PUBLIC
SIMULTANEOUS DISCLOSURE

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

URUGUAY

FINANCIAL SYSTEM REFORM SUPPORT PROGRAM

(UR-L1108)

LOAN PROPOSAL

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ABBREVIATIONS

AFAP	Pension Fund Administrators
ANCAP	National Fuels, Alcohol, and Portland Cement Administration
ANP	National Port Administration
ANTEL	National Telecommunications Administration
BCU	Central Bank of Uruguay
BROU	Banco de la República Oriental del Uruguay
COPAB	Banking Savings Protection Corporation
FSAP	Financial Sector Assessment Program
IMF	International Monetary Fund
MEF	Ministry of Economy and Finance
MSMEs	Micro, small, and medium-sized enterprises
NFPS	Nonfinancial public sector
OECD	Organization for Economic Cooperation and Development
OPP	Budget and Planning Office
OSE	State Sanitation Company
PCU	Program coordination unit
POS	Point of sale
PPP	Public-private partnership
SMEs	Small and medium-sized enterprises
SNIP	National Public Investment System
SOE	State-owned enterprise
SSF	Financial Services Superintendency
TFP	Total factor productivity
UTE	National Administration of Electric Power Generation and Distribution
VAT	Value-added tax
WEF	World Economic Forum

Project Summary

Uruguay
Financial System Reform Support Program
(UR-L1108)

<table>
<tr><th colspan="5">Financial terms and conditions</th></tr>
<tr><td colspan="3" rowspan="2">Borrower: Eastern Republic of Uruguay</td><th colspan="2">Flexible Financing Facility</th></tr>
<tr><td>Amortization period:</td><td>20 years</td></tr>
<tr><td colspan="3" rowspan="3">Executing agency: Ministry of Economy and Finance (MEF)</td><td>Original weighted average life:</td><td>maximum 12.75 years</td></tr>
<tr><td>Drawdown period:</td><td>3 years[a]</td></tr>
<tr><td>Grace period:</td><td>[b]</td></tr>
<tr><th>Source</th><th>Amount (US$)</th><th>%</th><td>Inspection and supervision fee:</td><td>[c]</td></tr>
<tr><td rowspan="2">IDB (Ordinary Capital)</td><td rowspan="2">250 million</td><td rowspan="2">100</td><td>Interest rate:</td><td>LIBOR-based</td></tr>
<tr><td>Upfront fee:</td><td>50 basis points</td></tr>
<tr><td rowspan="2">Total</td><td rowspan="2">250 million</td><td rowspan="2">100</td><td>Standby fee:</td><td>25 basis points[c]</td></tr>
<tr><td>Approval currency:</td><td>United States dollars from the Ordinary Capital</td></tr>
<tr><th colspan="5">Project at a glance</th></tr>
<tr><td colspan="5">Project objective/description:
The objective of the program is to improve the financial system’s contribution to economic growth in Uruguay by: (i) improving financial regulation and supervision; (ii) developing regulations and instruments to foster the financial inclusion of households and companies; and (iii) strengthening institutions and regulations aimed at providing long-term finance.
This operation is the first of two consecutive operations that are linked on a technical level, but financed separately as programmatic policy-based loan (PBL) operations with a deferred drawdown option.</td></tr>
<tr><td colspan="5">Special contractual conditions precedent to the single loan disbursement:
Disbursement of loan proceeds is subject to fulfillment, to the Bank’s satisfaction, of the policy reform measures described in the program components and envisioned in the Policy Matrix (Annex II), in addition to the other conditions established in the loan contract (paragraph 3.2).</td></tr>
<tr><td colspan="5">Exceptions to Bank policies: None</td></tr>
<tr><td colspan="5">Project qualifies as:[d] SV ☑ PE ☑ CC ☐ CI ☐</td></tr>
</table>

[a] The operation will use the “policy-based loan with a deferred drawdown option” modality (document GN-2667-2), which establishes an original drawdown period of up to three years from the date of eligibility for disbursements, with an option for a one-time renewal of another three years. The renewal of the drawdown period will be subject to payment of a renewal fee of 50 basis points on the undisbursed balance.

[b] The grace period will depend on the amortization schedule agreed between the borrower and the Bank when the disbursement request is formalized during the drawdown period.

[c] The standby fee and inspection and supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank’s lending charges, in accordance with the relevant policies.

[d] SV (Small and Vulnerable Countries); PE (Poverty Reduction and Equity Enhancement); CC (Climate Change, Sustainable Energy and Environmental Sustainability); CI (Cooperation and Regional Integration).

I. Project Description and Results Monitoring

A. Background, problem addressed, and rationale

1.1 **Macroeconomic context.** From 2003 to 2014, Uruguay grew at an annual average rate of 5%, driven by the agroindustrial and service sectors. In 2014, per capita GDP reached US$16,882. At the same time, poverty fell significantly, from 33% of the population in 2006 to 10% in 2014. However, the economy has begun to slow over the last three years, growing by 3.5% in 2014. Prospects for 2015 and 2016 are for still lower rates of growth, of between 1.5% and 2.5%. The deceleration in economic activity is the result of slower growth of important trading partners (such as Brazil, Argentina, and China), as well as exchange rate appreciation with respect to Brazil, declining commodity prices, and a possible increase in interest rates in the United States. Analysis of the long-term performance of the Uruguayan economy reveals a highly volatile growth path, with recurring crises and few episodes of accelerating growth. On the fiscal front, a primary deficit of 0.6% of GDP was recorded in 2014, with an overall deficit of 3.5%, while nonfinancial public sector (NFPS) debt was 43% of GDP. Although the current imbalance in the public finances is manageable in the short term, its high level has led the government to announce, as part of preparations for the Budget Law for the 2015-2019 period, a projected reduction of one percentage point of GDP in the fiscal deficit by the end of 2019. Under this scenario, NFPS financing needs would average around US$2.631 billion per year over the 2016-2020 period, representing approximately 4.7% of GDP. Given the current macroeconomic context, various assessments[1] agree that the challenge in coming years will be to ensure that the conditions are in place for the Uruguayan economy to embark on a stable path of sustained growth. This, in turn, will allow a deepening and consolidation of social gains.

1.2 **Economic and productive structure.** The country's main economic sectors are transportation and communications (16.5% of GDP); commerce, hotels, and restaurants (13.5%); manufacturing (13%); and other services (40%).[2] The structure of the economy is characterized by the importance of micro, small, and medium-sized enterprises (MSMEs), which account for 97% of businesses, 70% of private employment, and 40% of GDP. Although levels of productivity in the country's economy have grown over the last decade, they remain low. A recent study[3] shows that total factor productivity (TFP) growth over the 1960-2011 period was systematically lower than in the developed countries and other countries in the region. While in 1960 total TFP in Uruguay was, in relative terms, 75% of that in the United States, in 2011 it was just 40% (compared to 77% in Chile and 60% in Argentina).[4] Given the impact of TFP on growth,[5] the low

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[1] International Monetary Fund (IMF), Financial Sector Assessment Program (FSAP), 2012. IMF Article IV, 2015. World Economic Forum (WEF), The Global Competitiveness Report 2014-2015.

