Office of Evaluation and Oversight

Country Program Evaluation

Paraguay

2014-2018

IDB | IDB Invest

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Preface

This evaluation of the country program with Paraguay for the period 2014-2018 has been prepared as part of the work program of the Inter-American Development Bank's Office of Evaluation and Oversight (OVE) for 2018 as an input for preparation of the IDB Group's future country strategy. Country program evaluations (CPEs) seek to "provide information on Bank performance at the country level that is credible and useful, and that enables the incorporation of lessons and recommendations that can be used to improve the development effectiveness of the Bank's overall strategy and program." In addition to sovereign guaranteed projects, CPEs also cover the non-sovereign guaranteed operations carried out by IDB Invest. Accordingly, these evaluations provide an opportunity for independent evaluation of the full scope of the IDB Group's work.

This is OVE's fourth independent evaluation of the Bank's program with Paraguay. OVE's first evaluation (document RE-294, June 2004) covered the 1991-2002 period, which was marked by democratic transition and the prolonged economic and financial crisis experienced by the country from 1995 to 2002. The second evaluation (document RE-356, August 2009) covered the 2003-2008 period, which was characterized by major reforms that helped Paraguay emerge from the crisis and embark on a period of sustained economic growth, based on strong fiscal discipline and a buoyant external sector. The most recent evaluation (document RE-452, February 2014) covered the 2009-2013 period, which saw an intensification of the agricultural export model and the materialization of new opportunities, challenges, and vulnerabilities for the country's economy. Paraguay is currently transitioning toward a more developed economy, and this offers a valuable opportunity for the Bank to reevaluate its relationship with the country and its role going forward.

Acknowledgements

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Acronyms and Abbreviations

AFD	*Agencia Financiera de Desarrollo* [Financial Development Agency]
ANDE	*Administración Nacional de Electricidad* [National Electricity Administration]
CAF	*Corporación Andina de Fomento* [Development Bank of Latin America]
CPE	Country Program Evaluation
DAPSAN	*Dirección de Agua Potable y Saneamiento* [Water and Sanitation Division]
ECATEFs	*Empresas Consultoras de Apoyo Técnico y Fiduiciario* [Consulting Firms for Technical and Fiduciary Support]
ESSAP	*Empresa de Servicios Sanitarios del Paraguay S.A.*
FONACIDE	*Fondo Nacional de Inversión Pública y Desarrollo* [National Public Investment and development Fund]
ICAS	Institutional Capacity Assesment System
ICT	Information and communication technologies
MOPC	Ministry of Public Works and Communications
MSME	Micro, small, and medium-sized enterprises
OVE	Office of Evaluation and Oversight
PEU	Project Executing Unit
PROFOMAF	*Programa de Fortalecimiento y Modernización de la Administración Fiscal* [Fiscal Management Strengthening and Modernization Program]
PROPEF	Project Preparation and Execution Facility
REDIEX	*Red de Inversión y Exportación* [Investment and Export Network]
SENASA	*Servicio Nacional de Saneamiento Ambiental* [National Environmental Sanitation Service]
SENATICS	*Secretaría Nacional de Tecnologías de la Información y las Comunicaciones* [National Department for Information and Communications Technologies]
SFP	*Secretaría de la Función Pública* [Civil Service Department]
SME	Small and medium-sized enterprises
SNIP	*Sistema Nacional de Inversión Pública* [National Public Investment System]
TFFP	Trade Finance Facilitation Program

Executive Summary

Paraguay is experiencing a very positive period in its economic history. However, the model of growth based on agricultural exports and macroeconomic stability is showing signs of depletion. Following decades of stagnation and financial instability, the country has been experiencing sustained growth since 2003. This is a reflection of important reforms initiated during the crisis, supported also by favorable market conditions for the country's main goods exports. Economic growth has facilitated significant social progress and advances in modernizing the country. Nonetheless, important challenges remain in terms of building a modern State capable of supporting the development of a more sophisticated economy. Efforts to modernize in certain areas of government, including justice, education, and health, are still insufficient, which stands in the way of opportunities for evolving a more sustainable model of development.

The country also has more public funds available for investment. This is the result, in particular, of new sovereign bond issues and the additional resources obtained through renegotiation of the Itaipú Treaty, which since 2012 have been channeled through the National Public Investment and Development Fund (FONACIDE). Given this greater availability of funding, the country faces the challenge of prioritizing needs and preparing and implementing projects in an efficient manner.

For the Bank, this new growth phase in Paraguay has been accompanied by significant changes in financial relevance and strategic positioning. Until 2013, the Bank's relationship with the country had some immutable characteristics. Firstly, the Bank enjoyed a privileged role in Paraguay as the leading multilateral in the country. Secondly, the country's needs were concentrated in basic infrastructure sectors and entailed a low level of sophistication, and the predominant political economy led to a strong bias in favor of continuity in these sectors. The evaluation period saw the intensification of two trends that affected the Bank-country relationship: the loss of financial relevance and the more complex needs of the client.

First, an alternative multilateral model has begun to develop. In recent years, the Development Bank of Latin America (CAF) has become a major financial partner in the country's development, with growing levels of approvals. Although CAF financing is more expensive than that of the IDB, its business model—with a concentrated portfolio and extensive use of country systems—would appear better tailored to the government's preferences at this economic juncture.

Adding to this is the loss of relevance of Bank approvals in absolute terms, due to growth in the Paraguayan economy and new sources of external financing. The country's economic expansion means that the financial relevance of Bank flows has declined in comparison to the size of public spending and the budget of the Paraguayan government. In addition, new sources of financing have become available: since 2013, the country has been issuing bonds on the international markets, and these funds now amount to a larger sum than the financing provided by the IDB. As a result, the IDB's share of the country's external financing (multilateral plus bonds) has dropped from 70% in the 2000-2008 period to less than 30% in 2014-2017.

The 2013 sovereign bond issues led to a qualitative change in the relationship with the country. Firstly, Paraguay is making increasing use of this new source of financing, which is becoming more available and less expensive, except in periods of crisis. Although there is still room to work with Paraguay due to its low debt levels, the demand for Bank operations will depend on the nonfinancial additionality and technical assistance provided. Related to this is the fact that the shift in sources of financing alters the IDB's bargaining power. In addition, the bond-oriented financing strategy has also changed the way in which investment projects are prioritized and executed. Multilateral bank projects traditionally combine the prioritization of investment needs and their financing into a single technical and financial package. With greater access to international markets, financing is increasingly separate from the process of prioritization. Accordingly, the country is moving toward a more active role in project prioritization and the standards used (as in the case of transportation). Lastly, from a financial point of view, bonds are much easier to execute than IDB investment loans. Authorized amounts for bond issues are included directly in the budget, together with the name of the specific investment project for which the funds are earmarked. Once the budget law is in force, the Executive can implement the project quickly without any further need for legislative process. In contrast, Bank loans (and those of other international organizations) are subject to a formalization process that takes two years on average, including ratification.

Lastly, after 15 years of sustained growth, Paraguay's economy has begun to exhibit a greater degree of complexity. This, in turn, means that the client's needs are much greater and much more demanding than those faced by the Bank in the 1990s. This is not a new phenomenon for the Bank; it is similar to what it has experienced with other clients transitioning to upper-middle-income status. An example of the new needs emanating from the country is the recent promotion of the Digital Agenda. OVE's experience evaluating other country programs indicates that as clients become more sophisticated they place greater emphasis on nonfinancial aspects.

During the evaluation period, the Bank was proactive in its attempts to adapt to the new situation. Firstly, there were renewed efforts to improve the execution of operations and to lower transaction costs for the Bank and the country. Several technical cooperation operations were aimed at financing diagnostic assessments and analyses of execution problems, particularly those experienced after legislative ratification. Technical cooperation operation PR-T1163 addressed important issues for accelerating project execution, such as budget problems. While some progress was made, other changes are still too recent to be evaluated. In addition, toward the end of the period, the Bank attempted to promote the creation of a mega executing unit in the Ministry of Public Works (MOPC), though the effectiveness of this initiative cannot yet be confirmed. Also, the Bank sought to provide assistance in response to new requests from the client, including support for the Digital Agenda and the widespread introduction of information and communications technologies (ICT). As in the case of support for execution, it is still too early to determine whether these measures have been effective.

However, little could be done to address the main bottleneck to project execution: the lengthy legislative ratification process. Although increased ratification times cannot be directly attributed to bonds, there is evidence that Bank projects have been taking longer to ratify since 2013, possibly as a result of lower funding needs. Delays in ratification lead to greater delays in execution. Firstly, project diagnostic assessments often become outdated, requiring changes to components (particularly in the case of projects with major technology components). In some cases, cost estimates become outdated, requiring adjustments to components. Lastly, in some cases, ratification delays have meant that the political window of opportunity for project implementation was lost. This has been the case in particular for projects involving reforms. The Bank has acknowledged the problem and has initiated a dialogue with the country aimed at shortening time frames, although there have not yet been any concrete changes. The ratification process remains the main bottleneck to project implementation in Paraguay, as noted by OVE in past CPEs. In contrast to earlier periods, however, the new source of external financing (international bonds) does not entail the same transaction costs as a Bank project.

In terms of results, progress can be seen in basically all of the Bank's areas of action, although this cannot be directly attributed to IDB projects. The project results achieved during the period under analysis have been mixed, but there is evidence that the most significant achievements were in those sectors in which the Bank has a long-standing relationship. Inertia in the sectors creates its own challenges, yet it offers a number of advantages. There is a tendency to incorporate lessons learned into the subsequent project phases. Also, as mentioned in previous CPEs, even though it takes a long time to execute Bank projects (particularly in infrastructure), they do, ultimately, get implemented. And the ongoing relationship with the execution unit helps get results. In the social sector, the Bank was successful in leveraging the country's resources for projects in a variety of areas. With regard to technical cooperation operations, funding declined over the period and was largely used for operations support. There have, generally, been fewer resources for knowledge generation when compared with the average for the Bank.

In general, however, the Bank continues to experience the same problem identified in earlier periods: it has been unable to work with the country to strengthen governance and create sufficient institutional capacity in the sectors in which it is active. This endangers the sustainability of Bank projects and limits its impact as a development institution. The most successful example in Paraguay has been in the transportation sector, where there has been significant progress. But this also reflects the ex ante degree of institutional development in the sector, as well as the high level of Bank involvement as the main multilateral institution working in transportation. In the other sectors, where the degree of institutional development is lower still and more fragmented, achievements have been significant but do not form part of a more comprehensive strategy of institutional development. The water and sanitation sector is a perfect example of this situation.

Based on the findings of this evaluation, OVE recommends that the Bank:

1. **Redefine the Bank's model of intervention in Paraguay, placing emphasis on a more comprehensive vision of institutional development and targeting sectors where the Bank has a comparative advantage.** The Bank should continue its proactive dialogue with the client to identify emerging needs in this new stage of Paraguay's development. The Bank's institutional support should be more comprehensive and cohesive, preventing a piecemeal approach in institutional strengthening components. In the past, these components have often been difficult to implement. Moreover, as opportunities arise, a strategic vision of the country's institutions will be particularly important for framing the new issues and agendas for the Bank's work (e.g. the Digital Agenda). Independent of these considerations, the Bank should be prepared to reduce fragmentation in its portfolio.

2. Be more strategic in the use of technical cooperation, in order to support this new model of investment at the Bank, which will include more complex operations requiring greater knowledge and expertise. At the moment, a large contingent of technical cooperation operations are used to implement Bank projects. Although this adds value by expediting the execution of projects, it limits the pool of resources available for investing in the knowledge and expertise needed to support the new types of demand coming from the country. Accordingly, Management should continue to identify instruments that are easier to implement and that free up resources so the Bank can also support more complex operations.

