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**EL SALVADOR**

**IDB GROUP COUNTRY STRATEGY  
2021-2024**

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## ABBREVIATIONS

ANDA	Administración Nacional de Acueductos y Alcantarillado [National Water and Sewer Authority]
BANDESAL	Banco de Desarrollo de El Salvador [Development Bank of El Salvador]
BCR	Central Reserve Bank of El Salvador
CABEI	Central American Bank for Economic Integration
CCLIP	Conditional credit line for investment projects
CCR	Corte de Cuentas de la República [State Audit Office]
CDC	Country Development Challenges
CIMA	Centro de Información para la Mejora de los Aprendizajes [IDB education statistics portal]
CONAMYPE	Comisión Nacional de la Micro y Pequeña Empresa [National micro and small enterprise commission]
COVID-19	Coronavirus disease caused by the SARS-CoV-2 virus, first detected in 2019.
DCGER	Dirección de Adaptación al Cambio Climático y Gestión Estratégica del Riesgo [Climate Change and Strategic Risk Management Department]
DGICP	Dirección General de Inversión y Crédito Público [Public Debt Bureau]
DGII	Dirección General de Impuestos Internos [Internal Revenue Office]
ECOSF	Community family health teams
EHPM	Multipurpose Household Survey
FOP	Fideicomiso de Obligaciones Previsionales [Pension Obligations Trust Fund]
FSV	Fondo Social para la Vivienda [Social Housing Fund]
GDP	Gross domestic product
ICTs	Information and communication technologies
IHME	Institute for Health Metrics and Evaluation
IMF	International Monetary Fund
ISDEMU	Instituto Salvadoreño para el Desarrollo de la Mujer [Salvadoran Institute for Women's Development]
ISM	Salud Mesoamérica Initiative
ISSS	Instituto Salvadoreño del Seguro Social [Salvadoran Social Security Institute]
MARN	Ministry of Agriculture and Natural Resources
MINSAL	Ministry of Health
MSMEs	Micro, small, and medium-sized enterprises
OVE	Office of Evaluation and Oversight
PNAPS	Plan Nacional de Agua Potable y Saneamiento [National Drinking Water and Sanitation Plan]
pp	Percentage point(s)
RUP	Registro Único de Participantes [Master registry of participants]
SAP	Sistema de Ahorro para Pensiones [Pension saving system]
SDL	Special Development Lending/Loan
SEM	Sistema Nacional de Emergencia [National Emergency System]
SETEPLAN	Technical and Planning Secretariat
SIETUR	Sistema de Información Estadístico de Turismo [Tourism statistics system]

SIGES	Sistema de Información para la Gestión Educativa [Education management information system]
SIMMOW	Sistema de Información de Morbi-Mortalidad [Morbidity/mortality information system]
SSF	Financial System Superintendency
UNAC	Unidad Normativa de Adquisiciones y Contrataciones de la Administración Pública [Government procurement unit]
WDI	World Development Indicators

## EXECUTIVE SUMMARY

<b>Context</b>	<p>El Salvador faces challenges that have hampered growth, poverty reduction, and the consolidation of the middle class. The obstacles the country faces to achieving higher levels of economic and social development are associated with factors including the state of the productive infrastructure, low levels of education and financial development, governance challenges, a relatively undiversified economy, and extreme vulnerability to natural disasters and climate change. Although the country has managed to reduce violence, poverty, and inequality, a large segment of the population remains in a vulnerable position. The COVID-19 pandemic has exacerbated these challenges and highlighted the country's low digital connectivity, poor quality housing, and lack of adequate social safety nets. The crisis has also intensified the country's fiscal fragility, which could undermine growth and its social stability. Against this backdrop, the scenario in the years ahead looks complex, necessitating a balancing of the response to short-term challenges stemming from the socioeconomic impacts of the crisis with improvements to governance and the business climate to revitalize medium- and long-term growth.</p>
<b>The IDB Group in El Salvador</b>	<p>The 2015-2019 strategy proposed three target areas: (i) strengthening of public finance; (ii) increasing the quality of spending on human capital; and (iii) improving logistics infrastructure. In response to the impact of COVID-19, at the authorities' request, the Bank approved an extension of the strategy's validity period until June 2021. As of December 2020, the IDB Group had approved US\$2,380,300,000, including US\$1.715 billion in 13 sovereign guaranteed operations (US\$665 million for investment projects, US\$800 million to support reforms, and US\$250 million in special development lending (SDL) emergency support). Additionally, 48 technical cooperation operations and grants for US\$14.8 million were approved. IDB Invest approved transactions totaling US\$640.1 million, and IDB Lab approved operations for US\$10.4 million.</p>
<b>Priority areas</b>	<p>The objective of the IDB Group's strategy with El Salvador for the period 2021-2024 is to help mitigate the impact of the crisis on the country's outlook so as to achieve more vigorous, inclusive, and sustainable growth over the medium term. To this end, the proposed approach seeks to respond to the country's immediate needs deriving from the health crisis and its social and economic impacts, while supporting the rekindling of economic growth in view of the changing context. It was agreed with the authorities that the IDB Group's operations would focus on three priorities: (i) fiscal sustainability and efficiency; (ii) reducing social vulnerability; and (iii) revitalizing and restructuring production. Considerations regarding the mainstreaming of gender equality and diversity, climate change, environmental sustainability and natural disasters, and institutional capacity and the rule of law will be evaluated during implementation.</p>
<b>Projected financial scenario</b>	<p>The Bank projects sovereign-guaranteed approvals totaling US\$1.3 billion over the 2021-2024 period, with a program of approximately US\$325 million per year. At the end of the strategy period, El Salvador's debt with the IDB could account for 50% of the country's debt with multilateral institutions, and 22% of its external debt.</p>

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<b>Preliminary implementation considerations</b>	The Bank will continue to provide technical assistance to support the dialogue on key reforms and achievement of the lending program and portfolio objectives. It will work to strengthen government agencies' budget, treasury management, accounting, external auditing, and information technology subsystems to enhance fiduciary oversight. Coordination within the IDB Group and with other donors will remain central to progress in the priority areas agreed upon with the authorities.
<b>Risks</b>	The principal risks derive from macroeconomic, fiscal, and institutional issues, the impact of natural disasters, along with implementation challenges, especially under the constraints caused by the pandemic. The speed of the economic recovery, the magnitude of the ongoing impacts of the pandemic on productivity and employment, changing perceptions of the country's political and institutional context, together with the occurrence of a natural disaster are elements that could impact the government's priorities and the development of activities in the areas addressed by the strategy.

## I. CONTEXT

- 1.1 On 11 March 2020, the World Health Organization (WHO) characterized COVID-19 as a pandemic. The measures countries initially put in place to slow the spread of the virus by restricting mobility had immediate economic and social impacts. The global nature of the situation and the fact that these measures were adopted simultaneously meant that, on top of the impact of domestic measures, emerging market economies have had to contend with the shock of reduced economic activity among their main trade partners, a slump in tourism flows, and worsening financing conditions. These factors point to a deeper recession than the one witnessed after the 2008 international financial crisis and a slower recovery of economic activity to pre-crisis levels. The disruptive effect of the pandemic could also lead to permanent changes in trade flows, global value chains, and movements of people, affecting the recovery and the medium-term growth of many economic sectors and world regions.
- 1.2 El Salvador's economy is small<sup>1</sup> and highly dependent on the economic performance of the United States and on remittances. It is relatively undiversified, being dominated by the tertiary sector (70% of GDP),<sup>2</sup> in which two thirds of jobs are informal.<sup>3</sup> The shock caused by COVID-19 could therefore undermine the achievements of the past decade. The obstacles to a rapid recovery are closely linked to the development challenges of a more structural nature that the country faces, stemming from a low level of investment and its historically weak growth, which have limited the population's economic opportunities and the possibility of a more durable reduction in social and fiscal vulnerability. In conjunction with external factors, these have led to outward migration by thousands of Salvadoran citizens, mainly to the United States.
- 1.3 **Progress and challenges going forward.** Prior to the crisis, rising real incomes, including remittances<sup>4</sup> and government transfers,<sup>5</sup> helped to bring about a significant reduction in poverty. Between 2000 and 2019, poverty decreased from 46.6% to 27.1%,<sup>6</sup> putting it on a level with the Latin American average. The adoption of policies and programs to raise the quality and expand the coverage of health care services made it possible to bring maternal mortality down from 57.4 to 26.4 deaths per 100,000 live births between 2009 and 2018 and infant mortality from 17.4 to 12.5 deaths per 1,000 live births over the same period. As regards public safety, the homicide rate fell from 103 per 100,000 population in 2015 to 36 per 100,000 population in 2019.<sup>7</sup>

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<sup>1</sup> El Salvador accounts for 10.6% of the Central America, Panama, and the Dominican Republic region's population and 7.5% of its GDP.

<sup>2</sup> Central Reserve Bank of El Salvador (BCR).

<sup>3</sup> Salvadoran Social Security Institute (ISSS) statistical yearbook and Multipurpose Household Survey (EHPM) 2019.

<sup>4</sup> Remittances account for 20.9% of GDP (2019) and 37% of recipient households' income.

<sup>5</sup> Social expenditure rose from 8.3% of GDP in 2002-2009 to 9.1% of GDP over the period 2010-2017.

<sup>6</sup> Estimates based on official data from the EHPM 2000-2019.

<sup>7</sup> Direct victimization rates also fell (from 18.9% in 2016 to 14% in 2018) as did the rate of reported robberies and theft (from 87.6 in 2014 to 74.8 in 2017), and the drop in the number of reports of extortion remained unchanged (the rate decreased by 69% between 2010 and 2017).

- 1.4 Nevertheless, this poverty reduction did not translate into the growth of a stable middle class, but was accompanied by a rising share of vulnerable people. Before COVID-19, two out of three Salvadorans were poor or remained at risk of falling into poverty as a result of a downturn in growth and/or declining remittances. As regards crime and public safety, although the headline indicator (homicides) has improved significantly, rates of crime relating to extortion and theft remain high,<sup>8</sup> and there is still a high level of violence against women, which, based on the available data, has increased during lockdown.<sup>9</sup>
- 1.5 On the fiscal front, although the country began a gradual fiscal consolidation process last decade, leading to primary surpluses between 2017 and 2019, the level of public debt is high<sup>10</sup> and borrowing costs are rising. In conjunction with sluggish economic growth, this limits the fiscal space available to address negative shocks, such as COVID-19 or natural disasters.
- 1.6 Its lack of economic dynamism has kept El Salvador in the lower-middle income category for thirty years,<sup>11</sup> affecting its ability to consolidate progress on poverty and fiscal sustainability. The country's growth over the last five years has averaged 2.4%, below the Central American average.<sup>12</sup> Per capita GDP at current prices was US\$4,187 in 2019, the fifth lowest in Latin America and the Caribbean. This slow growth is mainly attributable to low levels of investment, which averaged 14% of GDP between 2014 and 2019, which compares unfavorably with the Central American average of 26% of GDP.
- 1.7 The factors underlying these social, fiscal, growth, and investment outcomes include shortcomings on the dimensions that directly or indirectly affect households' productivity, investment, and income generation capacity. These include gaps in coverage and quality of basic services such as education, water and sanitation, health, and housing; underdevelopment of productive infrastructure; low levels of financial inclusion; high levels of crime, and governance challenges in relation to fiscal management, government

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<sup>8</sup> Based on official data from the National Civil Police. By contrast with homicides, the rates of other types of crime remained high between 2015 and 2019. During the lockdown in 2020, homicides dropped by 45% while other crimes dropped by 26%.

<sup>9</sup> Between 11 March and 27 April 2020, there was a 30% increase in telephone support in response to incidents of domestic violence (United Nations Development Programme, 2020).

<sup>10</sup> Debt stood at 85.8% of GDP in 2020 (Ministry of Finance, 2021) and is projected to rise to 88.6% of GDP in 2021.

<sup>11</sup> The World Bank classifies the world's economies in four per capita income groups: high, upper-middle, lower-middle, and low. In 1987, El Salvador was in the lower-middle income group along with 18 other countries of Latin America and the Caribbean. In 2019, all but four economies had moved up to a higher income category; El Salvador was among those that did not.

<sup>12</sup> Central America grew one percentage point per year faster than El Salvador over that period.

effectiveness, transparency, and accountability;<sup>13</sup> as well as vulnerability to natural disasters.<sup>14</sup>

- 1.8 The unprecedented circumstances caused by the pandemic have exacerbated some of these constraints and will limit the capacity to reduce poverty and generate higher and more sustainable growth post-COVID-19. As a result of the lockdown measures and the external shock (mainly reflecting slower growth in the United States), El Salvador's GDP contracted by around 9%<sup>15</sup> in 2020, one of the sharpest declines in Central America. The lockdown highlighted the impact of the digital divide on the provision of basic public services, such as education and health, as well as the qualitative housing deficit. These are factors that disproportionately affect the income generating capacity of the poorest populations. The contraction in consumer spending and formal employment is projected to add almost 10 percentage points to the poverty rate, shrink the middle class by 7 percentage points, while increasing inequality.<sup>16</sup> This could lead to worsening crime indicators and rising social unrest, thus reinforcing the incentives to migrate. On the fiscal front, debt stood at 85.8% of GDP in 2020 (as of February 2021), a substantial increase on the 2019 level of 69.9% of GDP.
- 1.9 Against this backdrop, the most pressing challenges the country faces are managing available liquidity to mitigate the impacts of COVID-19 on vulnerable population segments, handling the health crisis,<sup>17</sup> and stimulating economic revival. In parallel, the authorities need to adopt measures in the medium term to enable it to progress toward the sustainability of the public finances and more transparent and government effectiveness, diversify production, create economic opportunities for the population, reduce poverty, and build resilience to the risks posed by climate change. On the basis of these priorities, the authorities

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<sup>13</sup> Based on the World Bank's governance indicator available for up to 2019, it can be seen that after a period of modest improvement in the first half of the 2010s, in the last five years (2014-2019) El Salvador experienced a deterioration, particularly on the dimensions of government effectiveness, the rule of law, and corruption control. By way of example, in 2014 El Salvador's performance in government effectiveness was above the Latin American and Caribbean average, ranking in 96th position out of 209 countries. In the 2019 ranking, it dropped to 135th position. In the case of the rule of law, the country went from 133rd position to 160th, and in that of corruption, from 119th to 141st over the same period. World Bank Worldwide Governance Indicators (<https://info.worldbank.org/governance/wgi/>).

<sup>14</sup> For further analysis of El Salvador, see the Country Development Challenges document (included in the links section of this document), *La Economía del Cambio Climático en Centroamérica* (ECLAC, 2012) and *Impactos Económicos del Cambio Climático en Centroamérica* (ECLAC, 2010).

<sup>15</sup> The IMF and the World Bank estimate declines of 9.0% and 7.2%, respectively, while the Central Reserve Bank of El Salvador (BCR) estimates a GDP contraction of 8.5%.