[2] Central Bank of Uruguay, GDP by industry, 2014.

[3] Fernández-Arias, E., Productivity and Factor Accumulation in Latin America and the Caribbean: A Database (2014 Update), Research Department, IDB, 2014.

[4] Ministry of Industry, Trade, and Tourism, Reporte de MIPYME [MSMEs Report], 2011.

[5] There is broad consensus that differences in per capita income across countries cannot be fully explained by differences in factor accumulation. Instead, TFP accounts for a significant share of these differences (IDB, 2014; Jones and Romer, 2010; Easterly and Levine, 2002; Klenow and Rodríguez-Clare, 1997).

productivity of the Uruguayan economy could become an important hurdle to growth over the long term. Another factor limiting the country's growth is low accumulation of physical capital. Although infrastructure investment has increased gradually in recent years as a result of foreign direct investment, demand substantially exceeds installed capacity.[6]

1.3 **The importance of the financial system for development.** The financial system performs a critical role in economic growth and welfare,[7] facilitating, *inter alia*: (i) the intertemporal smoothing of household and business consumption, reducing liquidity constraints and negative welfare shocks; (ii) maturity transformation, channeling short-term savings into long-term investments, and freeing up resources for key investments such as infrastructure; (iii) the channeling of funds to the most productive agents and projects; and (iv) mitigation of the impact of volatility and macroeconomic shocks. Although Uruguay has made important progress with respect to financial regulation and supervision, thus enhancing the soundness of the financial system,[8] the depth of its financial system is still relatively low compared to other countries in the region.[9] In 2014, Uruguay ranked eighty-fifth in the financial development index compiled by the World Economic Forum (WEF)—below Colombia (70), Chile (19), Brazil (53), and Peru (40). According to the WEF, the financial development pillar is, together with innovation, the one with the greatest impact on a country's competitiveness and development. To address this challenge and improve the financial system's contribution to growth in Uruguay, different diagnostic assessments[10] agree on the importance of continuing to improve financial regulation and supervision; of developing instruments to foster more inclusive financial development; and of strengthening institutions involved in long-term financing, so as to meet the infrastructure and investment needs of the productive sector without affecting fiscal stability.[11]

1.4 **Regulation, supervision, and development of the financial system and growth in Uruguay.** In order for the financial system to attain a level of development that maximizes its contribution to economic growth, regulation must attempt to ensure levels of stability that allow agents to make decisions in a predictable environment. At the same time, adequate financial system regulation

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[6] Aportes para la Agenda de Mejora: La competitividad y el desarrollo de Uruguay [Contributions to an Agenda for Improvement: Competitiveness and Development in Uruguay], Uruguayan Chamber of Industry, Uruguayan National Chamber of Commerce and Services, Rural Association of Uruguay, Chamber of Commerce, and the Rural Federation, August 2013.

[7] Beck, T., R. Levine, and N. Loayza, Finance and the Sources of Growth, Journal of Financial Economics 58 (12), 261-300, 2000.

[8] IMF data show that Uruguay has satisfactory levels of regulatory capital as a percentage of risk-weighted assets (13%); of liquidity, measured as liquid assets as a percentage of total liabilities (57%); and of past-due loans, measured as nonperforming loans as a proportion of total loans (2%). Levels of past-due loans are similar to, or better than, the median level for countries such as Brazil, Chile, and Colombia (15%, 30%, and 3%, respectively). August 2014 data for Uruguay; 2013 data for the other countries (IMF Article IV, 2015).

[9] Financial depth in Uruguay, measured as private sector credit as a percentage of GDP, was 27% in 2014—far from the median for LAC-5 (Brazil, Chile, Colombia, Mexico, and Peru) (36%).

[10] IMF, FSAP, 2012. IMF Article IV, 2015. WEF, The Global Competitiveness Report 2014-2015, 2014.

[11] The country's infrastructure financing needs over the next few years are substantial, at 3.3% of GDP per year (equivalent to US$265 million per year from 2012 to 2020).

and supervision are key to further developing the system without compromising its stability. They make it possible to avert financial crises, the effects of which undermine confidence in the financial sector, thus limiting growth in savings and potential growth in intermediation, forcing participants to leave the capital markets, and curtailing the availability of medium and long-term financing. The importance of financial regulation and supervision is shared by analyses that evaluate the impact of structural reforms on growth; these highlight such regulation and supervision as one of the most important factors for growth.[12]

1.5 **The current context in Uruguay.** The country's financial system[13] comprises financial institutions and the capital market. Formally, financial institutions are divided into financial intermediary institutions (13, comprising 2 public banks, 10 private banks, and 1 cooperative); consumer credit companies (34); finance companies (5); external financial institutions (4); Pension Fund Administrators (AFAP) (4); financial services companies (25); and money exchanges (59). In terms of the regulatory framework, the Central Bank of Uruguay (BCU) is responsible for monetary policy and financial system supervision, as well as acting as lender of last resort. Within the BCU, the Financial Services Superintendency (SSF) is responsible for supervision and regulation of the system and its participants (including the AFAPs). The role of the Banking Savings Protection Corporation (COPAB) is to guarantee bank deposits. Uruguay's financial system shrank significantly in the wake of the 2002 crisis, as a result of asset losses at local private banks.[14] Since then, the government has moved forward with a decisive reform agenda aimed at improving financial system stability as a foundation for sustained economic growth. These measures include the implementation process for the Basel II standards,[15] as well as a risk-based supervision methodology. In particular, banks' exposure to exchange rate risk requires close monitoring. U.S. dollar-denominated bank credit to the non-tradable sector accounts for a third of total credit to the private sector (7% of GDP), and constitutes a significant vulnerability for the system. The government has also promoted measures to mitigate exchange rate risk, and these have been acknowledged by the international institutions (see IMF Article IV). At this point in time, continuing the regulatory improvement process is critically important to addressing current challenges, which stem from international financial volatility, an expected deterioration in financial conditions, and the persistence of a stronger dollar.[16]

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[12] Evaluations of structural reforms in this area show highly significant effects on productivity and growth. These effects are quantitatively significant: reforms to the business environment can lead to increases in TFP and production ranging between 20% and 58%, and 7% and 19%, respectively. See Norris, D. et al., Reforms and Distance to Frontier, IMF Discussion Note, 2013, which uses regressions based on similar income levels to show that adequate financial regulation is important at any level of income. For the specific case of Uruguay; and IMF, FSAP, 2012. See also studies that link financial reforms and improved factor allocation in the economy in Larrain, M. and S. Stumpner, (2013), Financial Reforms and Aggregate Productivity: The Microeconomic Channels, New York, New York: Columbia University.

[13] Central Bank of Uruguay, Financial System Structural Report, 2013.

[14] From 2003 to 2004, credit to the private sector as a percentage of GDP fell from 43.2% to 24.2%. Since then, it has remained at levels of between 20% and 27%. World Development Indicators.