3. Continue working with the country to simplify the ratification and budget processes. This is the fourth CPE to identify legislative ratification as a bottleneck for the Bank's work in Paraguay. In contrast to previous CPEs, the country has made use in this evaluation period of international bond issues, which are handled differently from multilateral loans. This introduces the possibility of resuming work with the country to simplify legislative ratification processes, integrating the requirements for Bank loans with those of other comparable external borrowing instruments (e.g. international bonds).

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Background to the Country Program 2014-2018

1.1 Located in the Southern Cone of South America, Paraguay is a landlocked country in which the main source of wealth is linked to the exploitation of natural resources. Although it is predominantly agricultural, Paraguay's economy is growing at a fast clip, marking its transition to a more developed economy. Paraguay's per capita GDP, estimated at US$5,934 at the end of 2018, is the eleventh lowest in the region.[1] Nonetheless, the country's growth rate has been relatively high over the last 15 years, compared not only with its historical average but also with the regional average (Rojas-Suarez, 2018).[2] Since 2015, Paraguay has been classified by the World Bank as an upper-middle-income economy.

1.2 The combination of economic reform and a favorable external backdrop has allowed the country to grow at an above-average rate for Latin America. In general, this improved economic performance was facilitated by the economic and financial reforms that were launched in 2003, which allowed Paraguay to tap into more favorable conditions in external markets[3] (International Monetary Fund, 2016).[4] These reforms included a sweeping public finance overhaul, including the enactment of a Fiscal Responsibility Law, and the adoption of an inflation-targeting regime by an independent central bank.[5] The country's macroeconomic policy management has matured over time and is generally prudent and used to counteract the impact of external volatility.[6]

Recent economic, institutional, and social context

1.3 In the period under analysis for this country program evaluation (CPE), Paraguay's economy continued to expand, outperforming Latin America and the Caribbean as a whole despite a recent slowdown. In the 2014-2017 period, Paraguay's economy grew at an average rate of 4.3%, compared with a 1.8% average for

1 International Monetary Fund (October 2018), World Economic Outlook.

2 Rojas-Suarez (2018). *Paraguay: Is good macro policy enough to ensure adequate resilience to adverse external shocks? How does it compare to other emerging markets?* Center for Global Development Working Paper #477.

3 External conditions during the period were very favorable to Paraguay, with annual export growth of 7.7% between 2003 and 2008. In a marked departure from the previous trend, GDP per capita grew by 16% between 2002 and 2008 (2.5% per year), compared with a decline of 12% between 1996 and 2002 (2% per year).

4 International Monetary Fund (2016). *Paraguay: Staff Report for the 2016 Article IV Consultation.*

5 Central Bank of *Paraguay (2016). Paraguay: más allá de la estabilidad macroeconómica. Logros y desafíos.*

6 The inflation-targeting regime entails a floating exchange rate system in which the monetary authority intervenes solely to dampen market volatility. The annual inflation rate has remained in check at about 4%. The government deficit averaged less than 1% of GDP from 2012 to 2017, and public sector debt (including the central bank) was estimated at 18.2% of GDP at the end of 2017.

the region.[7] Although this rate is lower than in the previous decade—in which Paraguay grew 4.6% per year as compared with 3.9% for the region—it is still noteworthy considering the sharp drop in commodity prices.

1.4 The period was also characterized by favorable conditions for the traditional export sectors: agriculture and electricity.[8] External demand conditions for Paraguay's chief agricultural commodities (soybeans, grains, and beef) were favorable, and power exports grew steadily.[9] Together, these two sectors account for 35% of GDP. More recently, a decline in export prices has been offset by positive results in terms of the electricity supply[10] and agricultural output (owing to a good soybean harvest), along with newly rising consumption and investment (both public and private) and a recovery in *maquila* activities.

1.5 Growth in Paraguay remains fundamentally based on the use of natural resources, and the country still faces barriers that limit its competitiveness and, thus, its potential for development based on the productive sector. The agricultural frontier has expanded considerably in recent decades.[11] Soybean production rose from 3,500,000 tons in the 2000/2001 harvest to 10,340,000 tons in the 2016/2017 harvest. During the same period, wheat production rose from 220,000 to 1,280,000 tons, and corn from 950,000 to 4,500,000 tons.[12] At the same time, unemployment remained low,[13] but with a high level of informality. Thus, the Paraguayan economy is experiencing an upsurge in growth linked to greater utilization of the factors of production (intensive margin). As the country exhausts the possibility of expanding its resource use, the challenge arises of improving the productivity with which the resources are used (extensive margin). Accordingly, to ensure sustained growth over the long term, the Paraguayan economy faces the essential challenge of increasing its productivity.

7 The average for the region includes the average for the IDB's 26 borrowing member countries. All estimates for 2017 are from the International Monetary Fund.

8 Electricity not consumed in the country is sold by agreement to Brazil and Argentina, and this has become the country's main export, generating on average around US$2,103,600,000 per year between 2014 and 2017 (Central Bank of Paraguay, Monthly External Trade Tables, 2017).

9 Paraguay has an unusual energy matrix: it is one of the largest electricity exporters in the world but simultaneously has one of the lowest levels of electricity consumption per capita and the highest consumption of biomass in Latin America and the Caribbean. In 2015, energy exports—mainly electricity—represented 26% of total exports on average, while 12% of imports over the period consisted of fuels and lubricants. However, peak demand was close to 3,000 MW in 2017, leaving a surplus of more than 5,500 MW.

10 Both of the country's hydropower plants generated record amounts in 2016.

11 Consejo Agropecuario del SUR (2017). *Análisis de Capacidades Institucionales – Paraguay.* FAO.

12 http://capeco.org.py/

13 World Bank, World Development Indicators.

Key barriers include the quality of infrastructure, low levels of access to credit, an inadequately trained workforce, low levels of innovation, and inefficient regulations.

1.6 Paraguay faces basic problems of infrastructure. The 2017 Global Competitiveness Index produced by the World Economic Forum ranks Paraguay 118th out of 137 countries in terms of the quality of its infrastructure, and infrastructure deficiencies are one of the main obstacles to domestic economic activity and foreign investment. Paraguay's landlocked position means that roads play a critical role in integrating the country into the regional and global economies. Although the country's inventoried road network has undergone sustained expansion and quality improvements,[14] the length and quality of the network remains deficient, particularly in the western half of the country.[15] In addition, although Paraguay has abundant surface water and groundwater resources,[16] these are distributed unevenly across the country.[17] Water and sanitation services are provided by a multitude of operators of different sizes, financial and technical capacities, and legal status, and investment in the sector[18] remains insufficient to meet targets for the elimination of service gaps.[19]

1.7 Although Paraguay's indicators for access to and use of financial services have improved considerably,[20] there is still a need for long-term financing mechanisms, and financial inclusion is incomplete, particularly in rural areas and for micro, small, and medium-sized enterprises (MSMEs). Paraguay has 15 first-tier private banks, in addition to first- and second-tier State-owned banks. The purpose of the government lending institutions

14 According to the Ministry of Public Works and Communications (MOPC), the length of the inventoried road network stood at 75,120 km in 2018, compared with just over 31,200 km in 2011.

15 Nearly all of the main roads are paved. The percentage is 32% in the case of departmental roads (most of which have stone surfacing), and just 1.4% in the case of rural roads.

16 IDB and the Economic Commission for Latin America and the Caribbean (2018). Proceso Regional de las Américas Foro Mundial del Agua 2018: Regional Report. Available at: https://www.cepal.org/sites/default/files/news/files/informe_regional_america_latina_y_caribe.pdf.

17 These resources are abundant and readily accessible in the eastern part of the country.

18 Most of these investments have been directed into rural water and sanitation. In fact, the National Environmental Sanitation Service (SENASA) has been the main executor of investment in the sector, accounting for 64% of the total.

19 According to the National Water and Sanitation Plan (2018) prepared by MOPC-DAPSAN, investment in water and sanitation has varied in recent years, averaging US$55 million per year from 2014 to 2017. However, it is estimated that annual investment of US$487.4 million would be required each year to close the gap in service coverage by 2030.

20 This was due to improvements in indicators such as the number of branches and the number of ATMs in the case of access variables, and the volume of loans and deposit accounts in the case of usage variables. Paraguay also leads the region in the development of mobile money services, and 29% of the population has a mobile money account, according to the World Bank's FINEX survey (2017).

(Agencia Financiera de Desarrollo, Fondo Ganadero, and Crédito Agrícola de Habilitación) is to promote economic development by channeling resources to the productive sectors; however, their interest rates are similar to those available from private banks. MSMEs continue to have a hard time getting credit, and this limits their ability to grow and innovate.

1.8 Despite the country's economic growth, social progress in Paraguay has been limited. The noncontributory social programs created by different governments, together with the economic growth of recent years, have led to small gains in poverty indicators. Nonetheless, there is still room for improvement in the social sectors. The poverty rate fell from an average of 30.4% in the 2009-2013 period to 27.3% in 2014-2017. Over the same period, extreme poverty—still predominantly rural in nature—was 5.3%.[21] In terms of labor conditions, unemployment rose from 4.4% in 2013 to 5.8% in 2017,[22] while the rate of underemployment is close to 20%. The level of informality in the country is high, at more than 75% of workers in 2017.[23] The Gini coefficient remained virtually static during the period, at around 48.[24]

1.9 Weak productivity is partly the result of low levels of quality in the education and health systems. Considerable progress has been made in education in terms of coverage and years of schooling. The average number of years of schooling for individuals over 25 years of age rose from 7.4 in the 2004 2008 period to 8.7 in 2014 2016. Nonetheless, educational quality remains low; the World Economic Forum (2016) has Paraguay among the lowest-ranked countries in terms of several education quality metrics. Weaknesses are significant in preschool enrollment and, in particular, in workforce training and development programs. Only 27% of the economically active population completes secondary school, while only 10% of the population has post-secondary education.[25] According to that same organization's

21 Poverty declined from 27.2% in 2014 to 26.4% in 2017 (20.7% to 20.3% in urban areas and 37.0% to 36.2% in rural areas). Extreme poverty dropped from 5.5% to 4.4% (2% to 1.6% in urban areas and 10.7% to 9% in rural areas) (Bureau of Statistics, Surveys, and the Census (DGEEC), 2018) http://www.dgeec.gov.py/Publicaciones/Biblioteca/pobreza/Boletin%20de%20pobreza%202017.pdf.

22 World Bank, World Development Indicators.

23 Paraguay's labor market is characterized by a high level of underemployment, which in 2016 affected 12.1% of the economically active population. Paraguay also has a very young population: close to 57% is under 30. In 2016, the primary sector (agriculture, livestock, hunting, and fishing) accounted for 21.7% of the employed population, the secondary sector for 11.1% (manufacturing industry), the construction sector for 7.7%, and the services sector for 59.5%.

24 *Ibid*.

25 *Paraguay: Desafíos para el mejoramiento de la Educación Técnica y Profesional 2014-2018.*

Global Human Capital Index,[26] Paraguay ranked 90 (out of 130) in 2017, representing an improvement from 98th position in 2013.[27] Similarly, despite progress in the area of health,[28] maternal and infant mortality rates are still substantially higher than in Latin America and the Caribbean as a region[29] and in countries with a similar income level. The health system is fragmented and lacks the capillarity to meet the basic needs of the most deprived sectors of the population.[30]

1.10 In addition to the foregoing, State institutional capacity in Paraguay remains weak. Economic growth was not duly accompanied by institutional development (Figure 1.1), and as a result the Paraguayan government has not managed to effectively deliver the basic public goods associated with a more developed economy. Governance failures also limit the return on investments in physical and human capital (Hausmann et al., 2005).[31] In particular, given the country's productive structure, the government's ability to provide basic infrastructure works (roads, ports, waterways) is critical for increasing the return on physical investments. The IDB study "Paraguay: Rutas para el Desarrollo"[32] indicates that the country faces many barriers to improving its institutions, highlighting the low quality of public services,[33] intragovernmental coordination failures, a fragile justice system, limited institutional capacity for transparency and accountability, and deficiencies in national information systems. The perception of corruption remains a problem, too: Transparency International ranks Paraguay 123rd out of 176 countries on this variable.

