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Report No: PGD397

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT FOR A

PROPOSED LOAN

IN THE AMOUNT OF US$350 MILLION TO

ORIENTAL REPUBLIC OF URUGUAY

FOR THE

URUGUAY GREEN AND RESILIENT GROWTH DEVELOPMENT POLICY LOAN

October 23 2023

Environment, Natural Resources & the Blue Economy
Latin America And Caribbean

Oriental Republic of Uruguay

GOVERNMENT FISCAL YEAR

January 1 – December 31

CURRENCY EQUIVALENTS

Exchange Rate Effective as of October 24, 2023

Currency Unit = Uruguayan Peso (UYU)

UYU 39.94 = US$1.00

ABBREVIATIONS AND ACRONYMS

ANII	National Agency of Research and Innovation (*Agencia Nacional de Investigación e Innovación)*
ARCE	Public Procurement Regulatory Agency (*Agencia Reguladora de Compras Estatales)*
ANDE	National Development Agency (*Agencia Nacional de Desarrollo*)
BCU	Central Bank of Uruguay (*Banco Central del Uruguay)*
CBD	Convention of Biological Diversity
CET	Common External Tariff
CGN	National General Accounting Office (*Contaduría General de la Nación)*
CONAFIN AFISA	National Financial Corporation Administrator of Investment Funds SA (*Corporación Nacional Financiera Administradora de Fondos de Inversión SA*)
COVID	Coronavirus Disease
CPDC	Commission for the Promotion and Defense of Competition (*Comisión de Promoción y Defensa de la Competencia*)
CPF	Country Partnership Framework
DPL	Development Policy Loan
EEZ	Exclusive Economic Zone
ESG	Environmental, social and governance
FDI	Foreign Direct Investment
FOGADER	Guarantee Fund for the Implementation of Rural Development Policies *(Fondo de Garantia para la Implementación de Políticas para el Desarollo Rural)*
FTA	Free Trade Agreement
FUNDASOL	Uruguayan Foundation for Solidarity, Cooperation and Development (*Fundación Uruguaya de Cooperación y Desarrollo Solidarios*)
GDP	Gross Domestic Product
GHG	Greenhouse Gas
GPGs	Global Public Goods
GPG Fund	IBRD Fund for Innovative Global Public Goods Solutions

GRID	Green, Resilient, and Inclusive Development
GRS	Grievance Redress Service
HLO	High-Level Outcome
IBRD	International Bank for Reconstruction and Development
IMF	International Monetary Fund
INE	National Institute of Statistics (*Instituto Nacional de Estadística*)
KPI	Key Performance Indicator
LATU	Uruguay's Technological Laboratory (*Laboratorio Tecnológico del Uruguay)*
LUC	Law of Urgent Consideration (*Ley de Urgente Consideración)*
MA	Ministry of Environment (*Ministerio de Ambiente*)
MEF	Ministry of Economy and Finance (*Ministerio de Economía y Finanzas)*
MGAP	Ministry of Livestock, Agriculture and Fisheries (*Ministerio de Ganadería, Agricultura, y Pesca)*
MIEM	Ministry of Industry, Energy, and Mining *(Ministerio de Industria, Energía y Minería)*
MPA	Marine Protected Areas
NDC	Nationally Determined Contribution
NTM	Non-tariff Measure
PA	Prior Action
PFM	Public Finance Management
RCBEP	Annual Budget Execution Statement (*Rendición de Cuentas y Balance de Ejecución Presupuestal)*
SIIF	Integrated Financial Information System (*Sistema Integrado de Información Financiera)*
SSLB	Sovereign Sustainability-Linked bond
TdC	Court of Accounts (*Tribunal de Cuentas)*
TOCAF	Consolidated Text on Accounting and Financial Administration *(Texto Ordenado de Contabilidad y Administración Financiera)*
UNFCCC	United Nations Framework Convention on Climate Change
WB	World Bank
WBG	World Bank Group

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SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Operation ID	Programmatic
P179367	No

Proposed Development Objective(s)

The Program Development Objective is to promote i) greening of the economy, and ii) stronger and more resilient growth.