[15] The Bank has supported this process through the Program to Strengthen the Financial Services Superintendency (SSF) (2228/OC-UR).

[16] IMF Article IV, 2015. See the Financial Sector Note (IDB, 2015) for a full diagnostic assessment.

1.6 **Pending challenges.** Given the risks described and the high level of dollarization in Uruguay's financial system, international diagnostic assessments agree on the need to strengthen financial system regulation and supervision in three main areas: (i) institutional strengthening of the bodies responsible for both financial system supervision and regulation and publishing the financial information of supervised entities; (ii) implementation of Basel III standards in the financial system with a view to strengthening banking sector regulation, supervision, and risk management; and (iii) improved financial transparency, with the aim of improving financial system efficiency, ensuring improved financial risk management, and reducing the likelihood of a systemic crisis with consequent negative impacts on the country's growth.

1.7 **Financial inclusion, growth, and improved social welfare.** The economic literature shows that greater participation of the population in the financial system through financial inclusion stimulates growth and reduces inequality and poverty.[17] Greater financial inclusion facilitates greater resource flows to households and companies (or the more efficient and secure management of those flows), and this, in turn, improves the ability to withstand negative shocks, smoothing consumption, expanding economic, educational, and health-related opportunities, and boosting investment levels. Access to and use of electronic payments produces benefits in the form of lower transaction costs for households. These are reflected in lower physical and opportunity costs, generating savings that can reduce the depletion of assets.[18] All of this has a positive impact in terms of reducing vulnerability, inequality, and poverty among the population.

1.8 **The current context in Uruguay.** Levels of financial inclusion in Uruguay are below the average for the region, owing to scant use of financial services.[19] Data for 2014 show that only 45% of adults have an account in a formal financial institution (compared to an average of 95% in countries belonging to the Organization for Economic Cooperation and Development [OECD]). Moreover, the active use of accounts is very low, with only 16% and 6% of the population using them to receive salaries and pay for public utilities, respectively (61% and 44% in the OECD countries, respectively). Only 38% of the population has a debit card (80% in the OECD countries). Recent empirical evidence[20] shows that the use of financial services is most limited among the lowest social strata, which, in turn, limits their general access to credit (given their lack of credit history), as well as their ability to use alternative means of payment and improve management of their assets. In terms of banking infrastructure, the country falls

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[17] See, for example, Bruhn, M. and I. Love, The Economic Impact of Banking the Unbanked: Evidence from Mexico, Working Paper 4981, World Bank, 2009; Park, I. and F. Mercado, Financial Inclusion, Poverty, and Income Inequality in Asia, Asian Development Bank, Working Paper, 2015; IMF, Financial Inclusion: Can It Meet Multiple Macroeconomic Goals?, September, 2015. For an evaluation of a context similar to that of Uruguay, see Karpowicz, I., Financial Inclusion, Growth and Inequality: A Model Application to Colombia, IMF Working Paper, 2014.

[18] Jenny Aker et al., Zap It to Me: The Short-term Impacts of a Mobile Cash Transfer Program, 2011.

[19] This refers to the depth of financial services usage, reflected in the number of financial products that can be accessed by individuals and the frequency of their use.

[20] Sanromán G. and G. Santos, Who Holds Credit Cards and Bank Accounts in Uruguay? Economics Department, University of Uruguay, 2014.

below the average for Latin America and the Caribbean in terms of both the number of automated teller machines per km^2 and the number of bank branches (6.5 per 100,000 adults in Uruguay, compared to 21.1 in the region). Only 3% of the population aged 15 or older makes payments online, compared to 11% in Chile, 17% in Brazil, and 53% in Europe. Shortcomings in the area of financial inclusion represent a substantial challenge in terms of the financial system's ability to perform its key role in promoting growth (see above).

1.9 **Pending challenges.** To improve financial inclusion, Uruguay needs to make progress in three areas: (i) implementing a financial inclusion law to establish the regulatory framework for the sector, as a tool for social development and inclusion; (ii) issuing regulations relating to the provisions of the aforementioned law; and (iii) improving connectivity infrastructure and developing new tools and incentives for financial inclusion, with the aim of putting the law's provisions into practice, as well as improving access to and expanding the use of financial services in the country, and maximizing their impact in terms of benefits to the population (primarily, lower-income segments).

1.10 **Financing, productive investment, and growth.** Financing is a critical element in increasing investment, productivity, and economic growth. Greater access to long-term financing facilitates: (i) long-term investment, allowing projects to be developed in strategic sectors and productive infrastructure to be improved; (ii) the adoption of production technologies and techniques, as well as research, development, and innovation; (iii) access to markets and higher value-added segments in global value chains; and (iv) the mitigation of volatility and macroeconomic shocks to the economy.[21]

1.11 **Long-term financing and productive investment in Uruguay.** To improve productivity and consolidate growth, Uruguay needs to increase levels of private investment and improve the efficiency of public investment. Recent data show that growth in private investment has moderated since the 2010-2012 boom, with negative forecasts for the next few years.[22] The financing deficit in private sector productive investment is estimated at US$5.6 billion.[23] To bridge this gap, access to finance for Uruguayan companies needs to be increased. Data for the banking system show that credit to the private sector as a percentage of GDP was just 27% in 2014, compared to 70% in Brazil and 109% in Chile. Specifically, only 42% of small and medium-sized enterprises (SMEs) had a credit line, compared to 79% in Chile. This is significant given both the critical role of financing in improving economic productivity and the dominant role of SMEs in the Uruguayan economy.

1.12 With 40.5% of system assets, Banco de la República Oriental del Uruguay (BROU) is a significant participant in the banking system. Despite its mandate of providing medium and long-term credit to stimulate productive development, this function is currently limited by: (i) a weak organizational structure for risk management; and (ii) incomplete information regarding the payment capacity of

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[21] For an exhaustive analysis of the relationship between financial development and productivity, see the Support to SMEs and Financial Access/Supervision Sector Framework (IDB, 2014).

[22] World Economic Outlook, 2014.

[23] IFC Enterprise Finance Gap Database.

its debtors. These limitations reduce the BROU's ability to perform its public development bank role of promoting investment in economic sectors and market segments that are experiencing multiple market failures in the supply and demand for financing; these failures act as a disincentive to private sector activity. In Uruguay, these failures are especially acute in both the SME segment (owing to information asymmetries, the absence of collateral, fixed intermediation costs, etc.) and in infrastructure (given the strong presence of different types of externalities).[24] In addition to inefficiencies in banking intermediation, the capital market in Uruguay is almost nonexistent: stock exchange capitalization as a percentage of GDP is just 1.2%, well below the corresponding levels in Brazil (54%) and Chile (116%). This leaves the majority of firms and productive projects dependent on the banking system for financing.[25]

1.13 In terms of public investment, this depends to a large extent on the role of state-owned enterprises (SOEs), which play a dominant role in financing and carrying out the necessary infrastructure investments to provide basic public services for citizen welfare and private sector development.[26, 27] However, this role is limited by: (i) a decline in SOE operational efficiency[28] (with a drop in their contribution to the overall public sector balance from 4.6% of GDP in 2008 to 2.3% at end-2014);[29] and (ii) the lack of a system to coordinate, prioritize, and maximize

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24 For a review of the empirical evidence regarding the role of development banks, see, for example, Eslava, M., A. Maffioli, and M. Meléndez Arjona (2012). Second-tier Government Banks and Access to Credit: Micro-Evidence from Colombia, Technical Note 294, Washington D.C.; Inter-American Development Bank. Bonilla, C. and C. Cancino (2011). El Impacto del Programa de Capital Semilla del Sercotec en Chile [The Impact of the Sercotec Seed Capital Program in Chile] Working Paper 279, Capital Markets and Financial Institutions Division, Washington D.C.: IDB.