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26 This measures how well a country is developing its human capital on a scale of 0 (lowest) to 100 (highest), with four thematic subindices: capacity, insertion, development, and knowledge.

27 This was still below other regional economies such as Chile (53), Bolivia (54), Peru (66), Ecuador (76), and Brazil (77).

28 Life expectancy at birth rose from 71.5 years to 73 years over this period.

29 The average infant mortality rate in Latin America and the Caribbean (2010-2015) was 25.4 per 1,000 live births, while in Paraguay it was 30.8 per 1,000 live births. The average maternal mortality rate in Latin America and the Caribbean was 57.9 per 100,000 live births (2016), compared with 81.8 per 100,000 live births in Paraguay. Source: Economic Commission for Latin America and the Caribbean. https://www.cepal.org/Celade/publica/bol62/BD6206.html.

30 Alum, J. and M. de Bejaramo (2011). *"Sistema de Salud en Paraguay"*, Rev. de Salud Pública Paraguay, vol. 1(1): 13-25.

31 R. Hausmann, D. Rodrik, and A. Velasco, 2005, *Growth Diagnostics*, John F. Kennedy School of Government, Harvard University (Cambridge, Massachusetts).

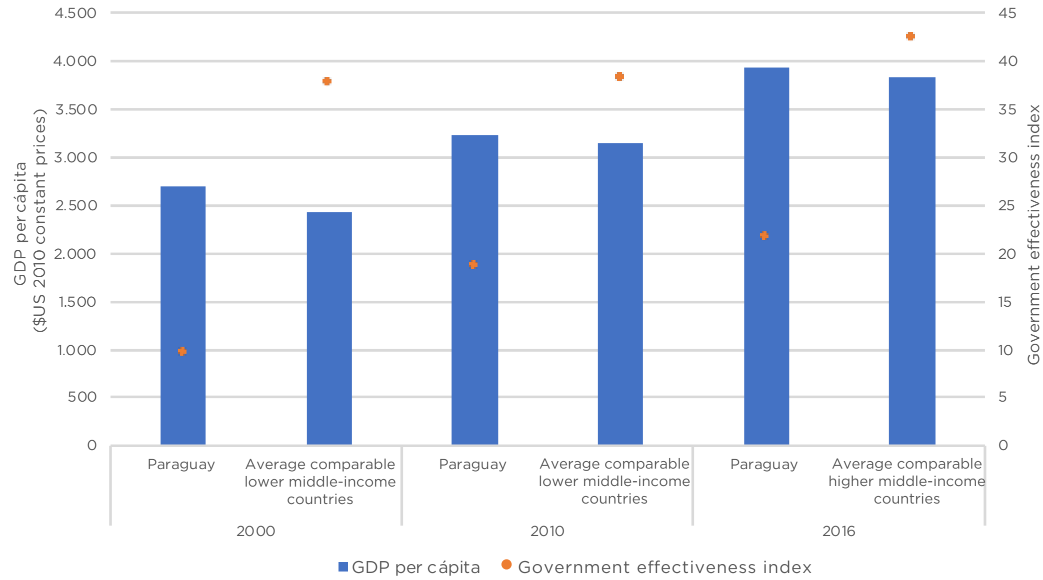
32 E. Almeida, F. Bastos, A. Quijada, and M. C. Acevedo (2018). Paraguay: Rutas para el Desarrollo, Inter American Development Bank, Washington D.C.

33 The IDB's Civil Service Development Index for Paraguay rose from 12 to 40 between 2004 and 2017, equivalent to the regional average and reflecting a medium level of development. V. Dumas, 2017. Diagnóstico Institucional del Servicio Civil en América Latina: Paraguay. Nota Técnica IDB-TN-1345.

Figure 1.1

Evolution of Paraguay´s governance index versus similar-income countries

Source: Governance indexes form the World Bank. GDP per capita from the WEO, IMF.



Nota: La efectividad del gobierno captura las percepciones de la calidad de los servicios públicos, la calidad del servicio civil y el grado de independencia de las presiones políticas, la calidad de la formulación e implementación de políticas y la credibilidad del compromiso del gobierno con dichas políticas. El rango percentil indica el rango del país entre todos los países cubiertos por el indicador agregado, donde 0 corresponde al rango más bajo y 100 al rango más alto. Los rangos porcentuales se han ajustado para corregir los cambios en el tiempo en la composición de los países cubiertos por el Índice. Para cada periodo se toman cuenta países con el PIB per cápita en el rango de US$1000 arriba y por US$1000 debajo de Paraguay.

1.11 A particularly important challenge for the Paraguayan economy is to use its investment resources more strategically and efficiently. In 2012, the country adopted the National Public Investment System (SNIP), which has helped to structure public investment and ensure that the most economically viable projects receive financing. However, this is just a first step.[34] Although such advances are important, there is still no public investment law to organize the planning, execution, and evaluation of public investment, or the institutional capacity needed to implement this investment. The execution of public investment projects is complicated by the rigidity of the budget structure and its administration, weak government control systems, a lack of qualified human resources, and the multiplicity of actors and documents required for any bureaucratic procedure (OECD, 2018).[35] In addition to this, the number of projects has increased significantly in recent years, further aggravating these challenges.[36]

34 Ministry of Finance (2017). *SNIP PY – 5 años invirtiendo en el país – compendio.* http://snip.hacienda.gov.py/normativas/compendio_snip.pdf.

35 OECD (2018). Multi-dimensional review of Paraguay. Vol 1. Initial Assessment, OECD Development Pathways, OECD Publishing, Paris.

36 Ministry of Finance (2017). *SNIP PY - 5 años invirtiendo en el país – compendio.* http://snip.hacienda.gov.py/normativas/compendio_snip.pdf.

1.12 Lastly, the economy remains vulnerable to external shocks due to its concentration by product and market. Key exports are concentrated and exposed to unpredictable climate phenomena (agricultural products). They are also vulnerable to significant, wide-ranging fluctuations in international markets. At the same time, exports are sent to a small number of trading partners, with more than half of exports sold to MERCOSUR countries, mainly Brazil. This reinforces Paraguay's vulnerability to business cycles in neighboring countries.

1.13 Paraguay still has significant opportunities to strengthen its development. The country has abundant natural and human resources, including a number of resources of great strategic value, such as aquifers, minerals, and energy resources. At the same time, a demographic transition is fully underway, with the country enjoying the "demographic dividend" of a growing population of young people of working age. Paraguay's status as a producer of surplus renewable energy is exceptional and helps to ensure that its electricity costs are among the lowest in the region. The country is in a favorable position for financing its development. Not only does it have the additional funds stemming from renegotiation of the Itaipú Treaty,[37] but also in 2013 it took the first steps toward tapping international capital markets. Since then, it has issued sovereign bonds for a total of US$2.8 billion. Debt levels are low and Paraguayan debt has become more competitive.[38] Since 2013, Paraguay has had a legal framework to promote public-private partnerships—Law 5,102/2013. Although only one infrastructure project has so far been developed under this framework,[39] reforms introduced in 2016 have led to the initiation of economic assessments for another three government-led initiatives and two private-led ones.[40]

37 The National Public Investment and Development Fund (FONACIDE) is a development fund created under Law 4,758/2012 that seeks to allocate in a rational and efficient manner the revenues that the country receives from Brazil as compensation for the power surplus generated by the Itaipú binational hydroelectric plant. The Fund is earmarked for education, infrastructure investment, health, and credit to the private sector.

38 The presence in international markets has been favorable and Paraguay's credit rating has improved steadily, from BB- in 2013 to BB with a stable outlook currently (Fitch Ratings).

39 In 2016, bids were invited for the first concession contract under the Public-Private Partnership Law: the expansion of Routes 2 and 7 (for US$520 million), which was signed in 2017. http://www.stp.gov.py/v1/inician-obras-de-mejoramiento-de-las-rutas-2-y-7/.

40 Informe de Gestión, Dirección de Proyectos de Participación Público-Privada [Department for Public-Private Partnership Projects].

02

IDB Strategy and Programming (2014-2018)

2.1 In late 2014, the Paraguayan government approved the 2030 National Development Plan.[41] The plan was developed in consultation with more than 2,000 key stakeholders, including the government, the private sector, and civil society, who over a period of one year identified and analyzed the country's main needs. The document sets out three priority strategic pillars: (i) poverty reduction and social development; (ii) inclusive economic growth; and (iii) Paraguay's inclusion in global markets. These pillars are addressed via four crosscutting lines of activity (equal opportunities, efficient and transparent public management, land use planning and development, and environmental sustainability), resulting in 12 strategies that will guide public policy with a view to building the Paraguay of 2030.[42] The strategies outlined in the plan are a response to the country's main challenge, which is to strengthen its economic growth outlook while seeking more equitable income distribution.

2.2 The country strategy document for 2014-2018, approved in May 2014, incorporates the recommendations of the previous CPE[43] and is aligned with the lines of action included in the National Development Plan (Annex, Table I.1). The strategy was designed in a context of high growth rates and the consolidation of a relatively undiversified agroexport model. According to the strategy document, growth "has not been very inclusive: employment generation has been low, and there has been little progress in reducing poverty [...] and extreme poverty [...]." In response to the identified challenges and the dialogue with the country, the Bank established the following strategic objective: "to support the country's productive transformation, with a view to achieving sustainable and inclusive economic growth that will translate into reduced poverty and inequality, through the generation of formal employment." To this end, the Bank prioritized interventions in the following sectors: (i) transportation and connectivity; (ii) water and sanitation; (iii) energy; (iv) productive development; (v) the financial sector; and (vi) public management. In addition to these priority areas, the strategy includes two crosscutting elements: support for the National Public Investment and Development Fund (FONACIDE), with a view to leveraging the use of government resources in education and health, and the inclusion of gender considerations and indigenous communities in Bank programs and initiatives.

41 The plan was the first to be approved, despite a constitutional requirement introduced in 1992.

42 Paraguay 2030 National Development Plan.

43 Box I.1 in the Annex lists the recommendations of the previous CPE, Management's responses, and the degree of compliance during the current period.

2.3 Both the approved program and the legacy projects from the previous period are generally aligned with the Bank's country strategy and, accordingly, with the country's needs. The program approved under the 2014-2018 country strategy is closely aligned with national priorities, as defined in the diagnostic assessments prepared during the strategy design phase, as well as with independent assessments of Paraguay's development challenges and the strategic pillars included in the National Development Plan 2030. Project objectives and their relationship with those of the strategy are listed in Table I.2 in the Annex.

Table 2.1. Available amount and number of operations by country strategy objective

Area of intervention	Strategic Objective	Amount approved (US$ million)		Number of approved operations	
		Loans	Technical cooperation operations	Loans	Technical cooperation operations
Transportation and connectivity	Transportation infraestructure and road safety	981.2	1,6	11	3
Water and sanitation	Water, sewerage and wastewater treatment	157.2	2.6	3	4
Energy	Electricity sustainability	61.4	0.4	2	1
	National biofuel production				
Productive development	Enterprise productivity and competitiveness	294.2	1.1	16	2
	Legal protection for land ownership				
	Delivery of agricultural public goods and services	34.8	0.3	3	1
Financial Sector	Financing through the financial system	625.3		18	
Pubic management	Fiscal sustainability	5.3	0.9	1	2
	Reduce levels of violence and crime	20.3		2	
	Effectiveness, transparency, and integrity of public entities	204.5	3.3	2	12
Crosscutting area	Student performance in language and communication	23.8	1.7	2	3
	Coverage of upper secondary education				
	Maternal and neonatal health		0.4		1
Not directly alligned		90.8	5.7	5	16

* The available amount for the period is included for loans approved prior to 2014.
Source: OVE, using IDB databases.