<sup>16</sup> Inequality and Social Discontent: How to Address Them through Public Policy ([IDB, 2021](#)).

<sup>17</sup> The first case of COVID-19 was reported on 18 March 2020. The installed capacity to address the pandemic was limited, with just 1.2 hospital beds per 1,000 population (below the Latin American and Caribbean region average of 1.9), and a rating of 44.2/100 on the 2019 Global Health Security (GHS) index. Cases in the first wave peaked in August 2020. Although this saturated the health system, the government was able to handle it. As of 30 March 2021, 993 confirmed cases and 31 deaths per 100,000 population were reported, making El Salvador one of the least affected countries in the Central America and Dominican Republic region in terms of contagion.

developed an immediate plan of action<sup>18</sup> and kicked off discussions with the International Monetary Fund (IMF) and multilateral banks on measures to stabilize the debt while prioritizing interventions to respond to short-term health, social welfare, and productive infrastructure needs, as well as to promote economic recovery and restructuring. Additionally, in dialogue with international organizations, government strengthening considerations are being addressed, particularly in the areas of public sector accountability, access to information and generation of data, revenue administration, supervision and control processes, and development of a culture of evaluation of effectiveness of public policies. However, should the effects of the pandemic or the negotiation of an agreement with the IMF drag on, the fiscal headroom available to respond to people's needs and expectations will be more limited. This represents a significant risk for the coming years in view of its possible implications for the country's social, economic, and governance situation.

## II. THE IDB GROUP IN EL SALVADOR

### A. Strategy implementation

- 2.1 The objective of the 2015-2019 country strategy with El Salvador was to support the government's efforts to spur broad-based economic growth. The strategy had three priority areas: (i) strengthening of public finance; (ii) increasing the quality of spending on human capital; and (iii) improving logistics infrastructure. The country strategy also defined citizen security, energy, land management and urban development, and productive development as areas for dialogue. Additionally, a crosscutting approach was taken for gender equality, reducing vulnerability to natural disasters and environmental degradation, combating climate change, and fostering regional integration. In response to the impact of COVID-19, at the authorities' request, the Bank approved an extension of the country strategy's validity period through to 30 June 2021.<sup>19</sup>
- 2.2 The Bank's support for El Salvador during the country strategy period was set against the backdrop of political fragmentation and macroeconomic instability. The absence of agreements between the main political actors and the government's lack of a legislative majority hampered dialogue between the executive and legislative branches and the ratification of Bank loans in the legislative assembly.<sup>20</sup>

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<sup>18</sup> The authorities took action promptly and started to manage funds (Legislative Decree 608 of 26 March 2020) to provide temporary relief to households and businesses affected by the containment measures in the form of cash transfers to vulnerable households; postponement of utility bill payments; deferred settlement of taxes and special levies in the worst affected sectors; and transfer of resources to municipal governments. Subsequently, a second package of measures was approved (Legislative Decree 640 of 5 May 2020) aimed at safeguarding jobs by setting up a trust to stimulate the economic recovery among businesses registered as employers with the ISSS and informal businesses affected by the COVID-19 crisis.

<sup>19</sup> Document GN-3018.

<sup>20</sup> The "Integrated Health Program II" (operation ES-L1095) took 2.8 years from approval (12/2015) to eligibility (09/2018), whereas the "Tax Administration Strengthening Program" (operation ES-L1131) took 2.3 years. The "Global Credit Loan for Financing Energy Efficiency in Small and Medium-sized Enterprises" (operation ES-L1132) took 1.5 years between approval (7/2018) and effectiveness (12/2019). Meanwhile, five operations in the legacy portfolio with which the 2015-19 country strategy began were canceled owing to lack of legislative ratification.

El Salvador began the period on an unsustainable debt and fiscal deficit trajectory, which was compounded by the default in 2017 and credit rating downgrades, leading to delays in decision-making by the public sector. The Bank nevertheless achieved significant results, consolidating its relevance in the country, particularly through its support for the fiscal consolidation process and the policy dialogue on education and logistics, which yielded lessons that may be relevant in the current circumstances. Technical cooperation proved an extremely valuable instrument in facilitating strategic dialogue and interagency coordination, and in achieving results in prioritized areas in which no loan operations took shape.

- 2.3 As a result of the COVID-19 crisis, in 2020 the IDB Group put in place a series of corporate, operational, and governance measures to bolster the timeliness and relevance of its support to the countries of the region.<sup>21</sup> In El Salvador's case the country program was rapidly adjusted via both programming and the active portfolio, so as to inject liquidity and support the immediate public health response, economic recovery, and employment, as well as fiscal policies to mitigate economic impacts.<sup>22</sup>
- 2.4 During the country strategy period,<sup>23</sup> the Bank approved 13 sovereign guaranteed loan operations for a total amount of US\$1.715 billion, including US\$665 million in investment loans, US\$800 million in policy-based loans, and US\$250 million in a special development loan (SDL). Of these, US\$550 million corresponded to operations addressing the public health emergency and the rising budgetary needs caused by the pandemic. Sovereign guaranteed loan disbursements in the period totaled US\$1,118,100,000, with a net negative cash flow for the country of US\$86.1 million. The Bank also approved 48 nonreimbursable technical-cooperation operations for US\$14.8 million in fiscal management, transportation, health, education, pensions, energy efficiency, and violence prevention, and two investment grants for US\$1.79 million aimed at Salud Mesoamerica and malaria prevention initiatives.
- 2.5 IDB Invest approved 22 nonsovereign guaranteed operations for US\$640.1 million,<sup>24</sup> largely to support access to more reliable and cleaner energy, diversification of the energy matrix to include more renewable sources, increased

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<sup>21</sup> IDB Group's Governance Response to the COVID-19 Pandemic Outbreak (document [GN-2996](#)). IDB Group's Response to the COVID-19 Pandemic Outbreak (document [GN-2995](#)).

<sup>22</sup> In agreement with the government, the Bank reformulated its operational program for 2020. The country's financing requirements to address the pandemic were met by allocating an additional US\$400 million for two new operations using the public health (operation ES-L1142, US\$50 million) and public policy and fiscal management prototypes (operation ES-L1143, US\$250 million), and the expansion from US\$100 million to US\$200 million of First Program of Access to Lending for the Recovery of Micro, Small and Medium-sized Enterprises (MSMEs) (operation ES-L1138), which was already in preparation. Also, as part of a concerted effort with the IMF to meet the financing requirements caused by the crisis, the Bank processed an emergency program - special development loan (SDL, operation ES-L1142), for US\$250 million. In the case of the portfolio, the redirection of US\$20 million from operation ES-L1095 was approved for the procurement of medical supplies and equipment for the health system. In the tourism sector, it was agreed that US\$200,000 from operation ES-L1066 be used to help the government design and implement biosecurity protocols to help boost the sector's resilience to the pandemic and better prepare it for changes in patterns of demand.

<sup>23</sup> Between September 2015 and December 2020.

<sup>24</sup> Previous approvals include US\$212.7 million for the trade finance facilitation program (TFFP) and US\$427.47 million for long-term operations.

lending to micro, small, and medium-sized enterprises (MSMEs) and women entrepreneurs, and support to the productive sectors of agribusiness, manufacturing, and foreign trade facilitation. Meanwhile, IDB Lab approved 17 operations for a total of US\$10.4 million, comprising 15 technical cooperation operations (US\$6.7 million), one loan (US\$800,000), and one equity investment operation (US\$3 million). IDB Lab projects focused on access to finance and training for young people for employment and entrepreneurship.

## **B. Main outcomes<sup>25</sup>**

- 2.6 Outcomes were achieved in the **three priority areas**. The crosscutting themes of **gender equality, climate change, and regional integration** were mainstreamed in sector operations implemented during the period and the outcomes are presented within each area.
- 2.7 In the area of **strengthening public finance**, the Bank supported the government's fiscal consolidation process through actions to bolster the sustainability, efficiency, and equity of public spending, and the effectiveness of public investment. Taking a comprehensive approach using an array of instruments, the Bank supported the development of a legal framework for fiscal responsibility to foster spending restraint and a reduction in the debt burden. The package of measures supported enabled the country to go from a primary fiscal deficit averaging -1.2% of GDP between 2013 and 2015 to a primary fiscal deficit of close to 0.6% of GDP in 2019. Reforms to the pension system were also supported. These reforms focused on the regulations under the laws governing the Pension Saving System and the Pension Obligations Trust Fund, helping reduce transfers to meet pension obligations from 2.2% of GDP in 2016 to 1.3% in 2019. With a view to achieving better expenditure efficiency, the Bank supported the gradual changeover from a management area-based budget system to a system focused on programs and results, and promoted reforms to the legal framework for public procurement and the implementation of the COMPRASAL II electronic procurement portal to make public spending more efficient and transparent.<sup>26</sup>
- 2.8 In the case of **raising the quality of spending on human capital**, the Bank's strategic approach aimed to consolidate health services through improved primary and preventive health care, as well as improve the quality of primary and secondary education. The crosscutting theme of gender equity was specifically emphasized in the objective of reducing maternal mortality and deaths from cervical cancer, as well as through coordinated care for victims of violence.
- 2.9 In the **health** area, the Bank helped expand primary level health care access and coverage for over 766,000 beneficiaries in the departments of San Miguel,

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<sup>25</sup> The outcomes of the Bank's support through the legacy active portfolio when the country strategy was approved are included, along with approvals during the period.

<sup>26</sup> These actions were structured as a programmatic series with two policy reform operations (operations ES-L1093 and ES-L1137) for a total of US\$550 million, with the objective of: (i) improving the efficiency of fiscal management, with emphasis on public spending efficiency; and (ii) improving the sustainability of the pension system. The programmatic series was accompanied by four technical cooperation operations. In parallel, dialogue on municipal public finances was supported with ES-T1266 to strengthen sources of municipal revenues in El Salvador, and the Tax Administration Strengthening Program (ES-L1131) was approved. Toward the end of the country strategy period, an emergency operation and a PBL were approved in response to the COVID-19 crisis (operations ES-L1142 and ES-L1143, respectively).

Chalatenango, Sonsonate, and San Salvador. These activities also enabled progress on the consolidation and sustainability of the service provision model through the community family health teams (ECOSF). This led to a rise in registrations for prenatal services from 56% to 90% and infant care services from 56% to 96%. Coverage of 95% of children was also achieved for the measles, mumps, and rubella vaccine. Activities in the maternal and child health area continued through the Salud Mesoamérica Initiative (ISM) in 14 of the country's poorest municipios,<sup>27</sup> helping improve maternal and child health indicators. In particular, over the period 2012-2019, the percentage of women using family planning rose from 53.5% to 75%, institutional births rose from 85.7% to 98.3%, proper treatment of diarrhea from 4.4% to 33.7%, and the percentage of children under two years of age taking micronutrient powder to prevent anemia rose from 0.6% to 24%.<sup>28</sup>

- 2.10 The National Emergency System (SEM) was created and a single health information system developed enabling progress on implementation of electronic medical records. The SEM is one of the cornerstones of the government strategy to respond to the COVID-19 crisis as it facilitates immediate attention to patients prior to their transfer to hospital.
- 2.11 In **education**, the Bank focused on improving the relevance of learning during primary and secondary education as a way of reducing school dropout rates, strengthening education management systems, and supporting job placement for young people. The government<sup>29</sup> was provided support to set up a digital transformation unit to enhance classroom learning and school connectivity. Additionally, the Bank provided technical assistance to set up the first school observatory<sup>30</sup> to obtain social statistics on schools nationally. The observatory's data are an input for a range of social programs, such as "Vaso de Leche" [Glass of Milk]; "Una niña, un niño, una computadora" [A girl, a boy, a computer] and "El Salvador Seguro" [Safe El Salvador]. A census and analysis has also been prepared on childcare in households where the parents' generation has emigrated.<sup>31</sup> These initiatives will be valuable for the follow-up and results monitoring of the recently approved conditional credit line for investment projects (CCLIP) in human capital and the implementation of its first loan for primary

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<sup>27</sup> San Antonio Masahuat, Ilobasco, Santa María Ostuma, San Esteban Catarina, San Ildefonso, Tacuba, Chiltiupán, San Cristóbal, Monte San Juan, Apastepeque, Tecoluca, El Sauce, Sensuntepeque, and Sociedad.

<sup>28</sup> Activities included the "Integrated Health Program" (operation ES-L1027); the "Integrated Health Program II" (operation ES-L1095); "Ciudad Mujer" (operation ES-L1056); and the second and third operations under the Salud Mesoamérica Initiative (ISM) (operations ES-G1002 and ES-G1003, respectively). The human resources of the ECOSF were sustainably institutionalized with their absorption by the Ministry of Health (operation ES-L1027 project completion report). The first and second individual operations under the ISM also worked to strengthen community teams.

<sup>29</sup> Support for the Sectoral Dialogue to Promote Education Quality (operation ES-T1261).

<sup>30</sup> Support for the Development of an Information System in the Education Sector and Census (operation ES-T1233).

<sup>31</sup> Children Raised by Grandparents in the Northern Triangle: Education Policy Responses. Phase I (operation ES-T1282).

- education.<sup>32</sup> The IDB Group also strove to increase job placement for young people, serving over 100,000 young people<sup>33</sup> through training courses, job placement services, and vocational guidance.
- 2.12 Within the framework of the country's initiative to provide **coordinated multisector care to women**, the Bank financed the provision of specialized health services and economic empowerment through the "Ciudad Mujer" program. This program paid particular attention to victims of violence against women.<sup>34</sup> In partnership with the Salvadoran Institute for Women's Development (ISDEMU), its services reached 716,000 women and showed their effectiveness at encouraging survivors of violence against women to seek institutional support. Digitally-based remote care channels were also reinforced with training of ISDEMU staff and specialized care given to victims of violence against women during the COVID-19 pandemic lockdown.<sup>35</sup>
- 2.13 The Bank contributed to El Salvador's productive transformation through improvements in **logistics infrastructure**, with an emphasis on improving rural areas' road connectivity to markets. Specifically, 66.15 kilometers of rural roads were improved, resulting in a reduction in vehicle operating costs for cars, buses, and trucks and increased speeds for vehicle users.<sup>36</sup> Also, the Malecón-La Unión road in the coastal strip area was completed and 16.6 kilometers of rural and tertiary roads were rehabilitated, which will help strengthen road connectivity between zones with high potential for tourism and productive activities.<sup>37</sup>
- 2.14 Infrastructure operations introduced specific actions to mainstream **climate change** resilience and adaptation considerations. Road<sup>38</sup> and productive development<sup>39</sup> operations addressed aspects of risk management and promotion of adaptation and mitigation measures, while the private-sector windows financed

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<sup>32</sup> The conditional credit line for investment projects (CCLIP) Building Human Capital (ES-O0008), and its first operation, "Improving Education Coverage and Quality" (operation ES-L1139) were approved by the Board of Executive Directors in July 2020.