25 Banks account for 98% of total system assets.

26 There is abundant empirical evidence demonstrating the positive impact of infrastructure on growth (see, for example, Straub, 2008 on Asia; Erget et. al., 2009 on the OECD; and Calderón and Servén, 2010 on Latin America).

27 The "industrial entities" defined in Article 221 of the Constitution are the main providers of telecommunications services (National Telecommunications Administration [ANTEL], petroleum and derivatives (National Fuels, Alcohol, and Portland Cement Administration [ANCAP]), electricity (National Administration of Electric Power Generation and Distribution [UTE]), water and sanitation (State Sanitation Company [OSE]), and ports (National Port Administration [ANP]).

28 Measured as the fiscal balance of the SOEs excluding transfer and tax payments, and adjusted for exceptional factors such as variations in ANCAP oil inventories and the impact of the Energy Stabilization Fund on costs incurred by UTE. The deterioration in the firms' operating balance before interest, taxes, depreciation and amortization (EBITDA) has been even more marked, dropping from 7.0% of GDP to 4.3% (see Munyo and Regent, 2015).

29 According to the draft national budget for the 2015-2019 period, an improvement of US$440 million is deemed feasible in the SOEs' operating balance.

public investment efforts.[30] Given fiscal projections for the next few years, the public sector will need to increase its efficiency if it is to continue performing its role in the area of financing and public investment without compromising fiscal stability. Fiscal restrictions mean that a favorable environment needs to be created to encourage private sector participation in the financing of infrastructure investments, thus bridging the current gap[31] and ensuring that the conditions are in place for the Uruguayan economy to enter a stable path of sustained growth.

1.14 **Pending challenges.** Given this context, progress is needed in four critical areas: (i) strengthening the public banking sector, improving its efficiency and its role of providing long-term finance to stimulate productive development; (ii) strengthening the capital market as a mechanism for promoting long-term financing and incentives for productive investment; (iii) improving the efficiency of SOEs engaged in infrastructure investment and the delivery of key services for development and welfare; and (iv) strengthening the regulatory framework to provide incentives for private investment in the area of infrastructure.

1.15 **Bank experience and lessons learned.** The program is consistent with the Bank's work in the areas of: (i) financing for productive development, alongside the BROU (3396/OC-UR); (ii) implementation of Basel II regulatory standards, through strengthening of the SSF (2228/OC-UR); (iii) improvement of BROU institutional capacities (UR-T1132, currently awaiting approval); and (iv) improvement of public expenditure and investment management (1795/OC-UR, ATN/OC-10195-UR, ATN/OC-10067-UR, ATN/OC-14068-UR, RG-T2455, 3161/OC-UR, and 3398/OC-UR). The program also incorporates lessons learned by the Bank in designing policy-based loans, particularly the Programs for Strategic International Positioning I, II, and III (2920/OC-UR, 2922/OC-UR, 3365/OC-UR, and 3418/OC-UR). These relate to the importance of: (i) adequate sequencing of reforms; (ii) interest of the country's authorities in promoting a reform agenda, and ownership of those reforms; and (iii) support for the reforms through technical assistance actions. These lessons have been incorporated into program design.

1.16 **Rationale and program strategy.** Consistent with international diagnostic assessments and the Bank's experience in the country, the objective of the proposed program is to improve the financial system's contribution to economic

[30] The empirical literature underscores the importance of the project design, selection, implementation, and evaluation process for the final impact of investments (see Esfahani and Ramírez, 2003; Haque and Kneller, 2008). For example, Gupta et al. (2014) showed that the investment selection process in emerging countries is particularly important for determining investment productivity, and that weaknesses in that process can lead to "waste" of around 40% in public investment. Flyvbjerg (2003) finds that significant cost overruns, lower-than-expected benefits, and low efficiency are common in developing countries, and can be attributed to weaknesses in investment selection and monitoring processes. Rajaram et al. (2014) highlight the need for rigorous project design and selection processes in ensuring that projects are based on credible estimates of costs and benefits. In recent years, the Uruguayan government has laid the groundwork for implementation of the National Public Investment System (SNIP), including approval of a law creating the SNIP. Nonetheless, public investment projects in the 2010-2015 budget were not evaluated through the SNIP. The IMF (2015), using a data envelopment analysis methodology, finds that there is significant room to improve investment expenditure efficiency in the region. It estimates conservatively that effective implementation of the SNIP could reduce "waste" by 10%, yielding benefits of US$30 million.

[31] The infrastructure deficit stands at approximately US$36 billion.

growth in Uruguay, supporting the design and implementation of regulatory reforms to address pending challenges in the areas of: (i) financial stability; (ii) greater inclusion of the most disadvantaged population groups and enterprises; and (iii) a greater supply of long-term financing for the promotion of productive development. The ultimate objective is to ensure that the conditions are in place for the Uruguayan economy to enter a stable path of sustained growth. This, in turn, will allow a deepening and consolidation of the social gains that have been achieved. To support the Uruguayan government on a gradual and sustainable reform path, the program will encompass two consecutive operations, as discussed below.

1.17 **Strategic alignment.** The program is consistent with the following priority areas of the IDB Country Strategy with Uruguay, 2016-2020 (document GN-2836): (i) productivity and competitiveness, through greater efficiency in the financial system; and (ii) public sector management, through greater efficiency in public institutions. Likewise, it is consistent with the priority objective of expanding the availability and variety of financial services established under the IDB Country Strategy with Uruguay (2010-2015) (document GN-2626). Within the framework of the Ninth General Increase in the Resources of the Inter-American Development Bank (document AB-2764), the program, by proposing reforms and policy measures in the financial inclusion subsector, will contribute to: (i) the financing priorities of support to small and vulnerable countries; and (ii) lending to reduce poverty and enhance equity. Specifically, it will support institutions and regulations that promote access to financial services. It will also contribute to the regional target for institutions for growth and social welfare: specifically, to the percentage of firms using banks to finance investments, as set out in the Results Framework. In terms of the development of institutional and regulatory reforms to promote access to financing, the operation is aligned with the Support to SMEs and Financial Access/Supervision Sector Framework (document GN-2768-3). Lastly, the program is also aligned with the Sector Strategy Institutions for Growth and Social Welfare (document GN-2587-2), in that it proposes reforms to strengthen financial institutions in Uruguay.