A. The IDB's financial and nonfinancial relevance in Paraguay

2.4 During the period under analysis (January 2014 to May 2018), the Bank approved a total of US$1.297 billion in sovereign lending (20 loans), slightly more than the level anticipated in the country strategy;[44] US$149.9 million in non-sovereign guaranteed lending (16 loans and part of a hybrid loan-guarantee operation); and US$123.5 million in private sector guarantees (4 guarantees and part of the hybrid operation).[45] In addition, a total of US$20.6 million was approved for technical assistance (54 technical cooperation operations).[46] Among the sovereign guaranteed loans approved were two policy-based loans (PBLs) for a total of US$400 million.[47] Table 2.2 displays the total number of public sector operations and the amounts approved by area of intervention, as set out in the country strategy.

Table 2.2 Sovereign guaranteed portfolio approved from 1/1/2014 y el 31/5/2018, by area of intervention

Area of intervention	Technical cooperation operations		Loans	
	Number of approvals	Amount approved in US$ millions	Number of approvals	Amount approved in US$ millions
Transport and connectivity	4	2,1	5	517
Energy	1	0,4	0	0
Water and sanitation	9	4,8	2	150
Productive development	4	1,5	5	250
Financial sector	4	0,3	3	90
Public management	18	5,8	2	220
Crosscutting area	11	4,2	3	70
Others	3	1,5	0	0
Total	**54**	**20,6**	**20**	**1297**

Note: Environmental projects were included under water and sanitation. The crosscutting area includes social sector and housing projects.

Source: OVE, using IDB databases.

2.5 The Bank is involved in practically every sector, although there is a high degree of inertia in approvals, which are concentrated in infrastructure (see Table 2.1). The loan portfolio has historically

44 The tentative sovereign guaranteed lending scenario was US$1 billion, based on the premise of significant progress with respect to execution levels.

45 These figures do not include Trade Finance Facilitation Program (TFFP) operations, but they do include canceled operations.

46 These figures do not include Multilateral Investment Fund (MIF) operations.

47 The two PBLs are PR-L1144 and PR-L1101.

been concentrated in the infrastructure sector (52% of IDB approvals from 2014 to 2017), particularly transportation, followed by operations relating to productive development (19%) and public management (17%). In this sense, there were no significant changes compared with the previous strategy period, as can be seen from the legacy portfolio. In fact, the Bank's work in most sectors is based on well-established intervention strategies, which in some cases have lasted more than 20 years, e.g., rural roads with four consecutive loans since 1993, the rural water and sanitation strategy, and reform of the public development banks since 2002 (see Annex, Figures I.1 and I.2). The legacy public sector portfolio consists of all operations approved prior to 2014 and includes twenty loans: eight in infrastructure (four in transportation, two in energy, and two in water and sanitation), four in productive development, three in the social sector, three in public management, and two in the financial sector. In addition to these operations, there are twelve legacy private sector operations from the previous period.[48] The Bank's portfolio is strongly concentrated in the infrastructure sectors, with a high degree of inertia. This focus is associated with the high transaction costs related with legislative ratification of the projects (as described in the implementation section).

2.6 In financial terms, the Bank remains an important partner, although its relative importance has been declining.[49] The Bank has historically been the main partner in Paraguay's development, and there is a strong degree of inertia in its model of intervention, despite changes in the country (Box 2.1). In the current period, the Bank's position as a privileged partner in financial terms is in jeopardy. Firstly, growth in the country and a fragmented portfolio mean that the Bank's participation in each sector is small relative to investment spending and growing smaller still (Figures I.17 and I.18 in the Annex). In addition to this natural and anticipated phenomenon, there were three significant events during the evaluation period.

Box 2.1. Structural patterns in the Bank´s actions in Paraguay

OVE has reviewed the program with Paraguay on three occasions, at different moments in the country's history. These reviews suggest a series of long-term structural patterns in the country and its relationship with the Bank.

48 The criteria for inclusion in the private sector legacy portfolio were that a loan had to still be active as of June 2018 and had to have an approval date prior to the evaluation period.

49 Consistent with the Paraguay CPE 2009-2013 and the country strategy with Paraguay 2014-2018.

Structural features of the country	Bank programming	Recurring OVE recommendations
• Agricultural country with a relatively undiversified economy that is highly vulnerable to economic and climate shocks. • A small, weak State with a limited democratic tradition. • A privileged relationship with the IDB as the main source of financing and technical dialogue. • Project launch delays related to legislative ratification, which affects continuity, raises transaction costs, and accelerates the technical obsolescence of projects.	• Programming initiatlly concentrated in three areas (infrastructure, productive sector efficiency, and modernization of the State). Towards the end of the 1990s, the portfolio started to become more fragmented. • Absence of a strategic operational model to guide the Bank's actions and capitalize on its privileged position in the country. • Bank programming treats execution problems more as a risk than as the focus of Bank action. • The problem of limited technical/ institutional capacity is addressed disjointedly through components under loans rather than through a comprehensive program of institutional strengthening.	• Support the country in preparing a development model. • Support the country in developing a model for integrating the Paraguayan economy into international markets. • Develop a comprehensive strategy for institutional strengthening.

2.7 A first change has been the consolidation of the Development Bank of Latin America (CAF) as an important multilateral partner for the country.[50] Paraguay became a full member of CAF in 2008, and the institution opened an office in Asunción in 2012 with the aim of strengthening its relationship with the country. From the outset, CAF has focused its action on sectors in which it has comparative advantages: transportation, energy, and the private sector. Based on approvals under the latest programming cycle, CAF approved 20% more financial resources than the IDB Group, despite the fact that its loans are more expensive for the country in financial terms. This occurred despite the fact that IDB approvals for Paraguay under the current strategy were the highest ever (US$1.5645 billion, compared with US$1.052 billion in 2009 2013 and US$756 million in 2005-2008).[51] Despite this, the Bank continues to hold the highest percentage of the country's debt to multilateral and bilateral organizations.[52]

50 CAF's role has been expanding throughout the region: it approved an annual average of US$10 billion in loans between 2009 in 2013, compared with the IDB's US$12 billion.

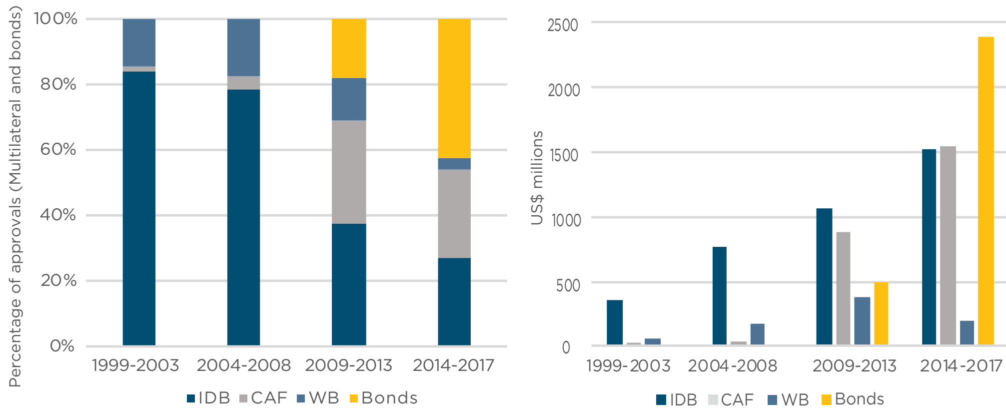
51 Including sovereign and non-sovereign guaranteed loans and approvals up to May 2018.

52 Bilateral and multilateral debt increased in nominal terms from US$1.705 in 2005 to US$2.671 in 2017, while as a proportion of total debt it fell from 73% to 37% as a result of diversification of financing sources.

Figure 2.1

Approval of multilateral loans and bonds

Source: OVE, using IDB databases.



2.8 A second element is the increase in availability—already apparent at the end of the previous period—of other funds for public investment. The previous CPE mentioned that renegotiation of the Itaipú agreements with Brazil would provide Paraguay with new funds for the social sectors (FONACIDE), and on average these have totaled US$51.1 million per year (2012-2017).[53] Adding to this has been the government's strategy, which in 2014 undertook to increase infrastructure investment by both the State and private stakeholders. As a result, public investment rose from an average of US$2.631 billion per year from 2009 to 2013 to US$3.513 billion in 2014-2017. Although average approvals by the Bank increased, its share of financing for investment in physical and human capital declined to 9.3% of total expenditure by the country, compared with 12.5% in the previous period (see Annex, Figure I.19).

2.9 Lastly, in the period under analysis, the country consolidated its new strategy of using sovereign bonds to finance investment (see Box 2.2), and this altered the dynamic between the country and the Bank in several respects. Since 2013, the executive branch has been authorized under the annual budget law to issue National Treasury bonds and keep them in circulation. These are issued exclusively for productive investments or for refinancing government liabilities.[54] Once the government began to prioritize bond financing, the IDB's portfolio faced a new series of execution problems. Firstly, problems relating to ratification intensified (as described in the following section).[55] Secondly, the implementation of Bank projects was affected because

53 Department of Financial Administration, Ministry of Finance.

54 The 2013 budget law (Law 4848/13), which authorized the first bond issue, also established exactly which types of investments the executive branch could use these resources for. In particular, it established that bond proceeds may not be used to finance current expenditure.

55 Although the longer ratification period cannot be directly attributed to international bond issuance, recent years have seen a marked increase in the average number of days, from 436 days for projects approved in 2013 to 624 for projects approved in 2016 (a figure that is likely to increase given that there are projects approved in 2016 that have still not been ratified).

executing units tended to prioritize the use of bonds, which they are able to get more quickly and at lower cost. Moreover, from the point of view of an executing unit, IDB projects ensure that funding is available over a multiyear period (although at a cost to the country, i.e. the credit fee), while sovereign bond financing has to be negotiated and approved each year. Thus, executing units have a greater incentive to execute bond-financed budget lines first, resorting to IDB funding only thereafter.[56]

Box 2.2. International bonds

Paraguay's first international sovereign bond issue took place in 2013 for US$500 million with a maturity of 10 years. Since then, international bonds have been issued annually: (i) in 2014, there was a US$1 billion issue with a 30-year maturity; (ii) in 2015, the 2013 bond was reopened for a further amount of US$280 million; (iii) in 2016, there was a US$600 million issue with a term of 10 years; (iv) in March 2017, an international issue took place for US$500 million with a 10-year maturity; and (v) in 2018, for US$530 million with a term of 30 years.

Treasury bond issues on the international market have helped to diversify sources of financing, lower the average interest rate on bonds, and extend the debt maturity profile. Treasury bonds issued on the domestic and international markets now account for more than 50% of Paraguay's total public debt. Debt to multilateral and bilateral financial institutions increased by US$210.2 million over the period, while new debt in the form of international bonds totaled US$3.41 billion. As required under law, the overwhelming majority of funds obtained on the markets were transferred to the Ministry of Finance (40%), the Ministry of Public Works (MOPC) (42%), and the National Electricity Administration (ANDE) (10%) for the purposes of debt management and productive investment.

2.10 Despite the loss of financial relevance, the Bank sought to act on key issues for the country, thus strengthening its nonfinancial relevance. In this sense, the IDB has helped to leverage the country's investment resources and eliminate bottlenecks to public investment, addressing the first and third recommendations of the previous CPE. For example, the IDB has collaborated with the Paraguayan government to strengthen the country's public investment capacity, one of the main bottlenecks, by strengthening country systems, particularly the SNIP (see paragraph 3.24). The Bank not only helped the country to develop that system, but it also sought to support the Ministry of Finance in developing methodologies and training the staff of executing units, including in the PM4R methodology developed

56 For example, the first bond issue was used to finance the Madame Lynch viaduct that connects the center of Asunción to the airport. This project was implemented in one year. In contrast, IDB loans first need to be ratified individually by the legislative branch, and this takes two years on average.

by the Bank.[57] The Scholarship Program (PR-L1086) helped to leverage the country's own funds, complementing resources from the Fund for Excellence in Education and Research (FEEI), which is part of FONACIDE[58] (see paragraph 3.27 for other examples). Lastly, the Bank supported the ICT strategy (Digital Agenda) by providing assistance for strengthening the recently created the National Department for Information and Communications Technologies (SENATICS) and by conducting studies to promote digital transformation of the health sector.[59] These actions demonstrated the Bank's attempts to strengthen the nonfinancial value added of its operations.