<sup>33</sup> The project "Promoting a Culture of Integration and Equal Opportunities for Youth Living in Poverty" (operation ES-T1260) benefited 73,000 students through training and internships. IDB Lab's "Pathways for Youth" project (operation ES-M1049) trained more than 14,000 young people and helped over 1,000 find jobs.

<sup>34</sup> The "Ciudad Mujer" initiative is a care model bringing together government institutions providing different specialized services for women in the same physical location to ensure that women receive timely, quality, and compassionate care without discrimination or revictimization. The initiative was financed through a portfolio loan (operation ES-L1056) and was strengthened with technical assistance ("Ciudad Mujer Joven" (operation ES-T1243), "Impact Evaluation of the Ciudad Mujer Program in El Salvador" (operation ES-T1279), and "Prevention of Femicide in El Salvador" (operation ES-T1286)). The program has directly benefited over 400,000 women.

<sup>35</sup> Prevention of Femicide in El Salvador (operation ES-T1286). The Violentómetro [Violence-meter] and Rueda de la Violencia [Wheel of Violence] initiatives encouraged the use of the ISDEMU - COVID-19 website.

<sup>36</sup> Rural Roads for Development Program (operation ES-L1045)

<sup>37</sup> Productive Corridors Program (operation ES-L1075).

<sup>38</sup> Rural Connectivity Program for the Northern and Eastern Zones (operation ES-L1061) financed activities to strengthen the Climate Change and Strategic Risk Management Department (DCGER) of the Ministry of Public Works.

<sup>39</sup> The Program for the Tourism Development of the Coastal-Marine Zone (operation ES-L1066) incorporated climate change, sustainable energy, and environmental sustainability initiatives.

clean-energy initiatives.<sup>40</sup> To mainstream the crosscutting perspective on regional integration, technical support was provided for the monitoring of the customs union with Honduras and Guatemala, and to the priorities envisaged under the Plan of the Alliance for Prosperity in the Northern Triangle.

- 2.15 In the **dialogue areas** agreed upon with the authorities, initiatives were undertaken that, by the end of the strategy cycle, had made instruments available to respond to the country's needs during the crisis and support it through the recovery. Specifically, **productive development** continued with the execution of a substantial portfolio inherited from the previous country strategy<sup>41</sup> supporting the transformation of the national development banking system. This effort culminated in the creation of the Development Bank of El Salvador (BANDESAL). Over US\$135 million was injected through BANDESAL in the form of productive credits benefiting over 4,800 MSMEs.<sup>42</sup> The development bank's role will be fundamental in safeguarding the productive infrastructure impacted by COVID-19 and in spurring the economic recovery by mobilizing finance. Also, through financial institutions belonging to the foreign trade finance facilitation program, 1,220 individual foreign trade transactions were supported, totaling US\$213 million.<sup>43</sup> In this area, the IDB and IDB Invest deployed specific actions to promote the provision of financial services to women.<sup>44</sup>
- 2.16 In **citizen security**, sector authorities were supported in the formulation and implementation of actions to help reduce the homicide rate from 105 to 36 cases per 100,000 population between 2015 and 2019. This decline was more pronounced in municipios benefiting from the IDB-funded program, where homicides fell by 51.2%.<sup>45</sup> The actions included the use of videosurveillance networks, a radio service, and cybersecurity, and the construction of 31 public spaces.
- 2.17 Lastly, in **urban development**, the Bank worked to reduce social vulnerability by improving living conditions in informal urban neighborhoods in San Salvador,<sup>46</sup> providing new or improved housing solutions to over 3,000 households and

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<sup>40</sup> The Capella Solar PV Project (operation 12232-01) financed by IDB Invest, aims to provide the country with an extra 293,000 MWh of clean solar photovoltaic energy, projected to reduce annual CO<sub>2</sub> emissions by almost 80,000 tons.

<sup>41</sup> As of 28 October 2015, the available amounts of the following operations were: "Program to Support Production Development for International Integration" (operation ES-L1057), US\$22.8 million (76% of the approved amount); "Tourism Development of the Coastal-Marine Zone" (operation ES-L1066), US\$24.4 million (97% of the approved amount); "Financing Productive Development for El Salvador" (operation ES-L1089), US\$96.3 million (96% of the approved amount).

<sup>42</sup> Financing Productive Development for El Salvador (operation ES-L1089); BANDESAL Monitoring and Evaluation System Implementation (operation ES-T1238).

<sup>43</sup> Of which, US\$99 million was in the form of credit guarantees and US\$114 million in that of loans.

<sup>44</sup> For example, with loan proceeds from the project "Financing Productive Development for El Salvador" (operation ES-L1089) credits were approved for more than 1,400 women-led MSMEs. IDB Lab devoted efforts to expanding rural credit to 1,400 micro and small women entrepreneurs in rural areas through the "Expansion of Rural and Periurban Credit for Salvadoran Women" project (operation ES-S1018) and supported an inclusive distribution model to support the economic and social empowerment of women and rural areas with the project "Scaling the 'Shatki' Distribution Model in El Salvador" (operation ES-T1255).

<sup>45</sup> Ciudad Delgado, Mejicanos, Soyapango, and San Salvador.

<sup>46</sup> Program for Housing and Comprehensive Improvements for Informal Urban Neighborhoods: Phase II (operation ES-L1022).

benefiting more than 8,900 families through better access to basic water and sanitation services. Also, flood and landslide risk mitigation works were financed in seven settlements.<sup>47</sup> A further 5,470 households benefited from new or improved housing solutions through IDB Invest<sup>48</sup> transactions to strengthen financial institutions' mortgage portfolios.

### C. Portfolio in execution and lessons learned

- 2.18 **Current portfolio.** As of 31 January 2021, the IDB portfolio in El Salvador comprised 11 sovereign guaranteed operations for a total approved sum of US\$745 million with an undisbursed balance of US\$613.6 million, focusing on: human capital, 48.1%; productive development, 47.8%; public finance, 3.6%; and public safety, 0.5%.<sup>49</sup> It includes 25 technical cooperation operations for US\$9.4 million with an undisbursed balance of US\$6.7 million in the areas of gender, education, health, violence prevention, agriculture, transportation, drainage, risk management, energy, regional integration, and institutional strengthening. There are also two investment grants with an approved amount pending disbursement of US\$1.5 million in the health area. In the knowledge area, studies are under way to support spending efficiency in electricity sector subsidies, investment, new revenue sources, public-private partnerships, and synergies in productive development projects. IDB Invest has an active portfolio of 17 transactions, with an exposure of US\$255.9 million, concentrated in the financial institutions and infrastructure sectors. The IDB Lab portfolio comprises 12 operations for US\$8.2 million, focused on financial services, human capital, MSMEs, and innovation.
- 2.19 **Lessons learned.**<sup>50</sup> At the **strategic** level: (i) in a complex political and institutional context hampering reforms or key initiatives prioritized by the strategy, technical cooperation can be used to enable an active dialogue on the medium-term objectives and to develop proposals that subsequently underpin investment or reform programs;<sup>51</sup> (ii) in the case of investment operations, which entail budgetary commitments after project execution has ended, it is important that the design envisage an analysis of resource needs to guarantee the sustainability of the works and investments financed;<sup>52</sup> (iii) faced with limited fiscal space, it is important that

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<sup>47</sup> Reduction of Vulnerability in Informal Urban Neighborhoods in the San Salvador Metropolitan Area (operation ES-L1016).

<sup>48</sup> Habitat for Humanity: Increasing Access to Home Improvement Financing (operation ES-L1086), part of IDB Invest's legacy portfolio.

<sup>49</sup> In the latest project monitoring exercise in March 2020, all the operations between eligibility and closure reported a satisfactory classification.

<sup>50</sup> This section is mainly based on project completion reports submitted during the strategy period, semiannual portfolio meetings, and the Office of Evaluation and Oversight (OVE) Country Program Evaluation for 2015-2019.

<sup>51</sup> For example, in the education area, the technical dialogue was deepened with four technical cooperation operations, culminating in 2019 in the programming of a US\$250 million CCLIP in the sector, with the first operation approved in 2020. Given the absence of new investment loans, the Bank continued to support work to improve the country's logistics infrastructure through four technical cooperation operations financing studies on mobility, goods transport, and preparing an infrastructure master plan. These inputs will help prioritize investments.

<sup>52</sup> This was a commitment by Bank management within the action plan for the adoption of the OVE recommendations on the 2011-2015 country strategy, which were 100% fulfilled.

the Bank monitor the formulation of the national budget proactively to ensure the allocations necessary for project execution are included; (iv) the strategic use of the intraregional technical cooperation instrument (CT/INTRA) contributes to the technical dialogue on loan preparation and the South-South dissemination of positive experiences in loan execution;<sup>53</sup> (v) for nonsovereign guaranteed operations, combining financing with technical assistance has made it possible to strengthen institutional capacity to meet demand from special market segments, particularly MSMEs and projects to raise environmental standards.

- 2.20 At the **operational** level, some of the recommendations considered relevant in the context of the COVID-19 pandemic, where speed of execution, communication, and availability of monitoring mechanisms are essential to making timely adjustments to enable achievement of results and accountability, are: (i) promoting the dissemination of IDB projects to foster greater involvement by qualified bidders so as to speed up execution and fulfillment of project objectives; (ii) for high-visibility projects, it is important that the IDB Group run communication and outreach campaigns and monitor information published in the media in order to gauge the public's reaction to the project and identify measures needed to minimize sustainability and reputational risks. Similarly, enhancing executing agencies' communications capabilities is beneficial, allowing them to be put in charge of effective and open communication of execution challenges, project benefits, and measures to ensure the appropriate use of resources; (iii) strengthening the analysis of national legislation on competencies and procedures in target areas boosts project sustainability and minimizes potential conflicts between the proposed execution arrangements and the country's laws; (iv) the country should be given support on monitoring and evaluation mechanisms so the impact of the Bank's activities on financial intermediaries such as BANDESAL and second tier State-owned banks can be measured to enhance the effectiveness and relevance of these programs; (v) IDB Invest's support should consider fostering competition and productivity gains so its actions can help create more favorable conditions for consumers and increase the supply of goods on the market.

### III. PRIORITY AREAS

- 3.1 Consistent with the priorities set by the government, the objective of the new IDB Group country strategy with El Salvador for the period 2021-2024 is to help mitigate the impact of the crisis on the country's prospects for recovery and to

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<sup>53</sup> The "Exchange El Salvador - Medellin Colombia on Strategies to Reduce School Violence" (operation ES-T1257); "Exchange Between El Salvador and Argentina on Policies for an Improved School to Work Transition" (operation ES-T1272); and "Exchange of Experience on Internal and External Evaluations of the National Education System of Ecuador" (operation ES-T1291) contributed to preparation of the CCLIP "Building Human Capital: Birth, Growth, Learning" and its first loan (CCLIP ES-O0008 and operation ES-L1139, respectively). Meanwhile, the Internship for "Seguros Futuro and Banco de Fomento Agropecuario de El Salvador to SAGARPA, Mexico" (operation ES-T1256) contributed to the preparation of the "Global Credit Program for Micro and Small Enterprises in El Salvador" (Banco de Fomento Agropecuario - BFA) (operation ES-L1136). Lastly, "BANDESAL Monitoring and Evaluation System Implementation" (operation ES-T1238) and "BANDESAL Knowledge Exchange with Mexico (Nacional Financiera - NAFIN) and Colombia (Bancoldex)" (operation ES-T1310) contributed to the design of the "Conditional Credit Line for Investment Projects to Facilitate Access to Business and Housing Loans" and its first loan (CCLIP ES-O0009 and operation ES-L1138, respectively).

achieve more vigorous, inclusive, and sustainable growth over the medium term. To support this objective, the proposed approach for the years ahead responds to the country's most immediate needs deriving from the health crisis and its social and economic impacts, while supporting the process of fiscal consolidation and the restructuring of production. In this regard, three priority areas have been identified to guide the IDB Group's support for the government program: (i) fiscal sustainability and efficiency; (ii) reducing social vulnerability; and (iii) revitalizing and restructuring production. Gender equality and diversity, climate change, environmental sustainability and natural disasters, and institutional capacity and the rule of law will be addressed in a crosscutting way, building on the progress made in the previous strategy cycle. In particular, an active dialogue will be maintained with the authorities to provide continuity to actions linked to institutional strengthening and transparency, and to identify both financial and nonfinancial initiatives enabling the expansion of the scope of these efforts. Based on the experience of the previous strategy, dialogue will be maintained on relevant issues that may move up the country's agenda as a result of the changing context, while contributing the Bank's technical knowledge and facilitating exchanges with other countries in the region.

- 3.2 The priority areas are interrelated and the sector emphasis within each was the outcome of an extensive dialogue with the country authorities and civil society.<sup>54</sup> This dialogue took into account how the global impacts of the pandemic are evolving and its short-to-medium term repercussions for El Salvador, the structural challenges the country faces, the portfolio of projects currently underway, the target areas for international cooperation, the indicative financing scenario, lessons learned from the previous country strategy, and Office of Evaluation and Oversight (OVE) recommendations on the 2015-2019 country program (Annex V). Activities will be aligned with the second Update to the IDB Group Institutional Strategy 2020-2023, specifically in the areas of institutional strengthening, developing quality human capital, financial inclusion, delivering inclusive and sustainable infrastructure services, and improving the productivity and resilience of small producers. The agenda of gender equality and diversity, climate change and environmental sustainability, and institutional strengthening and the rule of law will be promoted in a crosscutting way. Coordination and synergies between the IDB, IDB Invest, and IDB Lab will be addressed in accordance with the respective guidelines and business plans.<sup>55</sup>

#### **A. Efficiency and fiscal sustainability**

- 3.3 In the wake of the 2008-2009 international financial crisis, El Salvador embarked on a process of fiscal consolidation enabling it to reduce the overall deficit from 6.7% of GDP in 2009 to 3.1% in 2019, while the primary balance went from a deficit

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<sup>54</sup> This process included strategic dialogues on the authorities' vision of the country's challenges, sector discussions, workshops on obstacles to growth, coordinated monitoring with the authorities and other donors on the impacts of the COVID-19 crisis and the most immediate priorities, and meetings organized by the country with groups representing civil society.