1.18 **Coordination with other donors.** This operation is coordinated with IMF recommendations in the areas of financial system stability and improved capital market performance, and it complements actions by the World Bank and the Development Bank of Latin America (CAF) aimed at promoting long-term financing by fostering public-private partnerships and strengthening their institutional framework.

B. Objective, components, and cost

1.19 **Objective.** The objective of the program is to improve the financial system's contribution to economic growth in Uruguay by: (i) improving financial regulation and supervision; (ii) developing regulations and instruments to foster the financial inclusion of households and companies; and (iii) strengthening institutions and regulations aimed at providing long-term finance.

1.20 **Beneficiaries.** Program reforms are crosscutting in nature, and are aimed at overcoming financial and regulatory hurdles that hinder satisfactory operation of the financial system and the sector's contribution to growth. Given this objective, and the broad nature of the reforms, the program is expected to benefit all stakeholders in the economy. The financial inclusion component places particular emphasis on the population at the base of the pyramid, with the aim of reducing its vulnerability. The component to provide financing for productive development emphasizes SMEs by strengthening the actions of the public banks.

1.21 The program consists of four components:[32]

1.22 **Component I. Macroeconomic stability.** The objective of this component is to ensure a macroeconomic context that is consistent with program objectives and the parameters of the Policy Letter, as set out in the Policy Matrix (Annex II).

1.23 **Component II. Strengthening financial regulation and supervision.** This component seeks to strengthen the areas for further work identified in international diagnostic assessments:

a. **Institutional strengthening of regulatory bodies.** The objective of this subcomponent is to reinforce the stability of the Uruguayan financial system by strengthening its regulatory bodies. To this end, the first operation plans to improve the supervisory capacity of the Financial Services Superintendency (SSF) by improving information exchange with the Banking Savings Protection Corporation (COPAB). In the second operation, improvements in the SSF's technical and economic independence are envisaged, consistent with international best practices.

b. **Developing financial regulation.** The purpose of this subcomponent is to adapt the country's financial regulation to Basel II and III standards. To this end, the first operation includes: (i) adaptation of the regulatory framework to Basel III by incorporating measurement of the liquidity coverage ratio; (ii) a proposal to regulate risk ratings and ceilings on deposits with nonresident financial institutions for terms of less than 90 days; and (iii) consolidation of Basel II standards by regulating financial institutions' self-assessments of capital adequacy and by creating a manual for the capital self-assessment process. The second operation includes: (i) implementation of Basel III standards relating to measurement of the net stable funding ratio (NSFR) and capital requirements; (ii) improved regulation of bank resolution mechanisms, in accordance with the principles of transparency and efficiency; and (iii) development and implementation of financial intelligence activities, particularly intra-sector risk matrices and strategic operations analysis.

c. **Improving financial transparency.** The first operation includes the following measures aimed at improving financial system transparency: (i) launching implementation of the International Financial Reporting Standards (IFRS); (ii) harmonizing the criteria for hiring auditors across all financial entities, strengthening of the sanctions regime, issuing regulations to require BCU authorization of independent professionals working as auditors, and issuing reports on the prevention of money laundering and the financing of terrorism; and (iii) harmonizing regulations governing financial transparency and market conduct in the banking sector and the capital, insurance, and pension fund

[32] Some of the measures supported under the program have been implemented over the last year, and are a result of the ongoing dialogue between the Bank and the Uruguayan government. They are critical for development of the Bank-supported agenda to strengthen financial regulation and participating institutions.

markets, with a view to avoiding regulatory arbitrage. The second operation includes: (i) the entry into force of regulations mandating the use of the IFRS by financial institutions; (ii) entry into force of the National Secretariat to Combat Money Laundering and the Financing of Terrorism, as a deconcentrated body attached directly to the Office of the President; and (iii) evaluation of Uruguay's national strategy to combat money laundering and the financing of terrorism.

d. **Improving regulation of pension funds and the insurance sector.** With a view to supporting financial system stability, this subcomponent includes a proposal for reform of the corporate governance framework and the risk management system for insurance companies and the Pension Fund Administrators (AFAP), to establish proper control and greater transparency of their conduct. The second operation includes: (i) entry into force of minimum management standards for the AFAP and insurance companies, in order to improve market discipline; and (ii) approval of the Insurance Law by Uruguay's Parliament.

1.24 **Component III. Financial regulation for inclusive development.** This component introduces reforms in three important areas:

a. **Definition of a regulatory framework for financial inclusion as a mechanism for social development and inclusion.** To provide the country with a regulatory framework for financial inclusion, the first operation envisages the approval of a financial inclusion law that fosters access to and use of financial services by the entire population, as well as reform and modernization of the payments system. The second operation includes an evaluation of the performance of the Financial Inclusion Law, its impact on the use of financial services by the most vulnerable social groups, and proposals for its improvement.

b. **Regulatory development of measures to promote universal access to and use of basic financial services.** The first operation includes the issuance of regulations governing: (i) the payment of salaries, social benefits, pensions, and professional services through financial institutions or electronic money issuers; (ii) the Programa de Ahorro Joven para Vivienda [Young People's Housing Savings Program]; and (iii) the supervision of electronic money institutions with respect to the movement and source of funds. The second operation includes: (i) regulatory development of the Financial Inclusion Law to encourage substitution of electronic money for cash, through: (a) electronic transactions for buying and selling real estate and vehicles, and (b) the development of regulations governing the payment of taxes using electronic means; and (ii) development of a plan to raise public awareness of the programs and actions included in regulation of the Financial Inclusion Law.

c. **Development of new instruments and incentives to promote efficiency in the payments system.** To support financial inclusion, the first operation includes regulation of: (i) interoperability of terminal networks for processing electronic payments; (ii) VAT reimbursements on electronic purchases; (iii) fiscal benefits granted for the expansion of point-of-sale terminal networks; and (iv) the payment of leases and State suppliers via credits to accounts in financial intermediation institutions. The second operation includes regulation of interoperability in devices enabling cash withdrawals (e.g. automatic teller machines), and preparation of a report on progress in implementing regulations governing: (i) VAT reimbursements on electronic purchases; (ii) fiscal benefits granted for the expansion of point-of-sale terminal networks; and (iii) the payment of State leases and suppliers via credits to accounts in financial intermediaries.