2.11 The Bank has also played an important role in terms of technical assistance, which is generally very well received by clients. The General Perception Survey developed in 2016 by the IDB's Office of Strategic Planning and Development Effectiveness (SPD) reports that 21% of those interviewed consider technical assistance or nonfinancial support to be the Bank's most valuable contribution, with a further 8% identifying knowledge products as most valuable. The IDB continues to be the main provider of technical assistance in the country (Annex, Figure I.10).[60] However, technical cooperation resources for Paraguay have been declining steadily, due among other reasons to the end of funding from the Fund for Special Operations (FSO). There is also a tendency by the Bank to use available technical assistance funding for operational purposes: during the period analyzed, 25% of technical cooperation resources were used for this purpose. Paraguay is the Southern Cone country for which fewest studies are produced, owing, among other things, to data scarcity (Annex, Figure I.25). In terms of technical cooperation funding for knowledge, the data contained in the report "Knowledge Generation and Dissemination in the IDB," prepared by OVE (document RE-517), show that while the Bank allocated an average of 30% of technical cooperation resources to knowledge products between 2010 and 2016, in the case of Paraguay this was less than 15%.

57 PM4R is a course delivered by the IDB with the objective of strengthening participants' capacities for the management of development projects.

58 Funding for the program is US$73 million, of which US$50 million were provided by the IDB and the remainder by the FEEI.

59 SENATICS was created in 2013 (Law 4989). One of its roles is to introduce ICT into public service delivery and the internal management of public institutions. Technical cooperation operation PR-T1255, approved in 2018, is in the early stages of execution and is expected to conduct preparatory activities for the Digital Agenda loan, which is in the pipeline with an expected approval date of November 2018 (PR L1153, US$130 million).

60 CAF technical assistance is mostly for the operational support of its loans.

B. Implementation

2.12 The IDB's portfolio expanded during the evaluation period, adding pressure to the existing execution problems in the country. In fact, analysis of the Bank's institutional capacity assessments of its main executing units (Institutional Capacity Assessment System, ICAS) shows that the units exhibit a low level of development and that progress in strengthening them has been slow (see section II of the Annex). The case of the Ministry of Public Works and Communications (MOPC) is significant, as it is the main executing unit for IDB projects.[61] Successive ICAS studies since 2006 indicate that the MOPC has a medium level of development (and a medium level of risk), a classification that has remained more or less constant. To mitigate these difficulties, the Bank created a centralized project execution agency in 2016. Although it is too early to evaluate the effectiveness of this measure, some of the challenges can be highlighted, particularly its cost and consequent long-term sustainability issues, as well as its lack of effectiveness in helping to strengthen the MOPC.[62]

2.13 The fact that rising approvals have not been accompanied by clear improvements in execution has led to a rapid accumulation of undisbursed balances since 2013. As mentioned above, approvals reached a record level during the current period. In the absence of a radical change in the implementation model for Bank projects, this has translated into rapid growth in undisbursed balances (Figure 2.2). Although this is not necessarily a bad thing for the IDB (given that the credit fee, which increased by 50 basis points over the period, probably exceeds the opportunity cost for the Bank), it is undesirable from a developmental standpoint.[63] In addition to this increase in approved amounts, the number of active projects has risen and the portfolio remains fragmented (despite the increased size of investment projects).[64] Increased numbers of projects not only generate higher costs associated with the creation of executing units (expenditure on projects'

61 In fact, six out of the 20 investment loans approved during the period (30%) are with the MOPC.

62 The evaluation of the project executing unit (PEU) identified five areas in which opportunities exist for improvement. In addition, the leadership of the PEU contends that its current model of partial autonomy from the MOPC is a hurdle to faster execution of the projects under its responsibility. In addition, costs associated with financing the PEU (staff, office leasing, etc.) have been charged and a significant share of the staff have been hired either by Consulting Firms for Technical and Fiduciary Support (ECATEFs) or by the Bank itself. In addition, the PEU operates out of premises that are some distance from MOPC offices, which hinders communication between the two entities, and knowledge transfer is limited.

63 Close to 10% of the financial costs of Bank loans in Paraguay are associated with credit fees.

64 According to the Loan Management System, the number of active loans rose from 38 per year in 2010-2013 to 44 per year in 2014-2017. The average size of investment projects rose from US$31 million to US$48 million in this period, as compared with the previous period.

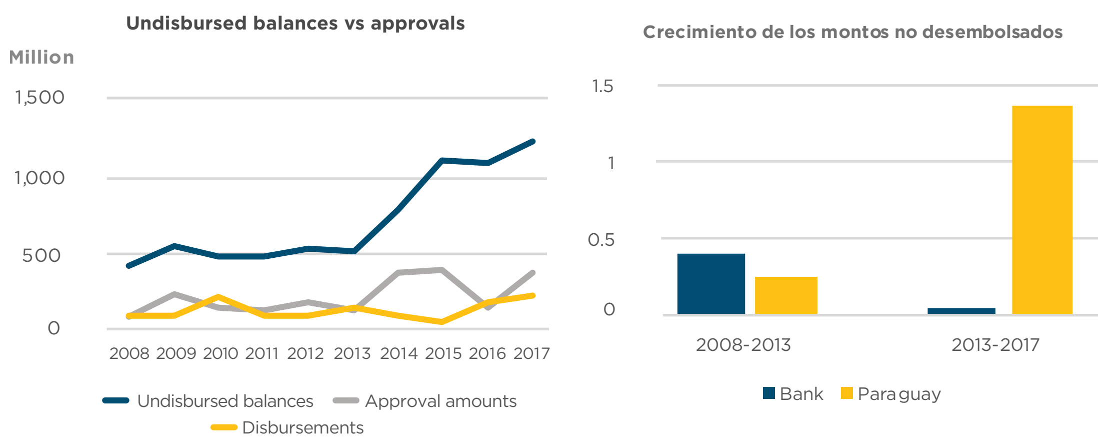
administrative components rose from US$15 million to US$35 million), but they also place more pressure on the IDB's Country Office once the portfolio matures and execution is fully underway (between 2010-2013 and 2014-2017, the number of approved projects for which no disbursement had yet been made rose from five to 11).

2.14 In terms of preparation and execution costs, there were no significant changes, although a reduction in execution costs did occur over the period. Costs relative to disbursed amounts fell from US$17,000 per US$1 million disbursed between 2011 and 2013 to US$14,000 per US$1 million from 2014 to 2018. The Bank average, though much lower, at around US$6,000 per US$1 million disbursed, rose by 10% over this period (Annex, Table I.13). Although this might be explained by Bank steps to mitigate some of the execution problems in the country—in particular, by strengthening the model of service units in the Country Office and training the staff of executing units—it might also be the result of a tendency for project administrative expenses to rise. In other words, part of the reduction in Bank supervision costs is associated with the use of ECATEFs to support project execution, as the cost of these companies is covered by administrative expense components in the loans.[65]

Figure 2.2

Undisbursed balances

Source: OVE, using IDB databases.



2.15 In general, the Bank has been proactive in seeking solutions to some execution problems. Prior to approving the country strategy, the Bank reached an agreement with the country to create a task force "with the specific objective of taking the measures necessary to improve execution."[66] The main bottlenecks identified, consistent with OVE's observations

65 There is a negative relationship between the size of the loans and the percentage that goes to administrative expenses. The transportation and water and sanitation sectors are atypical, however, as administrative costs represent a very high percentage of overall project costs (Annex, Figure I.26); this is associated with the use of ECATEFs.

66 Document GN-2769, IDB Country Strategy with Paraguay, Annex VI.

in previous CPEs, were as follows: the legislative ratification process; the country's budget processes; the need to improve execution processes by simplifying and automating processes; the training and use of management companies; the Bank's bidding requirements (bidding documents); and the need for a government center to ensure effective monitoring of key investments. The Bank acted on all these issues, but it is still too early to judge its effectiveness. One of the most notable Bank actions was technical cooperation operation PR-T1163, Program to Improve Project Execution, which was approved in 2014. This operation conducted a diagnostic assessment of the main bottlenecks to project execution following legislative ratification and proposed a number of solutions (see the table in the Annex that summarizes this technical cooperation operation).

2.16 However, nothing could be done with respect to the main problem, which concerns the legislative ratification process for projects, an issue that affects all multilateral institutions. Paraguay is one of eight countries working with the Bank that require legislative ratification for projects financed by multilateral institutions, and of those eight it is the one in which the process takes longest.[67] The lengthy ratification process creates a bias in favor of traditional infrastructure projects: Bank projects for other sectors —including the social sector, public management, and productive development— took almost 32% longer to obtain legislative ratification following approval (480 days versus 365 days). The same problem is seen in other countries requiring ratification, although in Paraguay it is worse and growing more so, compared with those other countries.

2.17 The lengthy ratification process has important operational implications for the Bank and other multilateral institutions. Firstly, legislative ratification significantly delays the launch of Bank operations, resulting in costs to both parties. Compared with the Bank average, projects take 424 days longer on average to reach eligibility in Paraguay, and 77% of this is the time taken for them to enter into effect. There is no significant difference in terms of execution times between Paraguay and the rest of the Bank once operations have entered into effect. Given that projects take just under two years (616 days) on average to reach eligibility, their designs or cost estimates frequently become outdated, and in some cases the political window of opportunity for reform has closed. All of this leads to higher numbers of

67 On average, it takes 441 days from the date of signature to obtain ratification in Paraguay, compared with 347 days in Costa Rica, followed by the Dominican Republic (263), El Salvador (131), Honduras (99), Bolivia (65), Nicaragua (47), and Haiti (42). See Table I.11 in the Annex for further details.

project cancellations or modifications.[68] The political economy of ratification also fosters a logic of inertia and a bias in favor of infrastructure, as noted in the previous CPE.

2.18 Another consequence of the lengthy ratification process has been the tendency to reduce the proportion of technical cooperation operations executed by the government. Since 2003, technical cooperation agreements have also required legislative ratification. Between 2000 and 2003, 54% of these agreements were executed by the government, while between 2014 and 2017 the figure was only 7%. Although there has been a general trend toward greater execution by the IDB in recent years,[69] this was particularly marked in the case of Paraguay, where all of the technical cooperation operations in 2017 were executed by the IDB. This, in turn, creates issues for the Bank, which is not set up to be an executing agency. It produces a growing burden of transaction costs associated with implementation of the technical cooperation agreements, even before taking into account the diversion of support and supervision resources away from loans and into technical cooperation operations.

2.19 Prior to the last period, the Project Preparation and Execution Facility (PROPEF) was the tool used most frequently by the Bank and the country to manage problems deriving from the lengthy legislative ratification period. The PROPEF, which still exists but is no longer used, facilitated continuity and helped advance investments for loans.[70] The instrument was used to cover financial gaps relating to the launch of projects when these had not yet been ratified and/or the borrower had not yet fulfilled conditions precedent to first disbursement. From 2000 —when the PROPEF was created— to 2013, Paraguay was the country that used this resource most frequently.[71] However, while use of the PROPEF was justified, it was not without cost to the country. In contrast to contingent technical cooperation

68 Delays in approval have led to a certain obsolescence in project design. For example, a number of activities that were to be supported by the loan are financed by FONACIDE, such as the police information system. This has necessitated a reformulation of the component with a view to increasing the emphasis on interconnecting the crime information systems of different departments and ministries, beginning with those of the Interior Ministry. Other important examples of the consequences of the lengthy ratification process were seen in the Early Childhood Development Program (PR-L1051) and the Program to Support the Modernization of Banco Nacional de Fomento (PR-L1048), which suffered a loss of political interest. Both projects were ratified after changes in leadership and experienced many disbursement problems.