<sup>55</sup> IDB Invest Business Plan 2020-2023 (document CII/GA-77-8) and IDB Lab Business Plan 2019-2021 (document MIF/GN-235-3).

in 2009 (-3.6% of GDP) to a surplus in the last three years.<sup>56</sup> This process was mainly driven by increased revenue, including increases in the income tax rate, modifications to excise tax rates and bases, and the creation of new taxes.<sup>57</sup> With the passing of the Fiscal Responsibility Law in 2016, El Salvador also took significant steps to increase fiscal transparency. The Law established the obligation to publish a medium-term fiscal framework setting forth the fiscal scenarios and underlying assumptions over a ten-year horizon. On the revenue front, measures were taken to combat evasion, and progress was made on compliance with Organisation for Economic Co-operation and Development (OECD) fiscal transparency standards, and as regards public spending, the “reserved expenses” item, which in the past had been used as a means of diverting funds illicitly, was eliminated.<sup>58</sup> Additionally, a pension reform was passed that reduced the fiscal cost of pensions. However, despite the adjustments made, the country’s debt level remained around 70% of GDP, partly as a result of sluggish growth, and borrowing costs rose.<sup>59</sup>

- 3.4 In response to the pandemic, the authorities’ immediate priority has been to provide temporary relief to households and businesses affected by containment measures with a program of measures representing 11.5% of GDP.<sup>60</sup> These actions, together with the decline in growth and fiscal revenue, raised the deficit and debt to 9.7% and 85.8% of GDP, respectively, in 2020. Additionally, the need to apply emergency measures for procurement and contracting required greater control and audit mechanisms, leading to the adoption of mitigation measures such as performing audits concurrently and making them publicly available to ensure accountability for expenditures incurred in relation to COVID-19.
- 3.5 Steering the economy toward a sustainable growth path over the medium term will be key to improving the investment climate and will require fiscal consolidation efforts to reduce debt levels to 60% by 2030, accompanied by crosscutting activities to strengthen the efficiency and transparency of expenditure and revenue alike. Given the limited fiscal space in the context of the pandemic, **improving spending efficiency** is a priority area of action in contributing to sustainability and enhancing the government’s effectiveness at providing critical basic services for growth and poverty reduction. Although primary public sector spending in

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<sup>56</sup> The primary balance, including pensions, was 0.7%, 0.9%, and 0.6% of GDP in 2017, 2018, and 2019, respectively (Ministry of Finance, 2020).

<sup>57</sup> The income tax rate for higher earners rose from 25% to 30% (Legislative Decree 957-2011). A tax on financial transactions (DL-764-2014); a levy on large taxpayers (DL-161-2015); and a special contribution for security (DL-162-2015) were created.

<sup>58</sup> As well as providing for the creation of a medium-to-long-term fiscal framework, the Law establishes three main rules: (i) achieve positive primary balances after completion of the fiscal consolidation period; (ii) achieve a minimum tax burden from the third year of implementation onward; and (iii) to remain below a current expenditure ceiling (as a percentage of GDP) following the fiscal consolidation period. The latter imposed a two-sided fiscal rule, reducing the share of current expenditure over time and increasing the capital as recommended in Izquierdo, Pessino, and Vuletin (2018).

<sup>59</sup> Borrowing costs came to 3.8% of GDP in 2019, if pension debt is included, 3.0% of GDP if it is not. Securing debt during the pandemic has been at considerably higher prices, which could raise borrowing costs to 6% of GDP for the period 2021-2024.

<sup>60</sup> The main steps included cash transfers to vulnerable households, deferral of payment for utility services; deferral of payments of tax and special levies in the hardest hit sectors; and transfers of resources to municipal authorities.

El Salvador before the pandemic was consistent with its level of development,<sup>61</sup> the technical inefficiency of spending—defined as the sum of leakage in targeted transfers and waste in public procurement and employee compensation—was equivalent to 6.5% of GDP, the second highest level in Latin America. The evaluation and redimensioning of fiscal benefits and prioritization of beneficiaries of social programs, based on up-to-date information and clear targeting criteria linked to well-defined policy objectives, therefore takes on particular relevance. Additionally, given the estimated level of efficiency in public procurement and employee compensation, it is key to strengthen public procurement and contracting systems to ensure integrity, transparency, and competition in the various stages of the contractual cycle, and a review of the civil service to identify actions to reduce inefficiencies in salary costs. Lastly, despite recent advances, the pension system continues to suffer from problems of limited coverage, low value pensions, and rising fiscal costs.

- 3.6 In terms of **investment** expenditure, El Salvador's levels are low compared with Central America, Panama, and the Dominican Republic,<sup>62</sup> and significant weaknesses were observed in its management, particularly as regards planning and project selection.<sup>63</sup> To address these issues, the Public Debt Bureau (DGICP) has developed the conceptual model of the public investment system, and a methodology for the design and evaluation of investment projects. This model and methodology are currently being reviewed and fine-tuned prior to implementation. To bridge the gaps in both investment financing and investment management, the country has reformed the framework for public-private partnerships in order to promote their use in the social sector and for productive infrastructure.<sup>64</sup> However, their use remains incipient. To boost the effectiveness of these initiatives, it will be important to accompany them with mechanisms to make the end-to-end investment cycle more transparent, whether in the context of public financing or through public-private partnerships.
- 3.7 At the same time, improving the targeting and relevance of spending requires **statistical capability** as a support to decision-making. The country bases its plans on data projections from the most recent national population and housing census, which was taken in 2007, and revealed a 20% discrepancy between the population projected in the previous census and that actually observed. Updating it would have benefits cutting across multiple sectors and development initiatives as it would provide key data for the optimization of resource allocation at the subnational and sector level based on the geographic distribution and needs of the population, and so enable better targeting, based on dimensions such as gender, as well as evidence-based monitoring and evaluation of program performance.

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<sup>61</sup> Estimated in 2017 by application of Wagner's Law (Izquierdo, Pessino, and Vuletin, 2018).

<sup>62</sup> Levels of public investment have averaged 2.4% of GDP over the last five years, compared with 4% of GDP across the Central America, Panama, and the Dominican Republic region as a whole (World Development Indicators (WDI), 2021).

<sup>63</sup> Better Spending for Better Lives. IDB. 2018.

<sup>64</sup> The Public-Private Partnerships Law was amended in 2018 to allow such partnerships to include the design, financing, construction, operation, and maintenance of infrastructure for health care services delivery through the ISSS and for the provision of education services, as defined in the General Education Law.

- 3.8 On the **income** side, to achieve fiscal sustainability in the medium-term without curtailing priority spending and investment, it will be necessary to adopt measures to bolster tax revenues and enhance the efficiency of the tax administration. Despite progress over the last decade, El Salvador is among the countries of the region with the lowest tax effort,<sup>65</sup> partly as a result of evasion, avoidance, and late payment of taxes. Measures to bring noncompliance down to the Latin American and Caribbean average through improvements in tax<sup>66</sup> and customs<sup>67</sup> management could increase tax collection by approximately 1.7% of GDP. Strengthening tax policy, through higher rates and reduced tax expenditure, could yield a similar result.<sup>68</sup>
- 3.9 Additionally, there is scope to support the strengthening of public finance through improvements in transparency and integrity. The IMF has identified fiscal governance as a source of vulnerability for corruption control in El Salvador, pointing to opportunities for improvements in several areas and at several agencies, including the external audit control agency, internal control, the rules to ensure transparency and accountability in public spending, the adoption of OECD fiscal transparency standards, a review of the governance of key entities such as the tax and customs authority, and for alignment of the current corruption control system with international standards.<sup>69</sup> Moreover, the IMF has also identified opportunities in financial integrity with a view to preventing money laundering, such as a review of the current regulations to adapt them to international standards, and strengthening prevention and regulation bodies, in terms of both processes and the adoption of new technologies.
- 3.10 In the 2021-2024 country strategy, through portfolio operations<sup>70</sup> and new financial and nonfinancial measures, the IDB Group will support the country's efforts to return to the path of fiscal sustainability over the medium term and improve efficiency and transparency in the use of public resources, taking account of the need to protect investment spending and the vulnerable population groups hardest hit by the crisis. On the *income* side, the design and implementation of mechanisms to strengthen tax collection, will be continued, including strengthening the independence and accountability of fiscal entities, and supporting the design

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<sup>65</sup> The tax effort in El Salvador is 48%, which is below the Latin American and Caribbean regional average of 58%. The Pessino and Fenochietto (2013) methodology was used for this comparison. The estimated tax effort is a measure of how close or far a country is from achieving its maximum collection potential (compared with other countries with similar characteristics).

<sup>66</sup> Evasion of valued added tax (VAT) is 33.1%, which is higher than the 26.4% average for the region (Internal Revenue Office (DGII), 2012). Income tax evasion stands at between 45% and 50% according to unofficial estimates (Fretes Cibils et al., 2013).

<sup>67</sup> Studies on customs fraud in El Salvador suggest it is equivalent to 2.8% of GDP. (Konrad-Adenauer-Stiftung, 2015).

<sup>68</sup> The VAT rate (13%) is below the Latin American and Caribbean regional average (15.5%). While personal income tax rates are similar to those of Latin America and the Caribbean, the corporate income tax rate (35%) is higher than the average for Latin America (27.6%) and, as an indicator of exemptions, tax expenditure is comparatively low (2.9% of GDP) (Ministry of Finance, 2015).

<sup>69</sup> El Salvador. Staff Report of the 2019 Article IV Consultation. IMF. May 2019.

<sup>70</sup> "Tax Administration Strengthening Program" (operation ES-L1131). Meanwhile, the "Integrated Health Program II" (operation ES-L1095) includes activities to enhance hospital management and efficiency.

and evaluation of measures consistent with a medium-term fiscal framework and a progressive tax policy that contributes to poverty reduction.

- 3.11 In relation to *public spending*, the development and adoption of measures to reduce inefficiencies at both crosscutting and sector levels will be pursued, such as subsidy targeting by means of a transparent technical methodology that incorporates sustainability criteria in its prioritization, and strengthening of beneficiary selection mechanisms for productive infrastructure support programs. In the pensions area, the Bank will continue to support the country on the use of tools enabling evaluation of different policy options to support decision-making. Moreover, to foster transparency and improve governance in the management of resources in a crosscutting way, the Bank will work with the authorities to strengthen control entities and the public procurement system, the dissemination of, and access to, fiscal information, and public accountability mechanisms. The IDB Group will complement these efforts with actions to strengthen the management of *investment spending*, with technical support to the authorities on the identification, planning, and structuring of projects under the new legal framework for public-private partnerships and the adoption of tools to facilitate works monitoring by the authorities and greater citizen participation in investment monitoring.<sup>71</sup> In a similar vein, efforts will be devoted to improving the statistical information system, with an emphasis on strengthening the lead agency, updating the national statistical database, disseminating information, and supporting planning, and the public policy monitoring and evaluation system, in order to improve government effectiveness and transparency in a context of fiscal constraint and the needs arising from COVID-19.

## **B. Reducing social vulnerability**

- 3.12 The loss of formal<sup>72</sup> and informal jobs as a result of COVID-19, in conjunction with the negative impact of the lockdown on the school year, could widen the human capital gaps that have hampered economic growth and a sustainable reduction in poverty in El Salvador, while heightening social risks, mainly among the young<sup>73</sup> and women, particularly in a context where the incidence of gender-based crime and violence remains high. Moreover, as mobility restrictions are gradually eased, this situation could have an impact on trends in migration. Efforts to improve the government's effectiveness at delivering key services such as social welfare, education, health, and housing will need to be stepped up if social vulnerability is to be reduced.
- 3.13 The pandemic has highlighted the need for a targeted and efficient **social protection system** that ensures the population has adequate and timely coverage against shocks and to use mechanisms that enhance its traceability and transparency. Historically, the country has relied on nontargeted subsidies on

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<sup>71</sup> One example is the georeferencing of the investment and/or the presentation of the financial and management results in a more comprehensible form for the public via the MapalInversiones platform, developed by the IDB and implemented by several countries of Latin America.

<sup>72</sup> The latest social security figures indicate a loss of 6.7% of ISSS contributors as of November 2020 (ISSS, 2021).

<sup>73</sup> Individuals living in households in districts of San Salvador under the sway of criminal gangs attain lower levels of education, asset accumulation, and employment income than individuals living elsewhere (Sviatschi, 2019. Using exogenous variations in the emergence of criminal gangs in El Salvador).

various public services, but these do not reach the poorest households and represent a significant tax burden. The master registry of participants (RUP) created in 2013 as a key tool in social program beneficiary selection based on predetermined criteria, has progressed slowly and few programs have used it to add beneficiaries to their rolls or monitor benefits. Meanwhile, programs exhibiting effective targeting of the most vulnerable population groups have had only minor impact owing to the low rates of coverage or limitations on benefits.<sup>74</sup> El Salvador will therefore need to emphasize the rationalization, targeting, and reach of social programs to boost their effectiveness, efficiency, and transparency in a context marked by significant fiscal constraints and worsening social vulnerability.

- 3.14 The biggest challenge in **education** remains the dropout rate, as it leaves many young people without opportunities and at heightened risk of antisocial behavior.<sup>75</sup> Pre-pandemic, the completion rate was just 34%,<sup>76</sup> below the Latin American average of 50%. This affects women and persons with disabilities most,<sup>77</sup> and reflects differences between individuals who had access to preschool education and those who did not. Coverage of early childhood services is very low (8% nationally), and preschool coverage, as well as being low (50% nationally), also has marked gaps related to income levels, with poorer groups reaching levels of 40% compared with 80% among wealthier groups.
- 3.15 Another challenge for the education system is to ensure that all students graduate from secondary education with the cognitive, technical, and socioemotional skills they need to access tertiary education and quality jobs, especially in the post-COVID-19 environment. The workforce's skills are limited, hindering employability in productive formal jobs, with 60% of firms reporting workers' inadequate education as an obstacle for their business.<sup>78</sup> Significant differences also exist between the participation of men and women in the labor market, with women's participation being among the lowest in the Latin American and Caribbean region. There is also a large gap between the participation rates of the disabled and nondisabled populations.<sup>79</sup> Education policy imposes rules for selection that have resulted in a teaching staff that does not meet the needs of a

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<sup>74</sup> For example, the Familias Sostenibles [Sustainable Families] conditional cash transfer program, previously known as Comunidades Solidarias [Caring Communities], is the main income redistribution program, with a coverage of 100,000 households in 2015, and continues to have limited reach. Evaluations show direct transfers to be well targeted on the most vulnerable populations, but both coverage and transferred amounts are low, limiting their impact on poverty and inequality indicators (Country Development Challenges (CDC)).

<sup>75</sup> As many as 94% of gang members have not completed formal education and just 65% have attended secondary school (Cruz et al., 2017).

<sup>76</sup> Lack of interest is the main reason for dropping out of the system (IDB education statistics portal (CIMA), 2018).

<sup>77</sup> Access problems for persons with disabilities are also apparent. In the 7-to-17 age group, people with disabilities have one year of schooling less than those who do not. [Análisis y Caracterización de las Personas con Discapacidad a partir de la Encuesta Nacional 2015](#).

<sup>78</sup> INSEAD, 2016.

<sup>79</sup> Women's workforce participation in El Salvador (45,5%) is half that of men (80%) and is 6.5 percentage points below the average female participation rate across the Latin American and Caribbean region (WDI, 2021). Among the population aged 18 to 59, there is a workforce participation gap of 17.8% between people without disabilities and those with disabilities (United Nations Children's Fund, UNICEF).