1.25 **Component IV. Strengthening financial institutions and regulations for productive development.** This component seeks to increase private investment levels and improve the efficiency of public investment by:

a. **Regulating the capital market to enhance its role as an instrument of long-term financing.** To support development of the capital market in Uruguay, the first operation includes: (i) establishment of prudential regulation for securities dealers, regulating their capital levels and necessary information requirements; (ii) a proposal for defining both the size of non-public offerings (in terms of the amounts and number of investors) and the minority stake in public offerings; (iii) regulation of information standards for capital market investors; and (iv) a proposal for harmonizing regulations governing the reporting of transactions by financial intermediaries and securities dealers. The second operation includes development of a master plan for the capital market that assesses the status of the local market and establishes a roadmap for both harmonizing its regulation with international standards and strengthening operation of the local public and corporate debt markets.

b. **Strengthening public banks to improve their efficiency and development financing objectives.** The first operation includes the issuance of regulations governing: (i) the design and promotion of a structural reorganization of the BROU, with emphasis on improvements in efficiency and commercial intelligence and changes to information and risk-management systems; and (ii) adaptation of the information required to evaluate the payment capacity of recipients of payroll loans and loans from the BROU's social credit division. The second operation includes implementation of the BROU reorganization strategy, comprising efficiency improvements in the commercial office network; implementation of a new product/channel matrix; a development plan for information and risk-management systems; commercial intelligence mechanisms; and analysis of the management of corporate holdings.

c. **Fostering the development of public-private partnerships.** With the objective of increasing long-term financing for productive investment, the first operation includes: (i) defining national objectives in the area of public-private partnerships (PPPs); and (ii) strengthening the operations of the PPP project unit by: (a) clarifying the design and approval process for PPP projects and the roles of the different participants therein; (b) establishing time frames for the procedure; and (c) including a role for the Ministry of Economy and Finance (MEF) and the PPP unit in awarding contracts. The second operation includes: (i) approval and registration of at least two PPP contracts; and

(ii) regulation of the process for formalizing the private sector's role in designing and implementing PPPs.

d. **Strengthening the efficiency of State-owned enterprises.** To improve the efficiency of SOE investment and management, the first operation envisages the introduction of a requirement for the following SOEs to establish management agreements with the Executive Branch (including a section relating to operational efficiency improvements in their 2016 budgets): the National Administration of Electric Power Generation and Distribution (UTE); the National Fuels, Alcohol, and Portland Cement Administration (ANCAP); the National Telecommunications Administration (ANTEL); the State Sanitation Company (OSE); and the National Port Administration (ANP). The second operation includes: (i) an Executive Branch decree confirming the management agreements signed between the MEF, the Budget and Planning Office (OPP), each SOE (UTE, ANCAP, ANTEL, OSE, and ANP), and the responsible ministries; and (ii) a strategy for strengthening monitoring and evaluation of all SOEs.

e. **Effective implementation of the National Public Investment System for the 2015-2019 budget.** The first operation includes the following measures aimed at improving public investment efficiency: (i) approval of a decree to regulate SNIP operations, specifying the general procedure for registering and obtaining a technical opinion on projects; (ii) an OPP resolution that includes: (a) SNIP technical rules, (b) a manual for investment evaluation and formulation, and (c) social prices and technical guidelines for socioeconomic evaluation; and (iii) a requirement in the budgets of the following SOEs that their 2015-2016 investment projects be evaluated through the SNIP: UTE, ANCAP, ANTEL, OSE, and ANP. The second operation includes: (i) registration in the SNIP of all central government investment projects included in the 2015-2019 budget; (ii) certification that all investment projects included in the 2016 budgets of ANCAP, UTE, ANTEL, OSE and ANP have been registered in the SNIP; and (iii) a study of efficiency in the public investment management process.

C. Key results indicators

1.26 The key indicator for measuring program impact will be GDP growth, which is expected to exceed GDP growth under a non-reform scenario by 0.05 percentage points. Program outcomes will be measured as follows: (i) the z-score as a measure of financial stability; (ii) the percentage of adults with an account in a financial institution; (iii) the number of new issues listed on the stock exchange; (iv) the interest rate differential; (v) the BROU's efficiency ratio; and (vi) the operating balance of the SOEs as a percentage of GDP. See the Results Matrix.

D. Economic analysis

1.27 The economic analysis estimates the impact of the supported reforms on the medium-term growth rate and on quasi-fiscal savings. Calculations for Components II and III are based on a general equilibrium model of financial development proposed by Dabla-Norris et al. (2014).[33] Sensitivity tests of the baseline results were conducted for a broad range of parameters. A discount rate of 12% was applied to the resulting real net benefit flows, consistent with Bank recommendations. In the case of Component IV, cost savings stemming from greater efficiency and improved planning were included as benefits. Use of a general equilibrium model is proposed for the evaluation of program impact as there is a calibration for Uruguay that confirms the viability of this approach; the availability of the data needed to recalibrate the model using 2019-2020 values has also been confirmed with the World Bank. In the case of Component IV, ex post recalculation of the economic analysis is proposed (see the Program Economic Analysis for further details).

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instrument

2.1 The current operation is the first of two consecutive operations that are linked on a technical level, but financed separately as programmatic policy-based loan (PBL) operations with a deferred drawdown option. The first operation is for a maximum amount of US$250 million, which is consistent with the country's external financing needs (US$2.595 billion in 2015). This operation would cover 9.63% of these needs. The amount of the second operation will be decided in the corresponding programming exercise based on the country's financing needs. In accordance with "Policy-based Loans: Guidelines for Preparation and Implementation" (document CS-3633-1), a programmatic approach facilitates policy dialogue between the country and the Bank, accords sufficient time for reforms to be implemented, and provides an opportunity for progress under the first operation to be evaluated and reforms adjusted based on the knowledge acquired. The second operation is expected to deepen the reforms initiated under the first.

B. Environmental and social risks

2.2 In accordance with Directive B.13 of the Environment and Safeguards Compliance Policy (document GN-2208-20 and Operational Policy OP-703), no classification is required. The proposed reforms will not have any negative environmental or social impacts.

C. Sustainability and other risks

2.3 Macroeconomic and fiscal sustainability risk is considered to be medium. To mitigate it, the project team will monitor the macroeconomic environment on a periodic basis. To ensure fiscal sustainability of the proposed reforms under the program, these have been designed to yield benefits and avoid an undue burden on the fiscal accounts. Fiscal sustainability of the reforms has been analyzed in the Program Economic Analysis. Program targets are aligned with the objectives of the draft 2015-2019 budget.

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[33] Dabla-Norris, E., Y. Ji, R. Townsend, and F. Unsal, 2014, Financial Deepening, Growth, and Inequality: A Structural Framework for Developing Countries.

III. Implementation and Management Plan

A. Summary of implementation arrangements

3.1 The executing agency will be the MEF, which will designate a program coordination unit (PCU) responsible for coordinating the agencies involved in execution, as well as presenting work plans and semiannual progress reports on compliance with the Policy Matrix (Annex II). The PCU will be the MEF's Coordination Unit for International Agencies, in coordination with the relevant authorities at the BCU, BROU, and OPP. The PCU, together with these agencies, will carry out periodic monitoring of the reforms envisaged in the Policy Matrix, with a view to preparing a semiannual report on progress towards the fulfillment of program conditions and submission of this report to the Bank.