69 According to the audit report prepared by the Office of the Executive Auditor in April 2018, the number of technical cooperation operations executed by the Bank grew steadily between 2010 and 2017, from 43% to 75%.

70 The objectives of PROPEFs were to: "(i) strengthen the preparation of projects belonging to the Bank's operational program, and (ii) increase support for including activities that finance project launch prior to first disbursement, and establishment of a framework to facilitate institutional sustainability" (document GN-2085-2).

71 From 2009 onwards, more than 80% of PROPEF resources were channeled to Paraguay (IDB).

agreements, PROPEFs represent actual debt that the country acquires independently of project execution. This means that the country assumes all risks relating to cancellation or delays.[72] Moreover, the greater availability of resources (from either technical cooperation operations or bonds) further diminished interest in PROPEFs, as these were able to perform the same role to a considerable extent.

72 For example, the Program to Strengthen Customs Revenue Administration (PR-L1026/PR-L1052), which was canceled, and the Escuela Viva II Program (PR-L1017/PR-L1028), which suffered excessive delays.

03

Results

3.1 This section presents the findings of the evaluation of the effectiveness of IDB interventions, as well as, to the extent possible, their contribution to achieving the strategic objectives established in the country strategy. The evaluation faced several limitations. Firstly, strategy evaluability is low as there were no preestablished targets for the selected indicators, and the latter were also defined in a very general way, limiting the ability to demonstrate results from the Bank's actions. Secondly, as a result of slow program execution, none of the investment projects designed under the 2014-2018 strategy have been completed.[73] For those that are underway, the percentage of funds disbursed is generally low, meaning that results have yet to be seen. Accordingly, the results discussed in this section are not necessarily aligned with the current strategy, but rather with the previously approved active portfolio.[74]

3.2 In general, analysis of the indicators attached to the country strategy objectives suggests progress in all of the areas in which the Bank is active, although these results cannot be directly attributed to the IDB program (see indicators in the Annex). The indicators are very general, and the evidence points to a strong correlation between the generally positive results and economic growth in the country. Additionally, compared with both budget funding and other alternative sources of finance, the IDB Group contributed a relatively small and decreasing proportion of available funding in Paraguay. Lastly, Paraguay's relative stability weakened the possibility of attributing a dominant role in policy reforms to the IDB.

3.3 A distinctive aspect of the portfolio in Paraguay was the low contribution of Bank projects to the country's institutional strengthening needs, both at the central level (projects for modernization of the State) and in terms of individual institutional strengthening components in each of the sector projects. The country strategy did not set any institutional development indicators. Despite the fact that the Bank proposed different targets for institutional support in practically all of the sectors, its efforts were disjointed and not guided by a holistic vision of the problems. With the exception of the transportation sector, where important advances were made in institutional strengthening, due mainly to a more comprehensive approach, progress in the other sectors was limited. These institutional development components generally experienced the greatest problems in

73 Of the projects approved during the strategy period, the only one to be completed was the Public Investment Management Program (PR-L1101), which was a policy-based loan.

74 The analysis presented in this section is based on sector studies, which are available upon request. The indicators in the results matrices are all presented in the Annex, together with the indicators for the country strategy objectives.

execution, further limiting their impact. Average disbursement rates for institutional capacity components in loans were 9%, compared with 31% for the central components of the loans. The figures for infrastructure projects were 2% and 12%, respectively.[75]

A. Sector analysis

1. Transportation

3.4 The country strategy had two development objectives in the transportation sector: (i) to improve transportation infrastructure; and (ii) to improve the level of road safety. To this end, the IDB program continued to support the three lines of action established in earlier years: improvement of the main highway corridors, the rural roads program, and modernization of metropolitan transportation. In the area of transportation, the program constituted a substantive part of the relationship with the country and was the most active area of intervention in the portfolio. A total of five investment loans were approved for US$517 million, accounting for approximately 25% of the total number of loan operations approved and 40% of the total amount. If fast-disbursing operations (PBLs) are excluded, this latter figure rises to 58%. Road investments increased considerably during the strategy period, and the Bank has performed a key role in the sector, contributing to the development and updating of the Master Plan, the Road Safety Plan, and the Logistics Development Plan, while also financing flagship projects included in the country's Investment Plan.[76]

3.5 The Bank's contribution was limited by significant delays. Disbursement levels were highest in the line of action concerning integration corridors and road rehabilitation and maintenance,[77] although there were also significant delays associated with ratification.[78] Disbursements from the portfolio relating to the improvement and conservation of rural roads were just

75 Based on an analysis of the investment categories, including 14 sovereign guaranteed investment loans approved between 2010 and 2018 (five in the infrastructure sectors), with disbursements as of August 2018.

76 The growth in investment in MOPC works has been highly significant as a percentage of GDP, reaching historic highs during the country strategy period. More significant still, between 2014 and 2015 tenders were invited for US$3.166 billion in works, representing a historic record and totaling more than all tenders over the previous 15 years. This amount was surpassed during the 2016-2018 period, when tenders were anticipated for works totaling US$4.66 billion.

77 In total, US$63.6 million were disbursed under Phase II of the Program for Paving of Integration Corridors and Road Rehabilitation and Maintenance (PR-L1075)—more than half of the total disbursed portfolio (51%)—as well as US$16.0 million under the San Juan Nepomuceno-Route 6 Junction Segment Improvement Project (PR-L1080).

78 Substantial delays have been experienced under PR-L1075, in large part due to ratification delays that grew to 489 days and led to the project being placed on "alert" status for the first few years.

US$50.9 million over the period. Of that amount, US$33.7 million corresponded to the National Rural Roads Program - Second Stage, Phase II (PR-L1019), approved in 2009,[79] and US$15.2 million to initial activities under the Rural Road Improvement Program (PR-L1084). Lastly, problems have been most acute in the project Downtown Redevelopment, Modernization of Metropolitan Public Transport, and Government Offices, which has required multiple adjustments and updates and is under review by the IDB's Independent Consultation and Investigation Mechanism (concerning construction of the Metrobus system in the Asunción area).

3.6 Despite the delays, the Bank's ongoing work with the country in the sector seems to have contributed to significant achievements consistent with the strategic objectives set out in the country strategy. This ongoing work has facilitated the incorporation of lessons learned. Given that the country has been adopting higher standards as it has grown, the Bank has also been flexible in terms of adjusting project standards. At the output level, the Bank has contributed to improvements in transportation infrastructure, with the projects facilitating the rehabilitation of 962 kilometers of the country's main highways (more than 100% of the target) and supporting the development of a maintenance management system covering 1,245 kilometers. Similarly, 1,570 kilometers of rural roads have been rehabilitated (approximately 60% of the target) together with 1,420 meters of concrete bridges replacing wooden structures, thus meeting the target.[80] In the area of institutional development, the transportation sector is possibly the area in which the Bank's achievements have been greatest. Through its actions, the Bank has helped to develop the MOPC's capabilities for sector planning and management and has also acted as an essential catalyst for developing the Ministry's socioenvironmental capacity. In addition, it has helped to improve road safety and mainstream gender considerations into road maintenance work. In contrast, the Metrobus project has faced many challenges, including design issues and problems of public perception, and it has not yet achieved the expected results.

2. Water and sanitation

3.7 In the water and sanitation sector, the country strategy sought to "increase the coverage of water and sewage (including wastewater treatment) services in the Asunción Metropolitan Area and in rural areas." The IDB's support for the water and sanitation sector in Paraguay is long-standing and highly

79 In addition, US$26 million had been disbursed prior to the period under analysis.

80 In terms of road safety, the Bank provided support for the inspection of 90% of paved roads, the 2008 Road Safety Plan, studies for the design and approval of the National Road Safety and Transportation Law, road education manuals, the creation of the National Road Safety Council, and the organization of road safety weeks.

relevant.[81] During the period, the Bank continued its work with the National Environmental Sanitation Service (SENASA) in rural areas, although it also supported operations for urban areas that fell outside the objectives of the country strategy (such as water distribution systems in the Chaco region and water and sanitation works in midsized cities, approved prior to 2014), as well as sanitation works in the Asunción Metropolitan Area.[82] Lastly, the Bank supported institutional strengthening actions, mainly through technical assistance operations and loans (particularly those executed by the Water and Sanitation Division [DAPSAN]).

3.8 Most results were achieved under the rural water program with SENASA, which the Bank has been supporting for years. In addition, the Bank has been successful in working with other donors on water and sanitation issues. The second phase is meeting targets and outcomes relating to increased water and sanitation service coverage in rural and indigenous communities (as of June 2018, 260 of the 266 potable water systems and 22,170 of the 23,200 individual basic sanitation solutions planned for this year had been built) and the installation of solid waste management systems in rural communities (nine of the 10 systems planned for 2018). However, the technical design specifications for water and sanitation systems have not yet been updated. Most of the Bank-financed systems are still in operation, but long-term sustainability of the results will depend on a rate policy that ensures that operating costs are covered (including electricity and chlorine) and on technical and institutional strengthening of the water and sanitation boards that are responsible for operating the systems.

3.9 The majority of water and sanitation funding was channeled into the urban pillar,[83] but these investments are still at an initial stage. Seven years after its approval, the execution rate for the Water and Sanitation Program for the Chaco Region and Intermediate Cities in the Eastern Region of Paraguay (PR-L1060) is 34%. The post-approval delays mean that it is still too early to say whether all the expected results will be achieved. To date, the program

81 The Bank has traditionally worked with the urban water and sanitation company (Empresa de Servicios Sanitarios del Paraguay S.A. (ESSAP), formerly CORPOSANA). Since the end of the 1990s, the Bank has entered into a partnership with SENASA to support the construction of rural systems and the training of the sanitation boards that operate them.

82 The country has requested that the Bank approve a public-private partnership for the water and sanitation and sewerage system in the Ciudad del Este Metropolitan Area. The introduction of private operators to manage the new water systems could help to resolve a number of ESSAP's weaknesses. Given the water and sanitation company's technical and financial weaknesses, the introduction of a new operator with international experience could help to improve the management of new investment. Nonetheless, given the weaknesses in sector oversight and regulation and the lack of a coherent rate policy, it is unclear that the conditions necessary for a public-private partnership are present.

83 In terms of approved amounts (70%) and numbers of operations (four).

has supported the construction of 10 water distribution networks, 111 kilometers of distribution lines in the Chaco region (out of 197 kilometers by the end of the project), and 9.5 kilometers of network in the community of Pesempo (out of an anticipated 223.15 kilometers).[84] In terms of institutional components, four master plans have been prepared to date. The Comprehensive Sanitation Program for the Bay and Metropolitan Area of Asunción (PR-L1029) is also in the initial stages of execution, but the largest contracts have already been awarded.[85] In terms of results,[86] as of 2017 two water quality and aquatic biota campaigns had been carried out to monitor the water bodies affected by the program (out of an expected 10). In the case of the other outputs, no results were expected at this point.

3.10 The Bank's program would have been even more relevant and effective if the institutional support components had contributed in a more unified manner to strengthening the country's planning, management, and regulation capacities in the water and sanitation sector. Institutional interventions were carried out through a number of technical cooperation operations addressing various highly relevant issues, in addition to institutional support for DAPSAN and SENASA under the operations. The technical cooperation operations addressed individually relevant issues such as the sustainable use of water resources, management of losses at the water company, and the implementation of a water usage model using social art interventions. The loans were supported with institutional strengthening components for the various relevant entities in the system. However, from a more holistic perspective, significant progress was not made during the period on Paraguay's key institutional challenges in the sector, such as fragmentation and formulation of a rate policy that would guarantee sustainability.

3. Energy

3.11 The country strategy objectives in the sector were to: (1) ensure the sustainability of power supply for the public; and (2) ensure the same for the productive sector, including boosting the domestic production of biofuels. The Bank's portfolio of sector operations remained small, and the focus was on executing operations approved during the previous period, which responded to the

84 The main sewerage network in San Juan Bautista is still under construction (27.6 km out of 200), while tenders have not yet been invited for construction of the condominial networks.