- quality educational system.<sup>80</sup> This problem has been exacerbated by the shift to online teaching. Meanwhile, the lack of statistical data affects education management and gives rise to inefficiencies in the allocation of human and financial resources.
- 3.16 Despite the job losses resulting from the recession, in the medium term the crisis could represent an opportunity for nontraditional sectors, such as e-commerce and digital services. However, to take advantage, more digital literacy and capacity to adapt and learn new practices will be required. This creates scope for matching potential labor market needs with the skills of young people who will be looking for work in the years following the pandemic, so as to help cushion the social risk, displacement, and migration.
- 3.17 The country has made significant strides in **health**, but challenges persist. Teenage pregnancies remain high, especially in the poorest income quintile<sup>81</sup> and a significant rise in chronic, non-communicable diseases has been observed, such that they have become one of the leading causes of hospitalizations and death in the country.<sup>82</sup> This is pushing up demand for hospital services, which is translating into shortages of beds and human resources and, going forward, is a risk factor for events like COVID-19. Mother and child mortality has dropped substantially, but weaknesses in service coverage and quality could slow the pace of improvements in the years ahead. As much as 10% of the population still lacks access to health care services<sup>83</sup> and integrated health networks are inadequately coordinated and their efficiency is limited on all levels. The system does not have standardized processes or adequate monitoring and supervision mechanisms. Instead, it depends on manual medical records, resulting in duplication and higher costs.<sup>84</sup> The country has successful experiences that could be expanded to strengthen the effectiveness, efficiency, and transparency of the sector's expenditure. For example, the Digital Health Strategy would enable better care to be given to beneficiaries and reduce inequities by catering to less favored sectors, while the associated information systems would facilitate monitoring of care provided to individual patients and analysis of service costs and invoicing.<sup>85</sup>

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<sup>80</sup> Just 6% of math and science teachers have a specialization in these subjects.

<sup>81</sup> The adolescent fertility rates (AFR) for El Salvador and the Latin American and Caribbean region are 57.7% and 41.2%, respectively. By income level, El Salvador's AFR was 118 in the poorest income quintile compared with 35 in the wealthiest (CDC).

<sup>82</sup> The main chronic, non-communicable diseases include cardiovascular disease, cancer, chronic respiratory disease, and diabetes. According to data from the Institute for Health Metrics and Evaluation (IHME), the leading causes of death in El Salvador are cardiovascular disease and chronic kidney disease.

<sup>83</sup> Among the poorest groups, the percentage of the population without access to health care services is 14.9%.

<sup>84</sup> A Ministry of Health (MINSAL) analysis suggests that savings of US\$4 million per year could be obtained in digital imaging. The services delivered to patients could also be made more efficient. For example, creating a digital file takes three minutes compared with 10 minutes for a manual one, and a digital emergency sheet takes one minute instead of five minutes.

<sup>85</sup> Another example is that of results-based financing models, such as the Salud Mesomérica initiative and the Regional Initiative to Eradicate Malaria. These programs are based on cost-effective interventions, direct technical assistance, clear, externally verified targets, and a systemic and integrated approach over the course of care provision.

- 3.18 In the case of **housing**, lockdown and the economic crisis have highlighted the vulnerability many Salvadoran households face as a result of the housing situation. Over the past thirty years, the formal housing supply has mainly been aimed at social strata with the highest purchasing power and has not been able to meet demand from the poorest population segments. As well as this limited supply of low-income housing, there are significant barriers to accessing mortgage lending. Just 2.4% of the poorest 40% of the population has a mortgage, compared with 3.6% in lower-middle income countries. Meanwhile, the proportion of women who have obtained a mortgage in El Salvador (3.7% of adult women) is less than half the proportion of men (7.4%), and lower than the average for the Latin American and Caribbean region (3.9%) and lower-middle income countries (4%).<sup>86</sup> In light of these limitations, 60% of the population segment receiving income less than four times the minimum wage has opted to build their own home on illegal plots in marginal neighborhoods, with substandard basic services<sup>87</sup> and with no legal certainty over title,<sup>88</sup> which also limits their access to credit. It is also calculated that 41% of the population lives in high risk areas and 84% of buildings in urban zones of El Salvador are highly vulnerable to major adverse natural events.<sup>89</sup> This represents a considerable economic and social vulnerability, and has been exacerbated by the COVID-19 crisis. The sector's regulatory framework is still developing, and legislative and regulatory proposals have been put forward to support an integrated vision for it, creating the opportunity to address these problems and define clear urban planning guidelines while fostering closer coordination of initiatives to address the country's affordable housing needs in a way that enhances spending effectiveness in the sector and promotes a contribution from the private sector that is consistent with the needs of the vulnerable population.
- 3.19 In the 2021-2024 country strategy, through its existing portfolio,<sup>90</sup> new operations, and technical assistance, the IDB Group will support the authorities' efforts to reduce the drivers of social vulnerability, with an emphasis on strengthening the management and targeting of spending on priority sectors. In the case of *social protection*, efforts will be made to enhance targeting and extend the reach of program benefits and social safety nets to support poverty reduction, equity, and job security.<sup>91</sup> In *education*, the Bank proposes to work with the government to

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<sup>86</sup> [Global Financial Inclusion Database](#). World Bank.

<sup>87</sup> Official microdata (Multipurpose Household Survey (EHPM)) show significant differences in lack of access to basic services such as water (18% of vulnerable households and 30% of the poor do not have running water) and in the quality of housing materials (19% of vulnerable households and 37% of the poor do not have solidly constructed walls).

<sup>88</sup> Official microdata (EHPM) show that 47% of vulnerable households and households living in poverty (income of less than US\$12.5 per day) did not own their own home in 2019, whereas in 2000 the figure was 41%.

<sup>89</sup> As of 2017, some 73,339 homes were estimated to be highly or very highly prone to flooding (Ministry of Agriculture and Natural Resources ([MARN](#)), 2017).

<sup>90</sup> "Integrated Health Program II" (operation ES-L1095), "Improving Education Coverage and Quality: Birth, Growth, Learning" (operation ES-L1139), and "Immediate Public Health Response to Contain and Control the Coronavirus and Mitigate its Impact on Service Delivery in El Salvador" (operation ES-L1144).

<sup>91</sup> In job security, the aim is to develop a digital services offering leveraging technology to provide the self-employed with personalized benefits, such as medical insurance, pensions, savings, and training, to bolster their economic and financial security and so help reduce their vulnerability.

develop a crosssector policy integrating an array of services in early childhood, mainly in the 0-to-3-years age range, expanding quality early childhood and preschool education and to boost the relevance and promotion of flexible arrangements so young people can complete their secondary education and gain labor market skills. These activities will include gender and digital skills components and involve coordination with the private sector. The development of educational infrastructure will factor in adaptation to climate change and resilience to natural disasters.<sup>92</sup> To strengthen the efficiency and effectiveness of spending in the sector, the Bank will work with the government on the management system, in particular, as concerns the timely generation and analysis of reliable data and its use in decision-making. In a complementary way, IDB Invest will seek to help close the education gap by supporting tertiary education institutions that foster these skills, and by providing business advisory support to strengthen its clients' gender equity and human capital practices. In *health*, support will continue for initiatives geared to modernizing the Ministry of Health's technology and enhancing health service management, quality, and coverage, including strengthening the capacity to respond to COVID-19 considering successful experiences at national and regional levels. In *housing*, the Bank will evaluate the use and development of financing instruments enabling better access to quality housing with greater resilience to natural disasters for vulnerable populations, emphasizing beneficiary targeting and identification considerations based on clear prioritization criteria, and the Bank will seek to provide technical support on aspects of managing the permitting process, supervision, and monitoring of new construction works. Activities in this strategic area will take gender and diversity considerations and strengthening of sector ministries' management capacity into account.

### **C. Reactivation and restructuring of production**

- 3.20 Over the last 10 years, El Salvador has embarked on a slow but sustained diversification of exports, reflected in the numbers both of products exported and of trade partners.<sup>93</sup> Nonetheless, its level of economic complexity, although above the Central American region's average, is still far short of the average for Latin America and the Caribbean. Efforts to develop sectors such as tourism, where the country is potentially attractive on account of its natural and cultural capital, have given rise to an expansion in some regions, but the COVID-19 crisis, compounded by shortcomings in the enabling infrastructure and the absence of an adequate interagency coordination framework, compromise its recovery and sustainable development in the years ahead. In traditional sectors, such as agriculture, which remains one of the main sources of food, employment, and income for the nonurban population, producers are ill-prepared to confront the risks associated with climate change and natural disasters.<sup>94</sup>
- 3.21 El Salvador is facing numerous challenges to stimulating its economic growth. The crisis is placing the emphasis on crosscutting issues that support reactivation and enable productivity gains and increased resilience to various types of shock. As well as the challenges mentioned in the two preceding areas, problems include

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<sup>92</sup> This concerns the construction and refurbishment of green buildings that meet sustainability standards.

<sup>93</sup> For more details see the CDC.

<sup>94</sup> An IDB study estimates that yields of rain-fed bean and corn crops will fall by 31% and 24% between 2020 and 2050, and that areas suitable for arabica coffee will shrink by 77% ([IDB, 2020](#)).

- access to finance, which constrains MSMEs' recovery; shortcomings in infrastructure services, which raise logistics costs for Salvadoran firms and limit sustainable and inclusive development in some parts of the country; and connectivity issues, which restrict the adoption of information technology, a key factor in the post-COVID-19 context.
- 3.22 Reactivating production and safeguarding employment depends largely on the MSME segment. However, the current recession is leading to a shortfall in the resources needed to finance the recovery plans of these production units. Despite their importance for the economy,<sup>95</sup> MSMEs have traditionally been underserved by the banking system: just 29% have credit lines or loans, 18% consider it difficult to obtain credit, and 36% consider it very difficult. Moreover, access gaps exist depending on rurality, income level, and gender. The penetration of accounts in rural areas is equivalent to 83% of that of urban areas and to 48% of the poorest population segment, and just 81 women have a bank credit for every 100 men. As many as 60% of small businesses report that they are underserved by the financial sector, a percentage that rises to 67% in the case of women-owned companies. Against this backdrop, a process of economic revival in the short term, and sustainable diversification in the medium term, requires **better access to credit** so as to finance MSMEs' recovery plans and investments geared to adopting more modern technologies and more productive business models with better resilience to events such as COVID-19, climate change, and natural disasters, as well as to foster growth of higher value-added productive activities. In this sector, the country has soundly managed financing institutions with a strong track record through which progress may be made on targeting resources based on specific development and economic recovery objectives, with measurable outputs and outcomes, that will enable the impact of the financing to be measured.
- 3.23 The poor performance of El Salvador's infrastructure and logistics sector significantly raises the costs of domestic production and limits the ability to take advantage of regional and international markets and the country's economic growth.<sup>96</sup> In **transportation**, challenges exist in terms of quality, connectivity, capacity, and resilience to climate impacts. Additionally, this sector generates 30% of greenhouse gas emissions. As much as 40% of the national highway system is unpaved and 62% of paved roads are in poor or fair condition. This, in conjunction with cumbersome customs procedures, results in poor logistics performance<sup>97</sup> that adds to the cost of doing business and affects competitiveness, productivity, and

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<sup>95</sup> The latest economic census, in 2005, estimated that MSMEs represented 99.5% of all companies, employed 65.5% of active workers, and created 42.7% of value added.

<sup>96</sup> Increasing investments in improvements to productivity, efficiency, and quality of infrastructure services by 5% over current levels could stimulate regional growth in Latin America and the Caribbean by 3.5% of GDP over the next 10 years. IDB, Development in the Americas (DIA) 2020. According to the [Plan Maestro de Infraestructura de El Salvador](#) [Infrastructure master plan for El Salvador], El Salvador would require investments of US\$1.613 billion over the next five years to raise potential growth by one additional percentage point.

<sup>97</sup> El Salvador scored 2.58 on the World Bank's Logistics Performance Index (LPI) in 2018, below the Latin American and Caribbean region (2.66) and Central American (2.69) averages. The main obstacles are identified as poor quality transportation infrastructure and inefficiencies in customs processes.

utilization of the regional market.<sup>98</sup> Improving infrastructure, and the trade entry and exit points, particularly strengthening customs posts, would help facilitate trade and economic recovery. The processes of improving border crossings, based on the coordinated border management model already being applied by other countries of the region,<sup>99</sup> use predictive and risk analysis tools to bolster tax revenue and trade integrity, thereby improving the efficiency of operating expenses associated with the control, security, and management of border posts. Growing urbanization and the country's vulnerability to natural disasters<sup>100</sup> present additional challenges to the development of resilient and inclusive infrastructure.<sup>101</sup> To overcome these challenges, the country's persistently low<sup>102</sup> levels of investment will need to be increased and substantial improvements made to investment planning, based on clear prioritization criteria, accompanied by policies and practices for the execution of works that foster competition, ensure transparency, and reduce the risk of cost overruns and extension of execution periods that impact investment effectiveness.

- 3.24 Access gaps in **water and sanitation** need to be bridged in order to improve the population's quality of life and to enable investments in productive sectors such as tourism and agriculture without compromising service reliability in urban and rural centers. Improving access is particularly important in rural areas, where more than 600,000 of the country's inhabitants (27% of the rural population) lacks a drinking water service, and 24% of businesses report having been affected by shortcomings in water distribution,<sup>103</sup> as well as in municipios reliant on tourism, where an increase in residential demand is expected, boosted by the eventual recovery and growth in tourism activity. Additionally, 48% of supply has been classed as intermittent and 50% of the population reports deficiencies in the quality of the water supplied. Climate vulnerability jeopardizes drinking water supplies and it is estimated that by 2100 the amount of drinking water available per capita will have declined by as much as 93%.
- 3.25 The water shortage is one of the most serious risks El Salvador faces, and it is being exacerbated both by population growth and the loss of woodland cover, particularly coffee forest. This woodland, which comprises high-diversity

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<sup>98</sup> The countries of the subregion as a whole are El Salvador's second largest trading partner after the United States, with exports of around 45.1% of foreign sales in 2019 and imports of 21%. [Informe Centroamericano. Un modelo de integración en evolución](#). Instituto para la Integración de América Latina y el Caribe (INTAL), IDB. March 2021.

<sup>99</sup> With IDB support, Nicaragua, Costa Rica, and Panama are implementing programs to modernize infrastructure, processes, and technology, not just to facilitate trade and improve logistics performance, but also to increase their trading capacity and leverage the process of integration.

<sup>100</sup> In El Salvador, 88% of the land area and 95% of the population are exposed to hydrometeorological or geophysical risks. United Nations Disaster Assessment and Coordination (UNDAC).

<sup>101</sup> El Salvador's urbanization rate has been rising rapidly, climbing from 59% in 2000 to 71% in 2017 (World Development Indicators (WDI), 2018). However, quality standards of urban transportation service operations are low. The San Salvador Metropolitan Area, which generates 33% of the country's GDP and 66% of its earnings, has witnessed rising rates of car ownership and congestion, leading to delays of approximately 364 hours per traveler per year, at an estimated cost of 1% of the region's GDP. IDB (2021) Congestión urbana en América Latina y el Caribe: características, costos y medidas de mitigación (in preparation).