Organizations

Borrower:	Oriental Republic of Uruguay
Implementing Agency:	Ministry of Economy and Finance

PROJECT FINANCING DATA (US$, Millions)

Maximizing Finance for Development

Is this an MFD-Enabling Project (MFD-EP)? Yes

Is this project Private Capital Enabling (PCE)? Yes

SUMMARY

Total Financing	**350.00**

DETAILS

World Bank Group Financing

International Bank for Reconstruction and Development (IBRD)	350.00

PRACTICE AREA(S)

Practice Area (Lead)	Contributing Practice Areas
Environment, Natural Resources & the Blue Economy	Energy & Extractives; Finance, Competitiveness and Innovation; Macroeconomics, Trade and Investment; Poverty and Equity

CLIMATE

Climate Change and Disaster Screening

Yes, it has been screened and the results are discussed in the Appraisal Document

OVERALL RISK RATING

Overall Risk	Moderate

Results

Indicator Name	Baseline	Target
Pillar 1: Greening of the Economy		
1. Second Nationally Determined Contribution (NDC) approved by Decree.	No (2022)	Yes (2024)
2. Area of native forest potentially covered by new fiscal incentives.[1]	0 (2022)	130,211 ha (2024)
3. Number of new Marine Protected Areas (MPA) created.	0 (2022)	1 (2024)
4. Number of certifiers of organic agricultural production registered under the national system.	0 (2022)	3 (2024)
5. Issuance of regulations specific to green hydrogen production and derivatives.	No (2022)	Yes (2024)
Pillar 2: Stronger and more Resilient Growth		
6. The share of imports, by value, subject to reduced import tariffs and certificate fees and risk-management controls.	0% (2021)	58% (2024)
7. Number of antitrust decisions and advocacy opinions issued.	14 (avg 2021-2022)	17 (avg 2023-2024)
8. Share of bank deposits (both nominal and indexed peso) over total deposits (in any currency).[2]	25.5% (avg 2022)	27.5% (2024)
9. Cumulative credits granted to rural women.[3]	138 (2022)	300 (2024)

[1] Based on estimates from the Forestry Division of the MGAP.
[2] Baseline and target are expressed in December 2022 prices using the Uruguayan Consumer Price Index for series in Uruguayan Pesos, and the US Consumer Price Index for series in US Dollars. Series in real US Dollars are then expressed in Uruguayan Pesos using the average exchange rate for December 2022 (40.07 Uruguayan Pesos per US Dollar) to avoid fluctuations due to exchange rate swings.
[3] FOGADER guarantees plus women that operate through the "*Programa Microcrédito Rural*". *Target is the sum of years 2022, 2023, and 2024.*

IBRD PROGRAM DOCUMENT FOR A PROPOSED LOAN TO ORIENTAL REPUBLIC OF URUGUAY

1. INTRODUCTION AND COUNTRY CONTEXT

1. **The proposed Uruguay Green and Resilient Growth Development Policy Loan (DPL) in the amount of US$350 million and a US$12.5 million grant from the IBRD Fund for Innovative Global Public Goods Solutions (GPG Fund), is a standalone operation that seeks to promote i) greening of the economy, and ii) stronger and more resilient growth**. The Government of Uruguay is committed to promoting economic growth and mainstreaming environmental, social, and governance (ESG) principles during its current tenure. The two pillars of this operation support these efforts by endorsing measures that mitigate greenhouse gas (GHG) emissions and promote biodiversity, which contribute to global public goods and underpin the country's brand on climate stewardship, increasingly important for its integration into the global economy. This operation also promotes institutional strengthening and structural measures that advance competitiveness and resilience in the face of negative shocks, a critical contribution coming out of the COVID (Coronavirus Disease) pandemic, which followed years of sluggish growth and stagnating productivity due to long-standing growth bottlenecks.

2. **The operation will include a proposed performance-based grant from the GPG Fund** in recognition of the provision of Global Public Goods (GPGs) in the form of GHG mitigation and globally important biodiversity conservation that the government has been advancing through the policy reforms supported by this DPL. This grant will be approved by the Board of Directors as part of this DPL loan package and will be provided through an innovative mechanism that will allow the performance-based reduction of interest payments on this DPL. Through its leadership on the Development Committee, the Government has been a strong supporter of the GPG Fund objectives and has made substantial efforts to advance innovative instruments to incentivize the provision of GPGs. Details of this innovative approach are included in Annex 6.

3. **The country's longest economic growth spell was showing signs of exhaustion long before the 2020 global recession hit.** Between 2002 and 2019, Uruguay's gross domestic product (GDP) per capita increased by 153 percent (real purchasing power parity) only behind Panama and Peru in the region. Reforms implemented after the 2002 crisis to improve the macroeconomic policy framework, sound debt management, and reduced exposure to neighboring economies contributed to this robust performance, helping increase resilience. In the last five years of the period, however, economic growth decelerated significantly, from 5.1 percent on average between 2003 and 2014 to 0.9 percent between 2015 and 2019, due to unfavorable conditions such as lower commodity prices, a series of adverse climate events and severe recessions in Argentina and Brazil, and limited progress in creating the conditions for a more competitive, integrated, and resilient economy.