85 These three contracts represent approximately US$78 million, or 70% of the loan.

86 The pace of execution has been fastest in the project administration component (25%), which is explained by project delays, and the works investment components (12.3% for the Bahía de Asunción collector sewers and 8.2% for the San Lorenzo sanitation works).

first strategic objective.[87] The multiphase program to support Paraguay's transmission system was approved in 2006 with the objective of increasing the security of supply and the efficient exploitation of available renewable electricity generation. The first phase (PR-L1010) was approved in 2006 for US$69.5 million; it was mainly executed during the previous strategy period and was completed in 2014. The second phase (PR-L1058) was approved in 2012 for US$50 million (plus US$100 million in counterpart funding from the European Investment Bank, US$50 million from CAF, and US$66.84 million from the National Electricity Administration (ANDE). This project is still in execution. The Bank also approved a technical cooperation agreement with the purpose of financing studies of the operations currently being evaluated. A technical cooperation operation is also under execution to support the Sustainable Energy for Development Program (PR-T1233), in the amount of US$350,000.[88]

3.12 Although execution of the second phase is only expected in 2019, it seems likely that the expected results will be achieved. The Bank's actions are contributing to the country strategy objective of ensuring the sustainability of power supply for the public and the productive sector, albeit on a small scale. Once the traditional congressional ratification delays were overcome, ANDE made satisfactory progress in executing the program.[89] By the end of 2017, 650,000 meters had been procured as planned, as well as the IT equipment required to monitor the mitigation of environmental liabilities. The expansion of the two substations had likewise been completed, and more than 50% of the transmission lines had been executed. At the same time, technical losses in the network continued to decline and are estimated at 25.4% in 2017. With the launch of the new transmission line, it is expected that the program target of 23.6% will be achieved. In energy, the IDB did not make a significant contribution to institutional development in the sector.

4. Productive development

3.13 The country strategy objectives in productive development were to: (1) enhance the productivity and competitiveness of firms; (2) guarantee the legal certainty of land ownership; and (3) increase

87 The IDB's lower participation in financing electricity sector investments has been further affected by the increase in bond financing. In 2016, investments were financed mainly by ANDE (37.6%), bonds (20%), CAF (14%), and the World Bank (13%), while the IDB financed 3.8% (ANDE, 2016 Annual Report).

88 This technical cooperation operation will finance the activities and technical, economic, financial, environmental, and social studies required to design the first phase of the investment plan to rehabilitate and modernize the Acaray hydroelectric plant.

89 The main execution difficulties that have arisen are due to a failure to comply with a contractual clause stipulating that ANDE implement separate accounting for the power generation, transmission, and distribution businesses before initiating disbursement of the final tranche of the operation (50%).

the supply of agricultural public goods and services. The Bank's program of action in the area of productive development consisted of fostering the conditions necessary to improve the productivity and competitiveness of firms, create jobs (particularly in production chains), and promote the economic participation of women. A total of four sovereign guaranteed investment loans (US$50 million) were approved under these lines,[90] as well as one PBL (US$200 million, still pending legislative ratification), 12 non-sovereign guaranteed investment loans (US$61.1 million), and three guarantees (US$84.8 million). In the case of IDB Invest, the 2014-2018 period saw the approval of 15 loans for four Paraguayan banks under the Trade Finance Facilitation Program and nine guarantees for two banks.[91]

3.14 Two sovereign guaranteed operations relating to the productive sector and approved prior to the strategy period were completed during the evaluation period. The Modernization of Agricultural Support Management Program (PAGRO), approved in 2006, sought for the first time to break the link between support and specific crops, as well as to transfer responsibility for the choice of technology to producers. This program is aligned with the objective of increasing the delivery of agricultural public goods and services, and a total of 44,482 farmers benefited from it—higher than the expected figure of 33,400. Preliminary findings from the impact evaluation indicate a significant increase in beneficiary productivity.[92] However, sustainability of the program is at risk given that farmers are often unable to get access to these technologies using their own resources. The other program (PR-L1018), the Program to Support Paraguayan Exports, was approved in 2007 and was aligned with the objective of improving the productivity and competitiveness of firms. It was successful in gradually achieving its objectives, although the planned execution period was exceeded. An initial evaluation of the instruments supported under the program (PR-L1018) suggests that these have had a positive and significant impact on the exports of companies using them, with a 19% gain over companies not participating in the program.[93] Nonetheless, the agency faces sustainability challenges. The Investment and Export Network (Rediex) —which is attached to the Ministry of Industry and Commerce and is responsible for supporting

90 No disbursements have been made under any of the sovereign guaranteed loans approved during the evaluation period.

91 Four technical cooperation operations were also approved (US$1.5 million).

92 The impact evaluation for the Modernization of Agricultural Support Management Program is still being finalized and has not yet been made public.

93 The evaluation is not yet publicly available but the findings are included in loan document PR-L1139.

investment and exports— suffered a 40% annual reduction in the 2018 fiscal year. An estimated 85% of its budget is financed by Bank loans, endangering long-term program sustainability.[94]

3.15 Five operations were carried out directly with the private sector, with an apparent bias in favor of large, sound borrowers. These projects included new investments by foreign shareholders with access to potential alternative financing. In some cases, the IDB Group took on operations that were already at an advanced stage of preparation and, therefore, it had relatively little influence over design elements. Now that the risks associated with the construction phase have passed and there is ample liquidity in the financial markets, a couple of these operations have become the subject of talks regarding early payment. In one case, the need for an action plan to address environmental challenges was a factor in the decision to prepay. Credit lines were also provided to financial intermediaries, but there is still no evidence that these have helped to expand access to finance.[95] The IDB Group also supported several emerging financial entities, a cooperative bank and a finance company that converted to a bank, actions that may be promoting greater competition in the country's financial sector.

3.16 IDB Invest continued to support an expansion in international trade through its Trade Finance Facilitation Program (TFFP). The TFFP aims to support bank access to international markets for international trade finance. This, in turn, is intended to increase available sources of financing for companies engaged in importing and exporting in the region, supporting their internationalization and deepening the regional integration process. In Paraguay, the predominant form of support is to small banks targeting SMEs. Most of the banks that have TFFP agreements do not use them but benefit from the international visibility and the possibility of access during times of volatility.

5. Financial sector

3.17 In terms of the financial sector, the country strategy had the following objectives: (1) to promote investment financing through the financial system, and (2) to foster greater financial inclusion. The Bank has traditionally been a key actor in the financial sector: it was involved in creating the Financial Development Agency

94 Subsequent to this loan, the Bank provided two additional loans to Rediex (PR-L1069 in 2013 and PR-L1139 in 2016).

95 The projections for expansion in the target portfolios that were run during the design phase of the operations were based on the rapid growth seen in previous years. Given events that the country is facing, such as volatility in commodity prices, the weak performance of Paraguay's main trading partners, and climate-related conditions, the Central Bank has issued recommendations for banks to proceed with greater caution and to diversify their portfolios, which means that they are not reaching their portfolio targets for MSMEs.

(AFD) in 2006,[96] the country's only second-tier bank, with which the Bank still has operations. In terms of the portfolio analyzed, including legacy operations from the previous strategy that were executed predominantly during the evaluation period, the Bank's activity included six loans for a total of almost US$150 million and three technical cooperation agreements. In 2011, a third operation was approved under the Conditional Credit Line for Investment Projects (CCLIP) for the AFD (PR-L1062),[97] as well as three new loans, focused this time on supporting financing to specific sectors: SMEs, the housing sector, and small farmers. Of these, only the first—approved in 2014 to support SMEs—has begun execution.

3.18 The projects to strengthen and expand second-tier banking fulfilled their objectives to a large extent, contributing to the two strategic objectives in the sector. Execution of PR-L1062 was satisfactory: the funds channeled through the AFD ensured that the average term of the loans financed under the program exceeded 13 years, six times more than the system average and significantly above the original target of 10 years. In addition, cofinancing equivalent to 5% of the total contributed by the AFD was obtained on identical terms from the international financial institutions involved. Funding through the AFD was particularly crucial for the housing sector, in which almost all of the credit made available by the international financial institutions for this purpose depended on the funds provided by the AFD. In terms of institutional strengthening of the AFD, technical cooperation PR-T1194 financed the preparation of a report that the agency will use as the basis for presenting a reform bill to the legislature.

3.19 Achievements were limited under the other two sovereign guaranteed programs that closed during the period. The Program to Support the Modernization of Banco Nacional de Fomento (PR L1048), approved in 2011, failed to meet its objective of extending financing to sectors not served by private banks. Most of the progress made under this loan was driven by the bank leadership named in 2017, when the program was already drawing to a close. In general, project execution was slow, and less than half of the anticipated amount was disbursed. The Program for Institutional Strengthening of the National Credit Union Administration (INCOOP) (PR-L1011), the oldest in the

96 Since its creation, the AFD has been consolidating and expanding its position in the market. It currently has several types of instruments for different types of financing needs, from SME loans to investment, housing, or education projects, among other things. The institution also managed to increase its resources through international loans and bond issues on the domestic market, in addition to securing 7% of the FONACIDE resources.

97 Of the US$130 million that the IDB approved for the AFD between 2006 and 2013, US$100 million corresponded to the first two operations under the Conditional Credit Line for Investment Projects, approved in 2008 and 2009, respectively.

financial sector portfolio, was the most problematic. Execution of the project was troubled, and its final date had to be extended by four years. Even after this, it was closed in 2017 having disbursed less than 60% of the original amount. Some progress was made under several of the project's components—mainly with respect to the regulatory framework, implementation of the credit risk clearinghouse for the credit union sector, and the provision of new IT equipment—but the critical improvements sought in areas like deposit security, for example, were not achieved. In addition, the sustainability of these advances is subject to technological obsolescence risks.

3.20 There were challenges in executing support for the private sector, including IDB Group public sector action to complement IDB Invest operations. The IDB Group's public sector window worked mainly with the AFD, which perceived certain private sector initiatives by the IDB Group as competition. For example, efforts to generate local currency financing with the Social Security Institute (IPS) to be used in IDB Invest operations was perceived as a form of competition that would deprive it of one of its traditional sources of financing. IDB Invest also structured and incurred due diligence costs for various projects with IPS financing, which produced a demonstration effect but ended up being financed by private banks (individually or as consortia) that offered lower interest rates and eliminated contractual restrictions such as environmental safeguards. Some of these banks were IDB Group clients and had access to credit lines, particularly for foreign trade.

6. Public management

3.21 The country strategy had three strategic objectives under the public management pillar: (1) consolidating fiscal sustainability; (2) reducing levels of violence and crime; and (3) improving the effectiveness, transparency, and integrity of public entities. As in previous periods, the areas of action remained focused on four main topics: (1) support for tax policy and administration issues; (2) improving security and strengthening justice; (3) public sector strengthening, particularly in the areas of human resources and public investment; and (4) support for statistical capabilities and the census. In addition to the strategy, however, a new area was added at the country's request: the Digital Agenda (see paragraph 2.10).