<sup>102</sup> Infrastructure investment in El Salvador between 2008 and 2015 averaged 1.8% of GDP, considerably lower than the Latin American and Caribbean regional average (around 3.5% of GDP). [InfraLatam](#).

<sup>103</sup> As estimated by the 2016 World Bank Business Survey.

agroforestry systems, represents 22% of the country's forested areas and is the main cover in watersheds, as well as an important source of income for rural workers.<sup>104</sup> Against this backdrop, it is key to link actions to recover and protect forest cover in critical sites to safeguard water supplies, particularly in densely populated areas, as well as to foster adaptation toward activities that expand this forest cover.

- 3.26 Meanwhile, over 95% of domestic wastewater is discharged entirely untreated and infrastructure is deficient.<sup>105</sup> According to the National Drinking Water and Sanitation Plan (PNAPS),<sup>106</sup> investments of over US\$12 billion will be required in order to achieve universal access to the service. This is beyond the sector's capacity given the inadequate rate framework, which makes it impossible to generate a reliable revenue stream, deficiencies in the regulatory framework, energy efficiency problems deriving from the use of obsolete and/or poorly designed equipment with negative impacts on institutional finances, and the disjointed regulatory framework, which takes a fragmentary approach to the sector.
- 3.27 The possibilities for progress on digital transformation and for leveraging the contribution of information and communication technologies (ICTs) to boost service productivity, inclusion, and quality<sup>107</sup> are seriously constrained by various factors,<sup>108</sup> including the population's limited **connectivity**. Just 32% of the country has fourth generation (4G) network coverage (compared with 67% in the Latin American and Caribbean region). Access to mobile broadband stands at 56%, compared with 65% in the region as a whole.<sup>109</sup> El Salvador is also below the regional average on other indicators such as average fixed broadband and mobile network access speeds. Additionally, the development of e-government and the level of maturity of cybersecurity in El Salvador falls short of the regional averages,<sup>110</sup> which represents a broad opportunity to leverage efficiency and transparency gains that may derive from ICT adoption in the public sector. Investments to bridge these gaps will facilitate the expansion of digital commerce and higher value-added services sectors, such as fintech, digital consumption, business process outsourcing, call centers,<sup>111</sup> and other knowledge-based services. The COVID-19 pandemic has shown that connectivity and technology adoption are also key to promoting job stability in some sectors, equitable access to basic services, such as health and education, and continuity of general citizen

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<sup>104</sup> Additionally, coffee is the country's most important agricultural product and a driver of economic activity: in 2016 it accounted for 5.5% of agricultural production, 30% of salaried employment in agriculture, and 26% of agribusiness employment (FAOSTAT, 2016). Women make up 44.2% of forest producers, including agroforestry coffee (EHPM, 2015).

<sup>105</sup> See Annex I, CDC.

<sup>106</sup> National Water and Sewer Authority (ANDA), 2018.

<sup>107</sup> According to the World Economic Forum, the adoption of ICTs is one of the areas where El Salvador is in a relatively weak position, ranking 105th out of 141 countries. The widest gap is observed in the percentage of the adult population that uses the Internet, which stands at 33.8% compared with 50% for Central America, and 59% for Latin America.

<sup>108</sup> Highlighting the absence of adequate institutional governance, an updated regulatory framework, and digital talent.

<sup>109</sup> [Indicadores de infraestructura y conectividad digital](#). IDB (2019).

<sup>110</sup> [Cybersecurity. Risks, Progress, and the Way Forward in Latin America and the Caribbean](#). IDB (2020).

<sup>111</sup> Known in Spanish as *subcontratación de procesos empresariales* and *centros de llamadas*, respectively.

- support services through e-government.<sup>112</sup> Apart from the resilient and low-emissions infrastructure to support this transformation, this process will require regulations and standards enabling access and widespread, secure use of these services, in order to safeguard information integrity and reliability.<sup>113</sup>
- 3.28 To support El Salvador's sustainable economic revival and promote a resilient restructuring of production, through the current portfolio and new financial and nonfinancial activities, the IDB Group will back initiatives to facilitate access to finance for investment and financial inclusion, the development of infrastructure, and digital transformation. The Bank intends to continue the work begun in the preceding strategy on *access to finance* and *financial inclusion*, with IDB and IDB Invest<sup>114</sup> portfolio operations. This effort has been stepped up in response to COVID-19 to ease the tighter lending conditions faced by smaller businesses and other segments with limited access to finance, strengthening beneficiary targeting and identification processes based on clear policy objectives and criteria. This will be complemented with additional IDB Invest actions to finance the growth of high value-added ICT services companies, as well as to enable financial institutions to adopt portfolio exposure hedging instruments and enhance credit technology. The development of the fintech industry will be explored from both the public regulatory angle and that of options for expanding financial services to reach underserved sectors.
- 3.29 In *infrastructure*, priority will be given to raising the quality, coverage, and efficiency of transportation and logistics, and water and sanitation services in a way that is inclusive, resilient, and low in emissions, so as to boost producers' competitiveness, facilitate trade, and improve the population's living conditions, while contributing to the sustainable development of key sectors for job creation and household incomes, such as tourism and agriculture. These initiatives will be complemented by ongoing IDB Group activities to boost coffee forest productivity and resilience to climate change.<sup>115</sup> In view of the fiscal constraints, the Bank will explore with El Salvador the options for structuring projects that envisage private involvement in infrastructure development.
- 3.30 The IDB Group will also seek to support the digital transformation through new interventions to expand *connectivity* and facilitate the adoption of information and communication technologies in both the public and private sectors. It will seek to strengthen the enabling framework for the digital transformation, including

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<sup>112</sup> According to the diagnostic assessment conducted by the Technical and Planning Secretariat (SETEPLAN) and the IDB, just 31% of formalities are available to be carried out online, and very few of them can be completed over the web. In addition, only 52% of government agencies' processes are connected with other institutions.

<sup>113</sup> To achieve a sustainable digital transformation, it is also necessary to strengthen the country's capabilities in cybersecurity, including enhancing the SaCERT incident response team, cybernetic protection of digital assets and critical infrastructure, training staff in cybersecurity, and strengthening national strategies and governance on the issue.

<sup>114</sup> Includes seven IDB Invest transactions with an exposure of US\$124.5 million in financial market support.

<sup>115</sup> The project "Strengthening the Climate Change Resilience of El Salvador's Coffee Forests" (operation ES-L1135) has the objectives of maintaining the ecosystem services provided by coffee forests and improving food security for small-scale coffee producers through the adoption of climate-smart agricultural technologies; incentives for marketing and cooperative initiatives; and modernization of coffee sector governance.

- governance and institutional structure, digital talent, and shared horizontal services such as cybersecurity, data, and interoperability, digital identity, the cloud, and digital finance. Taken together, these measures will help increase efficiency, productivity, and the visibility and traceability of transactions, reducing operating costs and improving the quality of controls.
- 3.31 **Dialogue areas.** The IDB Group will maintain a dialogue with El Salvador, contributing its technical knowledge and good practices to support the identification of medium-term priorities for investment and policy frameworks in the areas of public management and governance, citizen security, trade facilitation, and attracting investments in specific sectors such as tourism, agriculture, energy, and migration. Given the importance of **public management and governance** considerations in boosting levels of investment and generating higher and more inclusive growth over the medium and long term, the IDB Group will seek to provide the country with technical and operational knowledge on good practices in areas including public service management, civil service, corruption control and transparency. Considering the impact of crime on the business climate and the well-being of the population and the risk that this problem may be exacerbated by the pandemic, under the heading of **citizen security** the Bank will seek to evaluate options for crime prevention and reconstruction of the social fabric in coordination with other donors that are leading activities in the sector.<sup>116</sup> A dialogue will also be maintained to advance the knowledge agenda on the issue of **outmigration, return migration and remittances**, which are key factors in the living conditions of many Salvadoran households and represent a source of social vulnerability.
- 3.32 **Trade facilitation** and the **framework for promoting investments** will be included on the dialogue agenda to evaluate additional steps to promote simplification and regulatory enhancement, and to strengthen the business climate, regional trade, and the diversification of production into higher value-added sectors. In **tourism**, the Bank will continue the dialogue underway with the authorities to identify priority actions at the institutional level and specific investments to strengthen the sustainability of the sector, and its impact on quality of life, income, and jobs in local economies. In **agriculture**, the existing portfolio supports bolstering the resilience of coffee forests, such that the dialogue will focus on structuring a medium-term strategy to enhance the provision of public and private agricultural services, as well as private sector initiatives to boost the sector's productivity and competitiveness. In **energy**, there is also a portfolio supporting improvements in companies' energy efficiency via credit lines through the financial system, such that the dialogue will seek to develop policy options and investment opportunities for diversification into renewable energy sources and improvements to the efficiency of the energy matrix. IDB Invest will aim to contribute to these areas, particularly in the sustainable development of the agricultural sector, trade facilitation, renewable energies, and the efficiency of the energy matrix.
- 3.33 **Crosscutting themes.** This strategy includes gender equality and diversity, and climate change and environmental sustainability and natural disasters, as well as

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<sup>116</sup> The Central American Bank for Economic Integration (CABEI) is supporting two programs under the "Territorial Control Plan" to combat crime: the program to modernize the institutions responsible for public safety and the social development program (pending legislative approval).

institutional capacity and the rule of law as crosscutting themes. It will include measures to enhance the relevance of gender and diversity issues, especially in the areas of education, health, housing, and access to finance. The IDB Group will seek to support progress toward the country's nationally determined contribution (NDC)<sup>117</sup> and strengthen its natural disaster risk management through resilient and low emissions productive and social infrastructure, private sector financing based on sustainability criteria, and forest management to safeguard water resources. During implementation, the IDB Group will continue to identify opportunities to support the country on topics of institutional capacity, transparency, corruption control, and governance in the priority sectors identified in the strategy.

#### IV. PROJECTED FINANCIAL SCENARIO

- 4.1 According to the Ministry of Finance's fiscal projections, the gross financing requirement<sup>118</sup> of the nonfinancial public sector will be between 9% and 14% of GDP over the period 2021-2024. This will mainly be met from external loans, a large share of which is expected to come from multilateral organizations, consistent with the objective of stabilizing debt over the medium term.
- 4.2 In this context, and subject to the Bank's Ordinary Capital resource allocation exercises, annual approvals and disbursements of sovereign guaranteed loans are projected to come to US\$325 million and US\$343 million, respectively. The Bank's sovereign guaranteed lending over the period 2021-2024 is projected to come to US\$1.3 billion in new approvals and US\$1.371 billion in total disbursements. Under this scenario, the Bank's exposure will reach 10% of the country's total public debt, 22% of its external public debt, and 50% of its multilateral debt by the end of the strategy period (see Annex III).

#### V. IMPLEMENTATION CONSIDERATIONS

- 5.1 **Donor coordination.** Donor coordination was stepped up during the crisis in order to identify challenges and coordinate a relevant and timely response to the country's needs. In line with OVE's recommendations, this coordination and prioritization effort will be a core component of implementation, bearing in mind the limited fiscal space. The crisis has had a significant impact on the country's financing requirements and will continue to motivate close coordination among the main multilaterals to provide support on a scale allowing the authorities to mitigate the impact of the shock on businesses, employment, and poverty, and to return to the path of growth. The Bank will continue to coordinate with the IMF, the Central American Bank for Economic Integration (CABEI), and the World Bank to exchange information on the progress of each organization's programs and activities, review progress toward legislative ratification of operations, and coordinate the sequencing and complementarity of the interventions. Meetings

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<sup>117</sup> In its NDC, El Salvador has prioritized climate change mitigation and adaptation measures in land-use changes, energy, agriculture, water resources, infrastructure, and health. Its investment needs are estimated at around US\$2.090 billion (2018-2030) (Ministry of Agriculture and Natural Resources (MARN), 2018).

<sup>118</sup> This includes fiscal deficit financing after grants and payment of amortizations of domestic and external public debt.

have also been held with the Japan International Cooperation Agency (JICA) and the European Union to explore possible project cofinancing, and with the United Nations Development Programme (UNDP) to coordinate social sector support actions.

- 5.2 **Portfolio execution.** Work in coordination between the government and the Bank enabled substantial improvements in portfolio execution, which led to positive net flows for the country. This coordination effort will be stepped up during the pandemic and post-COVID-19 period so that IDB-financed projects achieve timely outcomes and contribute to the recovery. The amounts available in projects to address fiscal, health, education, access to finance, and climate change adaptation challenges are an invaluable starting point for maintaining the course of action on medium-term challenges and contributing to the strategic objectives agreed with the authorities for the years ahead (Annex I.1).
- 5.3 **Flexibility of the program to changes in the environment.** The uncertain context over the next few years will call for flexibility in the IDB Group's lending program and technical assistance resources to respond effectively to the changing conditions the country faces and support substantive dialogue enabling relevant solutions to be developed in various sectors. The IDB Group's contribution should be evaluated in light of this changing context, considering the instruments available in the public and private windows, the active portfolio, and the technical cooperation program.
- 5.4 **Country oversight and control systems.** As regards the use of country systems, fiduciary oversight currently relies wholly or partly on the budget, treasury management, accounting and reporting, internal control, external control, information system, and shopping subsystems. Diagnostic assessments applying international best practices, such as the Public Expenditure and Financial Accountability (PEFA)<sup>119</sup> and Methodology for Assessing Procurement Systems (MAPS)<sup>120</sup> enabled the identification of opportunities to enhance the subsystems mentioned to strengthen their contribution to accountability, transparency, and integrity in the public sector. On this basis, the main interventions envisaged for the strategy period aim to increase competition, efficiency, and traceability and independence of the systems. These actions include: (i) strengthening internal and external control by training personnel and improving manuals and systems at the State Audit Office (CCR); (ii) adapting international public sector accounting standards to strengthen accounting and reporting functions; (iii) promoting the positioning of the government procurement unit (UNAC) as the country's lead agency for procurement;<sup>121</sup> and (iv) strengthening El Salvador's electronic public procurement system (COMPRASAL).<sup>122</sup>

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<sup>119</sup> This program provides a standard framework for the evaluation of the strengths and weaknesses of public financial management systems, which are essential to support the objectives of macroeconomic stability, efficient resource allocation, and transparency of public finances.

<sup>120</sup> This is an international standard and universal tool for evaluating public procurement systems that contributes to the effectiveness and efficiency of public procurement and to the integrity and transparency of the use of public funds.

<sup>121</sup> For further details see Annex I Results Matrix and Country Systems Matrix.

<sup>122</sup> For more details of actions, see the Fiduciary technical note link available at the start of this document.

