TC ABSTRACT

I. BASIC PROJECT DATA

Region:	Latin America and the Caribbean Countries (Regional)
TC Name:	Strengthening the performance of State Owned Enterprises
TC Number:	RG-T2486
Team members:	Emilio Pineda (FMM/CUR) Team Leader; Gerardo Reyes-Tagle (IFD/FMM); Jorge Kaufmann (IFD/ICS); Jorge von Horoch (IFD/ICS); Huyngon Kim (IFD/FMM); and Marina Massini (IFD/FMM).
Operation type	Research and Dissemination
Date of TC Abstract:	July 2014
Beneficiary:	Latin America and the Caribbean countries
Executing agency:	Bank Executed
IDB (KPR):	US$150,000
Disbursement period:	Disbursement period: 12 months Execution period: 12 months
Types of consultants;	Individual
Prepared by Unit:	IFD/FMM
TC included in CS or CPD	No [X] **GCI-9 priority:** Yes [X]

II. OBJECTIVE AND JUSTIFICATION

2.1 State-Owned Enterprises (SOEs)[1] have an enormous economic and social impact in Latin America and the Caribbean (LAC). Governments in LAC are controlling shareholders and minority investors in a large number and wide variety of corporations.[2] A survey done by the OECD (2012) shows that five of the seven countries reported have more than 100 SOEs (Argentina, Brazil, Colombia, Mexico and Peru), while even those countries with the fewest SOEs–Chile and Ecuador- were in the dozens.

2.2 The assets of SOEs represent on average 12% of GDP in the Region while playing a fundamental role in production, pricing, and exporting of non-renewable natural resources (oil, gas and minerals) and in the provision of public services (electricity, gas, water and sanitation).[3] Furthermore, these corporations absorb significant fiscal resources and in some cases have important contingent liabilities that can pose threats to the fiscal sustainability in various LAC countries.[4]

2.3 The main justification for SOEs is as a way to solve market failures or address distributional concerns, where for example the government helps firms develop new

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1 Defined as those enterprises where the government is the controlling shareholder.

2 See OECD (2012), "Ownership Oversight and Board Practices for Latin American State-Owned Enterprises".

3 *Ibidem.*

4 See, IDB (2012), "State-Owned Enterprises (SOEs) in Latin America and the Caribbean (LAC): Overview and Fiscal Risks".

capabilities, reduce their capital constraints, or deliver subsidized electricity.[5] However, there is a theoretical and empirical literature showing that on average, SOEs are less efficient than their private counterparts and that they are not the best vehicle to achieve distributional goals. This underperformance is generally attributed to: (i) SOEs having social objectives that sometimes conflict with profitability; (ii) SOEs managers lack incentives and monitoring; (iii) weak management capabilities; and (iv) SOEs do not have an incentive to perform efficiently because they know their governments will bail them out.[6] As a result, SOEs' contribution to the development of LAC, through an efficient and fiscally sustainable provision of public services is undermined.

2.4 The Ministry of Strategy and Finance of Korea (MOSF) and the Inter-American Development Bank (IDB) co-hosted three international forums to discuss policies and reforms regarding State-Owned Enterprises (SOEs) management. As a result, the IDB and the MOSF reached an agreement to establish a framework for continuous cooperation between Latin American countries and Korea in order to enhance the performance of SOEs.

2.5 In the context of this framework of continuous cooperation, the objective of this Technical Cooperation (TC) is to have a better understanding on how SOEs in LAC can overcome some of the problems highlighted by the literature, including those that pose threats to fiscal sustainability and help solve the market failures that thwart development, by generating original research drawing on recent regional experiences, and facilitating knowledge exchange. In doing so, the TC will focus on:

a. Fiscal and Financial Discipline. One of the key aspects for the SOEs to perform efficiently is to assure that they operate in a financially sustainable way. Attention will be placed in the trade-off between hidden subsidies and service quality as well as debt management.

b. Corporate Governance, oversight and management capabilities of SOEs. Effective Corporate Governance with innovative oversight structures, such as Public Holding companies, has been used in the region and internationally to address the problems mentioned. Furthermore, only around 7% of SOEs in the region are subject to the surveillance of stock and financial markets.

2.6 The TC will benefit from the Korean ample experience in SOE reform and strengthening, particularly in those issues related to debt-management, corporate governance, and management systems and evaluation, among others.

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[5] For a review of this literature see Musacchio and Lazzarini (2014), *Leviathan Evolving: New Varieties of State Capitalism in Brazil and Beyond*, Harvard University Press.

[6] *Ibid.*

III. DESCRIPTION OF ACTIVITIES AND OUTPUTS

3.1 The TC will finance: (i) one seminar in the LAC Region that will focus in international lessons learned on SOE reform; and (ii) one issue paper to outline the policy reform agenda in the Region.

3.2 The seminar will be conducted with the participation of government and SOEs officials from LAC countries and Korea, as well as some IDB staff. The paper will be prepared with the contribution of experts in the area, including Bank's staff.

IV. BUDGET

Description and type of the procurement contract	Source of financing	
	IDB (KPR)	**Total**
Consulting services 1: One seminar to be conducted in Latin America	120,000	120,000
Consulting services: Policy Reform Issues Paper	30,000	30,000
TOTAL	**150,000**	**150,000**

V. EXECUTING AGENCY AND EXECUTION STRUCTURE

5.1 The Bank will be responsible for the contracting of consultancies and will carry out the selection and hiring of the consulting services in accordance with Bank procedures established in document GN-2350-7.5. Technical and disbursement responsibility at the Bank will be under Emilio Pineda (FMM/CUR).

VI. PROJECT RISKS AND ISSUES

6.1 One possible risk would be the lack of interest on the SOE topics from the participating governments. To mitigate this risk, the Bank is targeting countries that have very relevant SOEs and it is inserting itself into the regional networks that have discussed these issues over the last years.

VII. ENVIRONMENTAL AND SOCIAL CLASSIFICATION

7.1 According to the environmental policy and the safeguards this TC is under Directive B.13. Given its objective, this TC will not carry negative environmental nor social impacts, and that it is why it is not considered necessary to prepare an Environmental and Social Strategy.