3.22 Bank action was divided between many projects and technical cooperation operations. The Bank has been providing support to all areas of the judicial system, from crime prevention to prison management. The oldest program is the Program to Strengthen the Justice System (PR0146, approved in 2006), which has been accompanied by several technical cooperation agreements. There is also an Integrated Citizen Security Management Program (PR-L1077, 2014), which has not yet begun executing, having only recently obtained legislative ratification; it is supported by technical cooperation operation PR-T1218 for the pilot program. In the area of public sector institutional strengthening, the Bank has also been supporting several initiatives. The most significant is the initaitive to strengthen the Civil Service Department (SFP) and the creation of a civil service career system (PR-L1008).[98] The Bank has also supported Paraguay's public investment system since its creation, and this was particularly the case during the period under analysis, with technical cooperation agreements and the policy-based loan (PR-L1101). Statistics and censuses is an area of long-standing Bank support.[99] Lastly, in terms of tax policy and administration, the Bank provided continuity for the Fiscal Management Strengthening and Modernization Program (PROFOMAF) I by approving PROFOMAF II. This sought, firstly, to codify tax regulations and strengthen the Department of Taxation (SET), and secondly, to further develop the financial administration system (SIAF) and its integration with other systems, with a view to creating an integrated, interconnected system covering the entire public administration, the Integrated Administration System for State Resources (SIARE).[100]

3.23 In general, the Bank's support followed a similar pattern to that seen in previous periods, i.e., a portfolio of disconnected interventions targeted to areas important to certain government institutions. This support was typically provided through technical cooperation agreements that financed specialized consultants. Nonetheless, the Bank has been present in the most important sectors, and its support, particularly through technical cooperation operations providing specific expertise, has been highly valued by the client. The loans (civil service, PROFOMAF, census) generally finance specific activities (for example, census workers for the population census, the SIAF). The only one to attempt comprehensive public sector modernization was the loan supporting the SFP's efforts to create an efficient, meritocratic civil service. In terms of results, the civil service project is the most noteworthy, as it supported the successful implementation of a management system across much of the government. However, its sustainability is threatened by an excessive dependence on funding from bilateral and multilateral development partners.

98 This was supplemented by specific technical assistance projects to strengthen different government institutions, generally in the area of human resource training.

99 The Bank supported the 2002 census (PR0130), the 2011 economic census (PR-L1021), and the 2012 population census (PR-T1116, PR-L1049).

100 In addition to PROFOMAF, the Bank has provided targeted support in the areas of macrofiscal policy management and debt management (PR-T1238 and PR-T1256) that has been highly valued by the client.

3.24 In terms of results, Bank operations, particularly the civil service loan, were key to consolidating the SFP and implementing a human resources management system in many public institutions. Even so, the sustainability of the operation and its rollout to the entire public sector depend on the availability of budgetary resources. Policy conditions have been met under the Public Investment Management PBL (PR-L1101),[101] which has also been associated with important technical cooperation operations to support strengthening of the SNIP. Some of the achievements of the work with the SNIP include staff training in project management methods (such as the PM4R) and the development of methodologies. In fact, the Bank has played a key role from the outset in developing the country's public investment system. Nonetheless, although the rate of public investment execution has increased, the weak legal and strategic framework underlying the SNIP has limited its effectiveness. In particular, there is a need to create a legal and institutional framework that addresses the investment cycle comprehensively, from the identification of needs through to their prioritization, implementation, and sustainability. The effectiveness of support under PROFOMAF II for Paraguay's tax management was insignificant. With the abandonment of tax actions midway and the low amount of funds disbursed, "it cannot be expected that these actions will have had a quantitative impact that is distinguishable from the noise that accompanies the normal management of the tax system."[102]

7. Crosscutting area

3.25 Based on the assumption that the World Bank would be the main actor in the social sector, the Bank placed very little emphasis on this sector in the country strategy, concentrating on executing projects approved in the previous period. There were three loans in the legacy portfolio: PR-L1017 (Escuela Viva II Program), PR-L1051 (Early Childhood Development Program), and PR-L1066 (Program to Support Job Placement). One loan was also approved in the education sector (PR-L1097, recently ratified) and another in housing (PR-L1082), a sector that the Bank had not worked in in Paraguay for many years and which did not appear in the strategy. Eleven technical cooperation operations were also approved for the social sector.

3.26 The results of these programs were mixed, and in the case of the oldest projects, significant execution difficulties had to be overcome. The execution problems experienced in the health

101 In addition to maintaining a macroeconomic context consistent with program objectives, the Paraguayan government committed to 17 policy actions under the operation, including two legislative measures and 15 administrative ones. The government achieved satisfactory compliance with all of the general and special conditions precedent for the two disbursements.

102 IDB (2017), Annex 9.

and education programs were different. The health program was approved by a government that believed in a health model emphasizing primary care and that was interested in expanding this to include early childhood development services. The subsequent government, however, promoted a very different model, focused more on expanding the hospital network, and did not make sufficient room in the budget to execute the loan. This diminished interest, combined with the lack of institutional capacity at the Ministry of Health, led to a project that has so far yielded few results. In the case of the education program, which was a continuation of existing Bank work with the country, problems were experienced due to the loan modality used (a performance-driven loan).[103] The loan achieved many of its objectives, with the exception of the Ministry of Education building, planned for the last tranche. The Bank and the government agreed that the building would be constructed as part of the government offices center envisaged under loan PR-L1044. Lastly, the labor markets loan exceeded its targets for efficiency and training, although problems exogenous to the project were experienced, such as the government's decision to separate the Ministry of Justice from the Ministry of Work and Employment, which led to cancellation of the infrastructure component that had originally been planned. The housing sector loan[104] is being implemented and is expected to meet its objectives.

3.27 Technical cooperation operations approved under the strategy achieved positive results, and fulfilled, in particular, the objective of leveraging FONACIDE resources. PR-T1196 financed the design of the Ciudad Mujer program in Paraguay, following the Bank's experience in other countries. The first center, which was opened at the beginning of 2018, was financed with FONACIDE resources. Although it is too early to evaluate its effectiveness, the Bank's positive experience in other countries and the first few months of the center's operations in Paraguay suggest that the program can meet its objectives. Another example is the scholarship program (see paragraph 2.16). In addition, in the area of education, the two pilot Tikichuela programs in mathematics and science[105] had a very positive impact on student performance. Both programs are being expanded using government and European Union funding. Lastly, PR-T1158 generated instruments to implement a

103 Performance-driven loans were designed to emphasize the attainment of planned results, disbursing once these were achieved and verified. In the case of Paraguay, the implementation problems associated with this loan modality were related to, among other things, restrictions on the transfer of funds disbursed to the executing agency once the project tranche had already been implemented.

104 The Ministry of Housing and the government leadership promoted PR-L1153 heavily, leading to its ratification in record time.

105 An impact evaluation of the program shows that children in schools in the treatment group scored an average of 0.84 standard deviations higher on the final tests.

model of the comprehensive integrated networks for obstetric and neonatal care, and implementation was expanded to six health regions in the country by the Ministry of Health using funds from loan PR-L1051.

04

Conclusions and Recommendations

4.1 Paraguay is experiencing a very positive time in its economic history. Nevertheless, its growth model based on agricultural exports and macroeconomic stability is showing signs of depletion. Economic growth has facilitated significant social progress and advances in modernizing the country, but meager progress in modernizing certain areas of government, including the administration of justice, stands in the way of a more sustainable model of development. Paraguay's main challenge is to increase its rate of economic growth while at the same time distributing wealth more equitably. Even with more resources available, the country faces the challenge of prioritizing its needs and executing funding in an efficient manner.

4.2 For the Bank, this new growth phase in Paraguay brings with it significant changes in financial relevance and strategic positioning. The evaluation period saw the consolidation of a series of trends that affected the Bank's relationship with the country. Firstly, CAF has begun to establish itself as an important financial partner for development, with growing levels of approvals. Although CAF financing is more expensive than that of the IDB, its model of intervention—a portfolio that is concentrated in certain sectors and makes extensive use of country systems—would appear better tailored to the government's needs in this economic context. Secondly, Bank approvals account for an ever-smaller proportion of the government's needs. Since 2013, the country has issued bonds on the international markets totaling 60% more than IDB approvals. As a result, the IDB's share of multilateral approvals plus bond issues dropped from 70% in the 2000-2008 period to less than 30% in 2014-2017.

4.3 Adding to this has been a shift in the country's needs, to which the Bank has attempted to adapt. After 15 years of sustained growth, the client's needs entail a much higher level of complexity. This phenomenon is similar to the experience that the Bank has had with other clients making the transition to upper-middle-income economies in which technical value added and knowledge become essential. In the case of Paraguay, a recent example is the emphasis tha the country has placed on its Digital Agenda. Looking forward, the Bank should be prepared to engage with a more sophisticated client that values the specific knowledge and expertise associated with the operations more than the financial transfers themselves.

4.4 Along these lines, the Bank deepened its efforts to improve the execution of operations and lower transaction costs. Several technical cooperation operations were aimed at financing diagnostic assessments and analyses of execution problems, particularly following legislative ratification of the corresponding loans. While some progress was made (e.g.

exempting the counterpart contribution from the VAT), other changes are still too recent to be evaluated (e.g. the mega execution unit at the MOPC).

4.5 In general terms, delays in ratification continue to explain a significant part of overall delays, which continue to grow. Delays in ratifying projects mean that by the time they become effective, they are outdated in several respects. The diagnostic assessments upon which the models of intervention were based, the cost estimates, and even the degree of political will may have changed, as was frequently the case. Accordingly, the ratification process remains the main bottleneck to project implementation in Paraguay, as highlighted by OVE in past CPEs.

4.6 In terms of results, progress can be seen in basically all of the Bank's areas of action, although this cannot be directly attributed to the projects. The project results achieved during the period under analysis have been mixed, but there is evidence that the most significant achievements were in those sectors in which the Bank has long-standing relationships with the country. Although inertia in the sectors poses its own challenges, it offers a number of advantages. There is a tendency to incorporate lessons learned into the subsequent phases of projects. Also, as mentioned in previous CPEs, even though it takes a long time to execute Bank projects (particularly in infrastructure), they do, ultimately, get implemented. And the ongoing relationship with the execution unit helps get results. In the social sector, the Bank was successful in leveraging the country's resources for projects in a variety of areas. With respect to the private sector, there were instances in which there was a failure to coordinate with the public sector (see paragraph 3.20). With regard to technical cooperation operations, funding declined over the period and was largely used for operations support. There have, generally, been fewer resources for knowledge generation when compared with the average for the Bank.

4.7 In general, however, the Bank continues to experience the same problem identified in earlier periods: it has been unable to work with the country to strengthen governance, and in particular it has not been able to create sufficient institutional capacity in the sectors in which it is active. This not only limits the project impact attained by the Bank as a development institution but also endangers the sustainability of its results. The most successful example in Paraguay has been in the transportation sector, where there has been significant progress. But this also reflects the *ex ante* degree of institutional development in the sector, as well as the high level of Bank involvement as the main multilateral institution working in transportation. In the other sectors, where institutional development is lower still and more fragmented (e.g. the water and sanitation sector), achievements have been significant but do not form part of a more comprehensive strategy of institutional development.

4.8 Based on the findings of this evaluation, OVE recommends that the Bank:

1. **Redefine the Bank's model of intervention in Paraguay, placing emphasis on a more comprehensive vision of institutional development and targeting sectors where the Bank has a comparative advantage.** The Bank should continue its proactive dialogue with the client to identify emerging needs in this new stage of Paraguay's development. The Bank's institutional support should be more comprehensive and cohesive, preventing a piecemeal approach in institutional strengthening components. In the past, these components have often been difficult to implement. Moreover, as opportunities arise, a strategic vision of the country's institutions will be particularly important for framing the new issues and agendas for the Bank's work (e.g. the Digital Agenda). Independent of these considerations, the Bank should be prepared to reduce fragmentation in its portfolio.

2. **Be more strategic in the use of technical cooperation, in order to support this new model of investment at the Bank, which will include more complex operations requiring greater knowledge and expertise.** At the moment, a large contingent of technical cooperation operations are used to implement Bank projects. Although this adds value by expediting the execution of projects, it limits the pool of resources available for investing in the knowledge and expertise needed to support the new types of demand coming from the country. Accordingly, Management should continue to identify instruments that are easier to implement and that free up resources so the Bank can also support more complex operations.

3. **Continue working with the country to simplify the ratification and budget processes.** This is the fourth CPE to identify legislative ratification as a bottleneck for the Bank's work in Paraguay. In contrast to previous CPEs, the country has made use in this evaluation period of international bond issues, which are handled differently from multilateral loans. This introduces the possibility of resuming work with the country to simplify legislative ratification processes, integrating the requirements for Bank loans with those of other comparable external borrowing instruments (e.g. international bonds).

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