- 5.5 **Country environmental and social governance systems.** El Salvador faces challenges relative to other countries in Latin America in terms of regulation and compliance with environmental legislation, environmental practices, and institutional capacity in the sector (measured in terms of per capita environmental spending).<sup>123</sup> The IDB Group will work with the country to strengthen its environmental and social system to promote improvements in the following areas: (i) the environmental authorities' budgetary allocation and flow; (ii) civic participation and complaint resolution mechanisms; and (iii) compilation and management of environmental and social data.
- 5.6 **Synergies between the IDB Group's institutions.** To improve public-private coordination and maximize the impact of the IDB Group's operations as a long-term partner in El Salvador's development, the IDB, IDB Invest, and IDB Lab will continue to promote coordinated work agendas to create an environment conducive to attracting investments that contribute to a more sustainable and inclusive economic development process. Four areas identified where stronger coordination will be sought are SME financing and resilience; strengthening enabling conditions to attract more investment; evaluation of mechanisms such as public-private partnerships, especially in the transportation and energy sectors; and more explicit consideration of transparency and integrity risks in the public- and private-sector dialogue, as well as in the specific interventions of each window.

**Table 1. Country systems**

Country systems	Level of use		Expected actions during the country strategy
	Number of projects (%)		
	2021 baseline	Estimated use 2024	
Budget	100%	100%	• Monitoring and evaluation for continued use
Treasury management	100%	100%	• Monitoring and evaluation for continued use
Accounting and reporting	100%	100%	• Close the gap with international standards/best practices
Internal audit	0%	0%	• No action planned
External control	10%	10%	• Fiduciary evaluation • Strengthening country system
Information system	100%	100%	• Monitoring and evaluation for continued use
Shopping	70%	100%	• Monitoring and evaluation for continued use
Advanced national competitive bidding	0%	0%	No action planned
Partial national competitive bidding	0%	30%	• Close the gap with international standards/best practices • Fiduciary evaluation
Consulting services	0%	20%	• Close the gap with international standards/best practices • Fiduciary evaluation

## VI. RISKS

- 6.1 **Macroeconomic and fiscal situation.** The uncertainty surrounding El Salvador's prospects for recovery owing to the global impact of the pandemic, and its capacity to access finance under conditions consistent with fiscal sustainability, poses risks

<sup>123</sup> [Environmental Governance Indicators for Latin America & the Caribbean](#). IDB (2020).

to the scope and depth of the actions proposed in this strategy. A prolongation of the effects of the pandemic would mean policy efforts to mitigate the impacts of the crisis would remain in place, limiting the scope for efforts to spur the revival and could entail ongoing deterioration in sustainability indicators resulting in significant adjustments in investment spending over the next few years. Similarly, prolonged negotiations on an agreement with the IMF pose significant challenges to financing the deficit, stabilizing debt levels, and the Bank's potential financial support. To mitigate these risks, the Bank will work with the government in the areas of tax collection and efficiency and managing spending while closely monitoring trends in the main indicators using the macroeconomic safeguard mechanisms currently in effect, with a view to identifying corrective actions in a timely manner. The Bank will also continue to coordinate closely with other multilateral institutions to ensure programs are consistent and synergistic with reform needs and investment prioritization in the context of the potential adjustments that may be required depending on how the macroeconomic context develops. The Bank will monitor progress in COVID-19 vaccine administration in the country, identifying actions that can support the government in this process. In terms of external factors, the strong recovery of the U.S. economy projected for 2021 and 2022 is a factor that will favor the recovery of growth in El Salvador over this period. At the same time, changes in the monetary system and the trajectory of oil prices are considerations to bear in mind in the analysis of the country's financial and monetary stability. The Bank will therefore monitor the implementation of the recent monetary reform and evolution of the price of crude oil.

- 6.2 **Political context.** The recent legislative elections have yielded a new legislative assembly in which the executive branch has the support of a qualified majority, enabling it to speed up the approval of loans. Although the new context reduces the risk of the legislative delays that have characterized previous strategy cycles, it could lead to changing perceptions of the risks of the environment for accountability in State institutions and the effectiveness of the mechanisms available to foster participation among diverse segments of the population. Against this backdrop, the administration has committed itself to the proper functioning of the country's institutions and the rule of law. The Bank will continue to facilitate the dialogue between different actors in society, providing technical analysis of reform proposals and investment initiatives in close coordination with other donors.
- 6.3 **Execution.** The measures to address the COVID-19 health crisis have created major challenges for the execution of the Bank's operations, which will demand that executing agencies be better able to adapt and respond to emerging problems. To mitigate this risk the Bank will undertake strengthening and training activities for counterparts that include the lessons learned during the period, as well as making strategic use of technical cooperation to support the development of execution mechanisms tailored to local capabilities.
- 6.4 **Natural disasters and climate change.** El Salvador is exposed to a variety of natural hazards with far reaching economic and social consequences. The occurrence of a significant event could shift the country's priorities and narrow its options for post-pandemic recovery. The IDB Group will seek to mitigate these risks by making the Bank's mechanisms and instruments available to the authorities to address these phenomena and by incorporating factors that promote

disaster risk management and prevention in the discussion of the various operations. In addition, the strategy areas emphasize climate change adaptation considerations to reduce vulnerability to this phenomenon.

## ANNEX I: RESULTS MATRIX AND COUNTRY SYSTEM MATRIX

### 1. Results Matrix

Government priority	Country strategy priority areas	IDB strategic objective	Expected Outcomes	Indicators	Baseline (source and year)	
Economic recovery	Efficiency and fiscal sustainability	Strengthen tax collection	Increased tax revenue through administrative and policy measures	% tax revenue/GDP	18.3% (2020, Ministry of Finance)	
		Reduce public expenditure inefficiencies	Improved efficiency and equity of spending	% of electricity and liquefied petroleum gas subsidies received by the 7th to 10th income distribution deciles.	31.2% electricity and 37.8% gas (2018) <sup>1</sup>	
Social welfare	Reducing social vulnerability	Improve education coverage and relevance	Increased coverage of preschool education services	Net preschool attendance rate	53.7% (2018, Education statistics portal (CIMA))	
			Better education options to support young people's workforce integration	Young beneficiaries on accelerated and blended learning programs with a new life-skills module. <sup>2</sup>	Men: 0 Women: 0 (2020, Education management information system (SIGES))	
		Improve the coverage, quality, and efficiency of all levels of the health system	Stronger health system	Infant mortality rate in the San Salvador Department		9.2% (2017, Morbidity/mortality information system (SIMMOW))
				Coverage of prenatal care prior to the 12th week of pregnancy at national level		74.6% (SIMMOW, 2017)
		Facilities reporting their production information by electronic means in the prioritized municipios <sup>3</sup>		41 (2017, SIMMOW)		

<sup>1</sup> Source: "Subsidios Económicos en El Salvador. Costo Fiscal e Impacto Distributivo" (Tornarolli, 2019).

<sup>2</sup> This indicator was adopted as an approximation in view of the limitations on measuring the employability of the young people trained.

<sup>3</sup> Chalchuapa, Suchitoto, Cojutepeque, Santiago de María, Jiquilisco, Nueva Guadalupe, San Francisco Gotera, La Unión.

Government priority	Country strategy priority areas	IDB strategic objective	Expected Outcomes	Indicators	Baseline (source and year)	
		Increase financing for access to housing in vulnerable segments.	Improved housing conditions for vulnerable populations	Number of vulnerable households <sup>4</sup> benefiting from mortgage lending for low-income housing	2,500 (2020, Social Housing Fund (FSV))	
				Percentage of mortgage lending in the low-income housing segment issued to women	10% (2020, FSV)	
Economic recovery	Reactivation and restructuring of production	Facilitate access to finance for MSMEs	More MSMEs accessing credit	Proportion of medium-term credit to MSMEs (more than 12 months) in the MSME portfolio	58.6% (2020, Development Bank of El Salvador (BANDESAL)) <sup>5</sup>	
				Proportion of medium-term credit to women-owned MSMEs (more than 12 months) in the medium-term MSME portfolio	15.5% (2020, BANDESAL) <sup>6</sup>	
				Percentage of MSMEs in El Salvador operating in the rural sector that have access to credit.	1.5% (2018, National micro and small enterprise commission (CONAMYPE)) <sup>7</sup>	
			Recovery and revitalization of finance to higher value-added productive sectors	Year-on-year growth rate of commercial bank lending catering to nontraditional manufacturing activities	0.03% (2020/2019, Financial System Superintendency (SSF)) <sup>8</sup>	
			Develop inclusive and sustainable infrastructure services	Better quality infrastructure	Infrastructure quality, Global Competitiveness Index	61/100 (2019, World Economic Forum (WEF))
				Forest coverage preserved to safeguard ecosystem services	Land area in the country with natural forest cover	624,376 hectares or 29.6% of the country's land area (2018, Ministry of Agriculture and Natural Resources (MARN))

<sup>4</sup> Harmonized World Bank and IDB classification. Refers to population on an income of less than \$12.5 a day, based on: Ferreira, F. H., J. Messina, J. Rigolini, L. F. López-Calva, M. A. Lugo, R. Vakis, and L. F. Ló. 2012. Economic Mobility and the Rise of the Latin American Middle Class. Washington, D.C.: World Bank.

<sup>5</sup> The baseline uses the calculation of the balance of BANDESAL's MSME-finance portfolio as of 31 March 2020.

<sup>6</sup> The baseline uses the data on the proportion of women-owned MSMEs in the balance of BANDESAL's portfolio of finance for MSMEs' working capital and fixed asset investments as of 31 March 2020.

<sup>7</sup> Baseline with information available from the 2017 national survey of micro and small enterprises conducted by CONAMYPE.

<sup>8</sup> This indicator is a proxy built using official data published by the SSF. It is therefore straightforward to calculate and based on regularly updated data.

Government priority	Country strategy priority areas	IDB strategic objective	Expected Outcomes	Indicators	Baseline (source and year)
			Limited greenhouse gas emissions growth	CO <sub>2</sub> emissions (metric tons per capita)	1.1 (2016, World Development Indicators (WDI))
		Increase digital connectivity	More adoption of information and communications technologies	Percentage of adult population using the Internet	33.8% (2019, WEF)

## 2. Country Systems Matrix

Strategic objective	Expected outcome	Indicator	Unit of measure	Baseline	Baseline year	Main objective	Time distribution	Alignment with Corporate Results Framework
Increase use of country systems	Increased use of the shopping subsystem	Active portfolio using the shopping subsystem	Percentage of active portfolio	70%	2020	100%	At the end of the country strategy	- Institutional capacity and the rule of law - Productivity and innovation - Social inclusion and equality
	Increased use of the individual consulting subsystem	Active portfolio using individual consulting subsystem	Percentage of active portfolio	0%	2020	20%	At the end of the country strategy	- Institutional capacity and rule of law - Productivity and innovation - Social inclusion and equality
	Increased use of the partial national competitive bidding (NCB) subsystem	Active portfolio using the partial NCB subsystem	Percentage of active portfolio	0%	2020	30%	At the end of the country strategy	- Institutional capacity and the rule of law - Productivity and innovation - Social inclusion and equality
Strengthen country systems	Implementation of the Supreme Audit Institution – Performance Measurement Framework (SAI-PMF) action plan	SAI-PMF final evaluation report	SAI-PMF report	0%	2020	50%	At the end of the country strategy	- Institutional capacity and the rule of law - Productivity and innovation
	Implementation of action plan for adoption of International Public Sector Accounting Standards (IPSAS)	Progress on implementation of the action plan.	% progress on plan implementation	25%	2020	50%	At the end of the country strategy	- Institutional capacity and the rule of law - Productivity and innovation

Strategic objective	Expected outcome	Indicator	Unit of measure	Baseline	Baseline year	Main objective	Time distribution	Alignment with Corporate Results Framework
	Implementation of action plan resulting from the Methodology for Assessing Procurement Systems (MAPS) evaluation	Progress on implementation of the action plan.	% progress on plan implementation	0%	2020	40%	At the end of the country strategy	- Institutional capacity and the rule of law - Productivity and innovation - Social inclusion and equality
	The government procurement unit (UNAC) given support to make adjustments to the Integrated Procurement System (SIAC) and the Public Procurement Law.	Consulting services supporting the proposed Procurement Law	Consulting services	0	2020	2	At the end of the country strategy	- Institutional capacity and the rule of law - Productivity and innovation
	The UNAC given support on the use of the transactional public competitive bidding module to conduct the procurement of works, goods, and services electronically	Number of consulting services completed	Consulting services	0	2020	2	At the end of the country strategy	- Institutional capacity and the rule of law - Productivity and innovation
	Support on implementation of the mandatory master supplier registry	Consultant to implement the master supplier registry	Consulting services	0	2020	1	At the end of the country strategy	- Institutional capacity and the rule of law - Productivity and innovation

## ANNEX II: MAIN SOCIOECONOMIC INDICATORS

	2014	2015	2016	2017	2018	2019	2020
<b>Economic performance and inflation</b>							
Nominal GDP ( $\Delta\%$ )/b	2.7	3.7	3.2	3.3	4.6	3.5	-8.3
Real GDP (ref. year 2014) ( $\Delta\%$ )/b	1.7	2.4	2.5	2.2	2.4	2.4	-9.0
Consumer price inflation (%) (end of period)	0.5	1.0	-0.9	2.0	0.4	0.0	-0.1
<b>Credit</b>							
Credit to the private sector ( $\Delta\%$ )	5.6	4.7	5.4	4.8	6.1	5.8	1.5
Average borrowing rate (1 year)	3.9	4.5	4.6	4.7	4.6	4.6	4.4
Average lending rate (< 1 year)	6.0	6.2	6.4	6.5	6.6	6.6	6.8
<b>Savings and investment</b>							
Gross domestic investment (% of GDP)/b	16.4	16.0	16.0	16.7	20.3	19.1	13.3
Gross national savings (% of GDP)/b	11.0	12.8	13.7	14.8	15.6	17.0	9.9
<b>External sector</b>							
Current account balance (% of GDP)/b	-5.4	-3.2	-2.3	-1.9	-4.7	-2.1	-4.9
Net foreign direct investment (% of GDP)/b	1.4	1.7	1.4	3.2	3.2	2.4	1.5
Real effective exchange rate (2000=100)	97.6	96.3	98.5	100.2	100.7	104.8	105.3
Public external debt (% of GDP)	37.3	35.5	35.0	36.8	35.3	35.6	42.5
<b>Nonfinancial public sector (NFPS)</b>							
Total revenue (% of GDP)	21.9	21.9	22.1	22.8	23.0	22.8	22.7
Total spending (% of GDP)/a	26.0	25.5	25.2	25.3	25.6	25.8	31.3
Overall balance (% of GDP)/a	-4.0	-3.6	-3.1	-2.5	-2.6	-3.1	-9.7
NFPS debt (% of GDP)/a	64.6	66.2	67.5	69.2	69.2	69.9	85.8
<b>Memorandum</b>							
GDP (US\$ billions)/b	22.6	23.4	24.2	25.0	26.1	27.0	25.2

Source: Ministry of Finance and Central Reserve Bank of El Salvador (BCR) (February 2021), World Economic Outlook (October 2020).

a/ Includes trust fund and pension debt.

b/ Year-end estimates. US\$: United States dollars.