3.2 **Special contractual conditions precedent to the single loan disbursement. Disbursement of loan proceeds is subject to fulfillment, to the Bank's satisfaction, of the policy reform measures described in the program components and envisioned in the Policy Matrix (Annex II), in addition to the other conditions established in the loan contract.**

B. Summary of arrangements for monitoring results

3.3 Program implementation will be monitored by the MEF's Coordination Unit for International Agencies, which will submit information periodically and monitor the means of verification for program reforms. The borrower and the Bank will hold semiannual meetings to review compliance with the conditions required for the second program. As executing agency, the MEF will designate a staff member whose responsibilities will include: (i) maintaining official communication with the Bank and submitting reports and evidence of compliance with conditions under the operation (as well as any other report that the Bank may require) in accordance with the agreed time frames and conditions; (ii) advancing actions to achieve the policy objectives set out in the program (particularly those included as triggers for the second operation); and (iii) collecting, archiving, and submitting to the Bank all information, indicators, and parameters that will allow the Bank to monitor, measure, and evaluate program results. Consistent with its role, the MEF will coordinate the receipt of evidence regarding commitments made by the different government institutions. With respect to the final program evaluation, the Bank will prepare a project completion report, followed by an evaluation with two components. The first component relies on a general equilibrium model to estimate the impact of the policies on economic growth following implementation of the reforms. In the case of the second component, the same exercise described in the economic analysis will be conducted, but using effective values and defining a heuristic counterfactual (see the Monitoring and Evaluation Plan and the Program Economic Analysis).

IV. Policy Letter

4.1 The Policy Matrix for the proposed program is aligned with the corresponding Policy Letter issued by the Eastern Republic of Uruguay. The letter reaffirms the government's commitment to implementing the activities agreed with the Bank.

Development Effectiveness Matrix

Summary

I. Strategic Alignment			
1. IDB Strategic Development Objectives	Aligned		
Lending Program	-Lending to small and vulnerable countries -Lending for poverty reduction and equity enhancement		
Regional Development Goals	-Percent of firms using Banks to finance investments		
Bank Output Contribution (as defined in Results Framework of IDB-9)			
2. Country Strategy Development Objectives	Aligned		
Country Strategy Results Matrix	GN-2836	Increase medium and long-term financing. Strenghten public management systems.	
Country Program Results Matrix		The intervention is not included in the 2015 Operational Program.	
Relevance of this project to country development challenges (If not aligned to country strategy or country program)			
II. Development Outcomes - Evaluability	Evaluable	Weight	Maximum Score
	8.1		10
3. Evidence-based Assessment & Solution	9.6	33.33%	10
3.1 Program Diagnosis	3.0		
3.2 Proposed Interventions or Solutions	3.6		
3.3 Results Matrix Quality	3.0		
4. Ex ante Economic Analysis	7.0	33.33%	10
4.1 The program has an ERR/NPV, a Cost-Effectiveness Analysis or a General Economic Analysis	2.5		
4.2 Identified and Quantified Benefits	2.0		
4.3 Identified and Quantified Costs	2.0		
4.4 Reasonable Assumptions	0.0		
4.5 Sensitivity Analysis	0.5		
5. Monitoring and Evaluation	7.7	33.33%	10
5.1 Monitoring Mechanisms	1.5		
5.2 Evaluation Plan	6.2		
III. Risks & Mitigation Monitoring Matrix			
Overall risks rate = magnitude of risks*likelihood	Low		
Identified risks have been rated for magnitude and likelihood	Yes		
Mitigation measures have been identified for major risks	Yes		
Mitigation measures have indicators for tracking their implementation	Yes		
Environmental & social risk classification	B.13		
IV. IDB´s Role - Additionality			
The project relies on the use of country systems			
Fiduciary (VPC/FMP Criteria)	Yes	Financial Management: Budget, Treasury, Accounting and Reporting, External control, Internal Audit.	
Non-Fiduciary			
The IDB's involvement promotes additional improvements of the intended beneficiaries and/or public sector entity in the following dimensions:			
Gender Equality			
Labor			
Environment			
Additional (to project preparation) technical assistance was provided to the public sector entity prior to approval to increase the likelihood of success of the project	Yes	The Bank has allocated several technical cooperation activities to support the project: i) UR-T1132 is aimed at supporting the institutional reorganization of the BROU by generating a detailed analysis of the organization's structure and proposing a strategic plan that allows it to provide better services to SMEs, carry-out processes reengineering, and reducing costs; ii) ATN/OC-10195-UR and ATN/OC-14068-UR support the implementation of a results based framework in the public sector of the country; and iii) ATN/OC 10067-UR supports the design of the Public Investments National System.	
The ex-post impact evaluation of the project will produce evidence to close knowledge gaps in the sector that were identified in the project document and/or in the evaluation plan			

The Support Program for the Reform of the Financial System of Uruguay is the first of two programmatic loans supporting policy reforms. The objective of this program is to improve the contribution of the financial system to the economic growth of Uruguay, through (i) improvements in the regulation and supervision of the financial system; (ii) development of the regulation and instruments of financial inclusion of the unbanked citizens and SMEs and (iii) improvements in the institutions and regulations oriented to provide long term financing.

The vertical logic is consistent. The challenges to be resolved are diagnosed: bank supervision and regulation in need of strengthening amidst an environment of probable increased external risks; limited liquidity of the capital markets; low participation of citizens in the formal systems of savings and credit; and opportunities of efficiency improvements in public investments. The proposed activities and outputs (laws, regulations, stronger institutions, etc.) are aligned and aim at setting the normative and institutional basis to reduce the participation costs of firms and citizens, reducing the barriers to financing economic activity. The indicators of the results matrix would allow to follow products and to measure the results of the reform through the proposed evaluation.

Both the economic analysis and the evaluation plan rest on a micro-founded general equilibrium model developed by the International Monetary Fund (IMF) to measure the effect of this type of program (it is important to mention that this model was also recently used in the design of a similar programmatic line in Colombia CO-L1144). The model allows simulating the evolution of relevant variables of interest (like economic growth) affected by changes in the parameters of interest (for example, cost of participation, efficiency of financial intermediation, etc.). The advantage of access to the model is twofold: first, the necessary information for the estimations exists and is updated frequently enough to follow the program according to the monitoring and evaluation plan; second, there is a group of IMF officials who can provide support and suggestions for the calibrations and simulations. The disadvantage is that, for now, the quantitative exercises are performed by those officials, which limits the possibility to learn with higher accuracy the dynamics and orders of magnitude of the effects of the interactions of the variables in the model.

