient (1295/OC-AR: fiscal balance and social management; TC: SMEs in local development; and MIF cooperation socio-labor relations. 	<ul style="list-style-type: none"> for indigenous communities (\$5); PROFAM (\$5)]. - Secondary education program (\$257); education program (\$100). - Sanitation: watershed management (\$35); storm sewers (\$100); potable water (\$40). 	<ul style="list-style-type: none"> - Bank - Reduction of the low-income housing sector deficit by 10% by 2005. - 100,000 retention scholarships per year for students at risk for dropping out of school due to their families' unemployment or low income status, beginning in 2002. - 21,000 elementary schools with access to communication network and virtual learning in 2005. - Consolidation of 71 social programs in about 10 major areas in 2003. - Creation of incentives to reduce labor costs, lower the informal employment rate and improve job stability. In particular: uniform employment-contract registration system and reporting system on pension fund management company performance in place. - Implementation of the employment office system in four jurisdictions by 2002. - SINTYS (national tax and social security identification system) operating in 2002. - Coverage of a population of close to three million in the Province of Buenos Aires and in Greater Buenos Aires, through greater private-sector participation in water supply and sanitation investment finance.

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				<ul style="list-style-type: none"> - Legal framework for federal and provincial environmental management and compliance monitoring strengthened. - Improvements in air and watercourse quality, industrial effluent and solid waste management, soil management, etc.
Reform of the State and fiscal balance				
<ul style="list-style-type: none"> - Reduce the deficit via the Economic Emergency Law, rationalization of public spending, tax reform, curbing tax evasion, asset sales, and operational transparency. - Fiscal Responsibility Law. - Federal Pact (Law 25,235) to trim provincial government deficits (including pension system). - New Federal Tax Revenue-Sharing Law. - Pension system reform. - Improve the regulatory framework. - Enhance citizen security. 	<p>Support:</p> <ul style="list-style-type: none"> - Consolidation of ongoing reforms. - Further mechanisms for decentralizing public-sector operations and making them more transparent. - Institution-strengthening. - Initiatives to maintain economic stability. 	<ul style="list-style-type: none"> - Support measures to develop instruments needed to build a consensus on reforms, particularly regarding revenue-sharing (AR-0280: sector program, support to provincial governments). - Strengthen financial and tax administration and institution-strengthening programs to improve the workings of government and public-policy management at the national, provincial, and municipal level (AR-0264: strengthening AFIP II; MIF risk capital investment fund; TC trade rules OGMs). - Regional development of the less advanced provinces (AR-0232: regional development support program). - Improve regulatory frameworks (MIF) (intellectual property rights and regulatory framework tourism concessions). - Complete social security reform (1295-OC/AR: fiscal balance and social management). 	<ul style="list-style-type: none"> - WB: Support for provincial reforms; strengthening of workings of government [reform programs in the Provinces of Córdoba (\$303), Catamarca (\$70.7), and Santa Fé (\$300); provincial reform 3 (\$150); provincial reform 7 (\$150); municipal reform (\$300); Judiciary reform (\$50); fiscal relations between the Nation and the Provinces (\$300); public sector reform (\$400)]. - IMF: Fostering macroeconomic adjustment (Special Financial Support Program). 	<ul style="list-style-type: none"> - Government - Achievement of deficit-reduction targets until the deficit is erased in 2005, pursuant to the agreement with the IMF. - Better public safety indicators. - Widening of the tax base, simplification of the tax and public revenue systems and reduction in tax evasion. - Implementation of Federal Commitment. - Bank - Support the implementation of the new legal and institutional framework that will govern fiscal relations between the Federal Government and the provinces. - Signature of performance contracts with three entities to improve indicators of efficiency, effectiveness, and transparency of public-sector operations. - Signature of agreements for the implementation of commitment letters with citizens in three national government institutions.

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		<ul style="list-style-type: none"> - Promote violence prevention programs (AR-0247: citizen security). 		<ul style="list-style-type: none"> - Startup of the new ANSES administrative, financial, and accounting information system. - Improved dialogue and heavier involvement of civil society in assessments of public-service quality. - Enhanced capacity for more complete compilation of data and economic statistics in the central and provincial governments..
Regional integration				
<ul style="list-style-type: none"> - Liberalize trade within and beyond MERCOSUR. - Work out agreements with MERCOSUR members to harmonize statistics and economic and social policies. 	<ul style="list-style-type: none"> - Help advance regional integration. 	<ul style="list-style-type: none"> - Financing for physical integration with Chile and actions to achieve closer integration (AR-202: border crossings and integration corridors). 	<p>JBIC:</p> <ul style="list-style-type: none"> - Participation in financing to improve border crossings. 	<ul style="list-style-type: none"> - Government - Trade negotiations in the context of MERCOSUR and other trade agreements. - Coordination with MERCOSUR members to set fiscal, monetary, public-debt, and other targets. - Bank - Expansion and improvement of regional-integration infrastructure in the areas of energy and transportation. - Support the development of macroeconomic and investment-planning coordination in MERCOSUR countries. - Regulatory framework harmonization in the energy and transportation sectors.