### ANNEX III: ESTIMATED FINANCIAL SCENARIO FOR SOVEREIGN DEBT 2021-2024

US\$ million

	2015-2019 Strategy*							2021-2024 Strategy				
	2015	2016	2017	2018	2019	2020**	Total 2015-2020	2021	2022	2023	2024	Total 2021-2024
<b>Approvals</b>	<b>200.0</b>	<b>30.0</b>	<b>-</b>	<b>370.0</b>	<b>245.0</b>	<b>870.0</b>	<b>1715.0</b>	<b>400.0</b>	<b>250.0</b>	<b>325.0</b>	<b>325.0</b>	<b>1,300.0</b>
<b>Disbursements</b>	<b>50.8</b>	<b>80.7</b>	<b>70.1</b>	<b>389.5</b>	<b>238.2</b>	<b>288.8</b>	<b>1118.1</b>	<b>350.5</b>	<b>433.4</b>	<b>172.2</b>	<b>415.3</b>	<b>1,371.3</b>
Repayments	34.2	159.6	164.8	161.7	164.8	185.7	870.7	156.6	152.4	162.9	169.3	641.2
Subscriptions and contributions	15.1	0.2	2.1	0.2	-		17.6					-
<b>Net lending flow</b>	<b>1.5</b>	<b>(79.1)</b>	<b>(96.7)</b>	<b>227.6</b>	<b>73.4</b>	<b>103.1</b>	<b>229.8</b>	193.9	281.0	9.3	246.0	<b>730.1</b>
Interest and fee payments	12.9	54.8	52.1	65.5	73.2	57.4	315.9	57.9	52.6	47.5	41.9	199.9
<b>Net cash flow</b>	<b>(11.3)</b>	<b>(133.9)</b>	<b>(148.9)</b>	<b>162.1</b>	<b>0.2</b>	<b>45.7</b>	<b>(86.1)</b>	<b>136.0</b>	<b>228.4</b>	<b>(38.2)</b>	<b>201.1</b>	<b>530.3</b>

IDB debt	2,050.7	1926.6	1805.3	2028.4	2212.0	2315.1
Debt with IDB/debt with multilaterals (%)	57.5%	54.8%	50.5%	53.3%	59.8%	62.6%
IDB debt/external debt (%)	24.6%	22.7%	19.6%	22.0%	21.6%	20.0%
IDB debt/total govt. debt (%)	13.2%	11.8%	10.4%	11.2%	11.6%	10.7%

2509.0	2789.9	2799.2	3045.2
58.4%	57.0%	51.0%	50.1%
20.4%	21.5%	20.9%	22.1%
10.4%	10.7%	9.9%	10.0%

\* The country strategy transition was due in 2020. However, the government requested an extension and the existing strategy remained in effect until 30 June 2021.

\*\* The response to COVID-19 is reflected in 2020.

## ANNEX IV: DEVELOPMENT EFFECTIVENESS MATRIX (SUMMARY)

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

### COUNTRY STRATEGY: El Salvador

#### STRATEGIC ALIGNMENT

*Refers to the degree to which the design and objectives of the CS are consistent with the country development challenges and with the government’s development plans and priorities.*

#### EFFECTIVENESS

*This measures whether the country strategy is likely to achieve its intended objectives, through an examination of three dimensions: (i) the quality of the diagnostics on which Bank action is based in each area of work; (ii) the quality of the results matrix for the strategy; (iii) the use and buildup of country systems.*

Effectiveness dimensions	
I. Country Diagnosis - Country Development Challenges (CDC)*	Yes/No
- The CDC is comprehensive / holistic / complete	Yes
- The CDC clearly identifies the main development challenges	Yes
- The CDC presents magnitudes of the main development challenges that are based on empirical evidence	Yes
II. Priority Areas Diagnostics	%
- That clearly identify and dimension, based on empirical evidence, the <b>priority area’s</b> specific constraints and challenges	100%
- That clearly identify and dimension, based on empirical evidence, the <b>main factors</b> or causes contributing to the specific constraints and challenges	100%
- That provide corresponding <b>policy recommendations</b>	100%
III. Results matrix**	%
- The strategic objectives are clearly defined	100%
- The expected outcomes are clearly defined	100%
- The strategic objectives and expected results that are directly related to the main constraints identified in the Diagnosis	100%
- The indicators are outcome indicators and are SMART	100%
- The indicators have baselines	100%
IV. Vertical logic	Yes/No
- The CS has vertical logic	Yes

## ANNEX V: OVE COUNTRY PROGRAM EVALUATION RECOMMENDATIONS

### Management's response to the Recommendations of the Evaluation of the EI Salvador Country Program 2014- 2019

OVE recommendation	Management's response
<p><b>Recommendation 1:</b>  <b>Set clear criteria for prioritizing country strategy objectives, taking into account the potential contribution of the legacy portfolio, IDB Invest, and synergies with other donors.</b> The constraints imposed by the country's limited fiscal space could well persist into the 2020-2024 period, so selecting the strategic objectives for the new country strategy will require a rigorous process of setting priorities that seeks to maximize the use of program resources. The legacy portfolio and private sector operations may constitute valuable inputs towards fulfilling the selected objectives. Likewise, it will be more important than ever to promote effective coordination with other donors. Accordingly, OVE recommends:</p> <ul style="list-style-type: none"> <li>i. Setting clear and explicit criteria for prioritizing the country strategy objectives</li> <li>ii. Taking into account the contribution of the legacy portfolio and IDB Invest, as well as possible synergies with other donors with similar objectives.</li> </ul>	<p><b>Agree</b></p> <p><b>Actions proposed by Management</b></p> <p>The Bank is engaged in active dialogue with the new authorities to decide on the priority areas of the new country strategy.</p> <ul style="list-style-type: none"> <li>i. As part of this process of dialogue to select the country strategy priorities, several criteria are being considered, including the country's main development challenges as identified by the Bank, the legacy portfolio and corresponding lessons learned, and the new government's priorities, both general and specific to the program with the IDB (as opposed to other donors). The objectives set out in the new country strategy will be the result of an agreement between the IDB Group and the authorities on the areas that will guide the Group's actions in the years ahead.</li> <li>ii. The portfolio in execution and lessons learned are key inputs for the selection of priority areas and objectives and for the identification of special aspects to take into account during implementation of the strategy. The dialogue with the authorities has been a coordinated effort by the IDB and IDB Invest, intended to strengthen the private sector's contribution to tackling the country's development challenges and tap synergies between the Group's two windows. Specifically, IDB Invest is participating in the preparation and design of the country strategy, which will enhance the strategic alignment of future approvals in the private sector in priority areas such as SME access to financing, energy and transportation infrastructure, and productive diversification. With respect to donors and creditors, the Bank will continue to promote coordination through its participation in the fiscal roundtables and international cooperation, in order to identify synergies and avoid duplication of efforts. By way of example, the IDB and the World Bank have worked closely on the design of their respective operations planned for this year in education, in order to achieve more effective multilateral support for the government's strategy to improve the quality of primary education. While the World Bank will focus on replacing existing schools, the IDB will concentrate on community-based early education and the expansion of preschool programs.</li> </ul>
<p><b>Recommendation 2:</b>  <b>Foster the strategic use of technical cooperation operations to promote a national consensus designed to bring about the resolution of key development issues and the legislative ratification of loans.</b> The technical default that took place in 2017 and the lengthy ratification times for loans illustrate a larger problem for the country: difficulty in reaching consensus. In this context, the IDB's technical cooperation operations have been shown to play a key</p>	<p><b>Agree</b></p> <p>One lesson learned from the 2015-2019 country strategy was that technical assistance offers strategic value and effectiveness in terms of making progress on key issues for the country's development. In this regard, the Bank agrees on the importance of continuing to use this tool to make headway in areas that are critical for the country's development in the medium term and to contribute—via technical inputs—to the political debate surrounding legislative ratification of loans.</p>

OVE recommendation	Management's response
<p>role in achieving consensus on controversial issues such as fiscal reform, which in turn expedites legislative ratification of the associated loans. Accordingly, OVE recommends:</p> <ul style="list-style-type: none"> <li>i. Continuing to make strategic use of technical cooperation operations to promote the availability of objective analyses of key issues for the country's development that can be used by the parties to reach consensus.</li> <li>ii. Facilitating technical dialogue on the operations during the legislative ratification process.</li> </ul>	<ul style="list-style-type: none"> <li>i. This line of action will be continued. During implementation of the 2015-2019 country strategy and as recognized in OVE's country program evaluation, the Bank's technical analyses facilitated the political discussion on fiscal reform, pension reform, and budget approval. In addition, technical cooperation served to produce additional technical inputs that supported dialogue in the education and logistics sectors. In education, the analyses conducted during the strategy period supported a substantive dialogue with the new authorities, helping to make education a priority area and set the necessary agenda for the next several years. Based on this, the government requested preparation of a loan operation in this sector for the first time in over 10 years. In logistics, technical cooperation supported the preparation of technical inputs that were part of the Infrastructure Master Plan published in early 2020, which will guide public investment in transportation, water and sanitation, energy, and climate-related risk management.</li> <li>ii. The Bank will make inputs available to the actors involved in legislative ratification, to help focus the discussion on the technical merits of the proposals under consideration.</li> </ul>
<p><b>Recommendation 3:</b>  <b>Promote mechanisms to reinforce the sustainability of investments supported by the IDB.</b> Despite visible improvements over the period, the sustainability of the reviewed operations could not be guaranteed as planned. In a context of fiscal constraints, there were (unanticipated) challenges in terms of allocating the budgetary resources needed to give continuity to these services as well as to maintain the investments made. The sustainability challenges were not limited to the financial sphere but rather also encompass the need to consolidate State policies (to which the preceding recommendation contributes), agreements (including at the subnational level), and coordination and maintenance mechanisms. Accordingly, OVE recommends:</p> <ul style="list-style-type: none"> <li>i. Considering, in the design stage of country program operations, the future budgetary implications for the country, e.g. infrastructure maintenance or additional staff.</li> <li>ii. Promoting agreements between the stakeholders involved, seeking to lock in their commitment to sustainability.</li> <li>iii. Advancing the country's interest in strengthening institutional mechanisms responsible for the maintenance of investments.</li> </ul>	<p><b>Agree</b></p> <p>Management agrees on the importance of the sustainability of investments supported by the IDB.</p> <ul style="list-style-type: none"> <li>i. The Bank will continue to include, from the design stage forward, actions to guarantee the maintenance of infrastructure financed by the Bank and the retention, by government agencies, of additional personnel hired for the interventions. This recommendation is consistent with the work that the Bank has been doing since the recommendation that OVE made in its evaluation of the 2009-2014 country program with El Salvador, specifically in relation to incorporating into investment projects the budgetary implications of the investments, in order to facilitate execution and guarantee their sustainability. This was set out in Management's action plan for implementation of OVE's recommendations, by including targets such as analyses of the budgetary implications of IDB-financed investments, which have been fully met, as documented in the follow-up to the action plan.</li> <li>ii. The Bank will strive to promote agreements aimed at preserving the benefits that have been achieved thus far through the Bank's programs, particularly in the fiscal, human capital, and infrastructure areas, and it will promote the sustainability of future interventions. As with projects that have already been approved (e.g. the health project ES-L1095, which included an analysis of the additional spending generated by the investments made under the operation), for operations now in the design stage, consideration is being given to step-down financing arrangements that will promote the absorption, by the authorities, of the costs generated by the investment and additional staff. It is important to note the decisive role that the authorities have played in defining and adopting these agreements.</li> </ul>

OVE recommendation	Management's response
	<p>iii. The Bank will work to promote the country's interest in strengthening institutional mechanisms responsible for maintaining the investments, sharing knowledge about successful arrangements in other countries in the region. Ultimately, however, the adoption of any particular mechanism will depend on the authorities.</p>
<p><b>Recommendation 4:</b>  <b>Reinforce the results framework of the IDB Group's new country strategy with El Salvador, so that it may guide the program to be executed, promote learning, and achieve greater use of country monitoring and evaluation systems, helping to strengthen them.</b> OVE found that the results framework of the country strategy made it difficult to collect data and that the selected indicators only partially covered the expected actions and the program as executed. This made it hard to use the framework to guide implementation, evaluate outcomes, and generate lessons applicable across the program. Accordingly, OVE recommends:</p> <ul style="list-style-type: none"> <li>i. Seeking greater alignment between the results framework of the new country strategy, its objectives, and the lines of action of the program to be executed;</li> <li>ii. Promoting the use of this framework as one of the tools to monitor the effectiveness of the program and extract lessons;</li> <li>iii. Supporting the country in efforts to strengthen its monitoring and evaluation system, so that system indicators can serve as the basis for the results framework of the country strategy and the operations and can be updated in a timely and reliable manner.</li> </ul>	<p><b>Agree</b></p> <p>Management is in agreement on the country strategy's value as a guide for programming and will work towards greater incorporation of country monitoring and evaluation systems into the results framework to the extent that these systems allow. It should be noted that the country strategy, beyond the priority areas reflected in the results framework, envisages dialogue areas for issues that the Bank and the government wish to explore in greater depth during implementation of the strategy. These areas of dialogue are not covered in the results framework because they are not expected to impact the program. However, a situation could arise in which progress is achieved at a faster pace than expected, in which case a program of financing could be established in some of these areas. The dialogue areas impart flexibility, enabling the Bank to respond to the country and deepen its support in response to the pace of progress and the government's interest in the IDB's financial support.</p> <ul style="list-style-type: none"> <li>i. The Bank will strive for alignment between the strategic objectives of the new country strategy and the operations contained in the program agreed upon with the government in the priority areas, while also maintaining the flexibility needed to respond to changes in government priorities that are justified by conditions in the country.</li> <li>ii. The Bank will promote use of the country strategy results framework as a tool for monitoring the effectiveness of the program, ensuring that individual operations contribute to the strategic objectives in the country strategy. The program's effectiveness in achieving the results proposed in the operations will be taken into account in all corresponding analysis, such as project termination reports.</li> </ul> <p>The Bank will support national efforts to strengthen the country monitoring and evaluation systems at the level of operations, and as agreed with the authorities, opportunities for improving sector statistics will be considered. Previous efforts in this regard have included the operation for Tourism Development in the Coastal-Marine Zone (ES-L1066), which provided support to the government on the tourism statistics system (SIETUR) for monitoring the operation and generating statistics for the sector. However, bearing in mind that institutional strengthening takes time, a distinction must be made between the time needed to prepare and implement the new country strategy and the time needed to strengthen these systems. With this in mind, Management believes that strengthening the monitoring and evaluation systems and the subsequent generation of indicators and data will serve as an input for future Bank operations and country strategies.</p>