POLICY MATRIX

Policy objectives	Agreed policy measures Program I	Agreed policy measures Program II
Component I: Macroeconomic stability		
The objective of this component is to ensure a macroeconomic context that is consistent with program objectives and the parameters of the Policy Letter.	The macroeconomic context is consistent with program objectives and the parameters of the Policy Letter.	The macroeconomic context is consistent with program objectives and the parameters of the Policy Letter.
Component II: Strengthening financial regulation and supervision		
Institutional strengthening of regulatory bodies	Improve SSF supervisory capacity by improving information exchange with COPAB (deposit insurance).	Improve SSF technical and economic independence consistent with international best practices.
Developing financial regulation	Adaptation of the regulatory framework to Basel III by incorporating measurement of the liquidity coverage ratio. Proposal to regulate risk ratings and ceilings on deposits with nonresident financial institutions for terms of less than 90 days. Consolidation of Basel II standards by regulating financial institutions' self-assessments of capital sufficiency and by creating a manual for the capital self-assessment process.	Implementation of Basel III standards relating to: – Measurement of the net stable funding ratio (NSFR); and – Capital requirements. Improved regulation of bank resolution mechanisms, in accordance with the principles of transparency and efficiency. Development and implementation of financial intelligence activities, particularly intra-sector risk matrices and strategic operations analysis.
Improving financial transparency	Launch implementation of the International Financial Reporting Standards (IFRS) by opening the regulations governing introduction of the IFRS in financial institutions to public consultation. Harmonize the criteria for hiring auditors across all financial institutions, strengthen sanctions, and issue regulations to require BCU authorization of independent professionals working as auditors and issuing reports on the prevention of money laundering and the financing of terrorism. Harmonize regulations governing financial transparency and market conduct in the banking sector and the capital, insurance, and pension fund markets, to avoid regulatory arbitrage.	Entry into force of regulations mandating the use of the IFRS by financial institutions. Entry into force of the National Secretariat to Combat Money Laundering and the Financing of Terrorism, as a deconcentrated body attached directly to the Office of the President. Evaluation of the national strategy to combat money laundering and the financing of terrorism.

Policy objectives	Agreed policy measures Program I	Agreed policy measures Program II
Improving regulation of pension funds and the insurance sector	Proposal for reform of the corporate governance framework and the risk management system for insurance companies and pension fund administrators (AFAPs), to establish proper controls and greater transparency of their conduct.	Entry into force of minimum management standards for ASAPs and insurance companies, in order to improve market discipline. Approval of the Insurance Law by Uruguay's Assembly.
Component III: Financial regulation for inclusive development		
Definition of a regulatory framework for financial inclusion as a mechanism for social development and inclusion	Approval of a financial inclusion law that fosters access to and use of financial services by the entire population, as well as reform and modernization of the payments system.	Evaluation of the performance of the financial inclusion law, its impact on the use of financial services by the most vulnerable social groups, and proposals for its improvement.
Regulatory development of measures to promote universal access to and use of basic financial services	Issue regulations governing the payment of salaries, social benefits, pensions, and professional services through financial institutions or electronic money issuers. Issue regulations governing the Programa de Ahorro Joven para Vivienda [Young People's Housing Savings Program]. Issue regulations governing the supervision of electronic money institutions with respect to the movement and source of funds.	Regulatory development of the financial inclusion law to encourage substitution of electronic money for cash, through: – Electronic transactions for buying and selling real estate and vehicles; and – Development of regulations governing the payment of taxes using electronic means. Development of a plan to raise public awareness of the programs and actions included in regulation of the financial inclusion law.
Development of new instruments to promote efficiency in the payments system	Issue regulations governing interoperability of terminal networks for processing electronic payments. Issue regulations governing VAT reimbursements on electronic purchases. Issue regulations governing fiscal benefits granted for the expansion of point-of-sale terminal networks. Issue regulations governing the payment of leases and State suppliers via credits to accounts in financial intermediation institutions.	Issue regulations governing interoperability in devices enabling cash withdrawals (e.g. automatic teller machines). Preparation of a report on progress in implementing regulations governing: (i) VAT reimbursements on electronic purchases; (ii) fiscal benefits granted for the expansion of point-of-sale terminal networks; and (iii) the payment of State leases and suppliers via credits to accounts in financial intermediaries.

Policy objectives	Agreed policy measures Program I	Agreed policy measures Program II
Component IV. Strengthening financial institutions and regulation for productive development		
Regulating the capital market to enhance its role as an instrument of long-term financing	Establish prudential regulation for securities dealers, regulating their capital levels and necessary information requirements. Proposal for defining both the size of non-public offerings (in terms of the amounts and number of investors) and the minority stake in public offerings. Issue regulations governing information standards for capital market investors. Proposal for harmonizing regulations governing the reporting of transactions by financial intermediaries and securities dealers.	Development of a master plan for the capital market that assesses the status of the local market and establishes a roadmap for both harmonizing its regulation with international standards and strengthening operation of the local public and corporate debt markets.
Strengthening public banks to improve their efficiency and development financing objectives	Design and promote a structural reorganization of the BROU, with emphasis on improvements in efficiency and commercial intelligence and changes to information and risk-management systems. Adapt the information required to evaluate the payment capacity of recipients of payroll loans and loans from the BROU's social credit division.	Implementation of the BROU reorganization strategy, comprising: – Efficiency improvements in the commercial office network; – Implementation of a new product/channel matrix; – Development plan for information and risk-management systems; – Commercial intelligence mechanisms; and – Analysis of the management of corporate holdings.
Fostering the development of public-private partnerships	Define national objectives in the area of public-private partnerships (PPPs). Strengthen the operations of the PPP project unit by: – Clarifying the design and approval process for PPP projects and the roles of the different participants therein; – Establishing time frames for the procedure; and – Including a role for the Ministry of Economy and Finance (MEF) and the PPP unit in awarding contracts.	Approval and registration of at least two PPP contracts. Issue regulations governing the process for formalizing the private sector's role in designing and implementing PPPs.

Policy objectives	Agreed policy measures Program I	Agreed policy measures Program II
Strengthening the efficiency of SOEs	Introduce a requirement for the following SOEs to establish management agreements with the Executive Branch (including a section relating to operational efficiency improvements in their 2016 budgets): UTE, ANCAP, ANTEL, OSE, and ANP.	Executive Branch decree confirming the management agreements signed between the MEF, the Budget and Planning Office (OPP), each SOE (UTE, ANCAP, ANTEL, OSE, and ANP), and the responsible ministries. Strategy for strengthening monitoring and evaluation of all SOEs.
Effective implementation of the National Public Investment System for the 2015-2019 budget	Approval of a decree to regulate SNIP operations, specifying the general procedure for registering and obtaining a technical opinion on projects. An OPP resolution that includes: (i) SNIP technical rules; (ii) a manual for investment evaluation and formulation; and (iii) social prices and technical guidelines for socioeconomic evaluation. Establish a requirement in the budgets of the following SOEs that their 2015-2016 investment projects be evaluated through the SNIP: UTE, ANCAP, ANTEL, OSE, and ANP.	Registration in the SNIP of all central government investment projects included in the 2015-2019 budget. Certification that all investment projects included in the 2016 budgets of ANCAP, UTE, ANTEL, OSE and ANP have been registered in the SNIP. Study of efficiency in the public investment management process.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-___/__

Uruguay. Loan ____/OC-UR to the Eastern Republic of Uruguay
Financial System Reform Support Program

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Eastern Republic of Uruguay, as Borrower, for the purpose of granting it a financing to cooperate in the execution of the Financial System Reform Support Program. Such financing will be for an amount of up to US$250,000,000 from the Ordinary Capital resources of the Bank, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on ___ __________ 20__)

LEG/SGO/CSC/IDBDOCS: 39954147
Pipeline No.:UR-L1108