4. **The Uruguay Systematic Country Diagnostic Update[4] identifies limited integration into the global economy, a weak competitive environment and shallow credit markets are among the most pressing binding constraints to economic growth and development**. The country lags with respect to structural peers in trade integration, and its exports had stagnated heading into the pandemic, alongside a greater concentration of products and markets, with limited participation into global value chains. Domestic competition is also limited, characterized by a fragmented legal and institutional framework. According to the product market regulation index Uruguay exhibits

[4] World Bank Group. 2022. Uruguay: Systematic Country Diagnostic Update. World Bank, Washington, DC.

significant regulatory constraints that hinder competition.[5] In addition, although Uruguay's financial sector is sound, it is small, bank-centric, concentrated, and highly dollarized. Limited financial intermediation is a relevant cross-cutting constraint to economic growth, diversification, and resilience in the face of shocks.

5. The COVID pandemic had a significant impact on the people and the economy, adding to the challenges. Tourism and other service sectors sensitive to social distancing were impacted significantly, while unfavorable weather conditions affected agricultural exports. The combined impacts led to a 6.3 percent fall of GDP in 2020. The country's pre-existing wide social safety net was reinforced with emergency measures to target the poor and vulnerable people, as well as to help firms survive the shock. However, poverty incidence increased from 8.8 percent in 2019 to 11.6 percent in 2020, meaning around 100,000 people fell below the poverty line. The country implemented a rapid and comprehensive vaccination campaign early in 2021, one of the most successful in the world, contributing to a rebound in economic activity. GDP expanded 5.3 percent in 2021, and the recovery continued into 2022. By 2022, poverty levels had declined to 9.9 percent.

6. Uruguay thus faces the challenge to reignite robust economic growth while increasing resilience in the face of shocks, including weather-related, which are increasing both in frequency and intensity due to climate change. Rising temperatures and precipitation variability are expected to worsen in the years ahead, leading to more frequent and intense weather events, such as droughts, floods, and heat waves, impacting ecosystems, water resources, biodiversity, hydroelectric energy production, and people's health. With annual average precipitation projected to increase by about 100 millimeters by 2050, annual losses from floods are expected to grow from US$64.2 million currently to US$352.8 million by 2030.[6] For example, concurrent with the pandemic, the recurrent *La Niña* weather events have been affecting Uruguay's agricultural production due to drought. The recent drought ranks among the worst in the past century, with direct agricultural, livestock and dairy losses estimated at around 2.5 percent of GDP. Climate effects impact not only food production but the whole food system and its supply chains, affecting food prices increasing risks of food insecurity especially for the most vulnerable population. The impact on the economy from these multiple crises was reduced only in part thanks to improvement in terms of trade, but also in large measure to the resilience that was built into the system of governance, finance, social safety nets and production over many years. This operation supports measures that tackle the source of vulnerability and help build resilience while advancing a green economy.

7. This operation focuses on supporting Uruguay through a green and resilient growth program of reforms under two pillars. The program reflects and supports the continual institutional strengthening of its capacities for sustainability in key productive and environmental sector institutions while also building stronger, more resilient programs and policies on trade and finance. The first pillar focuses on reforms that will promote greening of the economy through climate-smart organic agricultural production, protection of terrestrial and marine habitat (with green and blue carbon co-benefits) critical for the maintenance of agricultural and fisheries production in the long-term, and measures to promote innovation on green hydrogen production. The second pillar seeks to promote stronger and more resilient growth. It will do this by increasing competitiveness through reduced trade tariffs - including the first reduction of external tariffs since Mercosur's inception-, enhancing the competition policy framework to promote market competition, and advance credit in domestic currency to deepen the financial sector and help decouple from external shocks, and credit-related measures that include a program targeted to

[5] (World Bank 2015a)
[6] Uruguay: Systematic Country Diagnostic Update. World Bank Group, 2022.

rural women in response to historical gender gaps in access to finance.

8. The two pillars are complementary and mutually reinforcing. On one hand, failure to advance the climate change agenda affects the growth prospects of a country heavily reliant on natural capital, as reflected in its country brand, "*Uruguay Natural*". Measures supported under Pillar I promote Uruguay's profile as a niche economy of sustainable practices and helps differentiate its products, reach higher-income markets, and diversify export destinations. Enhanced natural capital management helps build resilience in agricultural production and fisheries, but also promotes further growth in tourism, an important source of jobs and income. On the other hand, a stronger and diversified economy makes the country less vulnerable to climate change and helps advance climate commitments. Measures supported under Pillar II provide background for effective climate action and sustainable practices. A competitive tradable sector and deeper capital markets can attract green investments that use Uruguay as a platform for climate-smart exports. This DPL pillars are consistent with the World Bank Global Crisis Response Framework (GCRF) and this operation's policy actions are aligned with its four pillars including measures to attend to food security, supporting jobs in the agricultural sector, crisis preparedness of its productive sector and long-term policies to support the Green, Resilient, and Inclusive Development (GRID) agenda including advancing the NDC and provision of GPGs.

9. The operation is built around policy areas supported by the World Bank (WB) that strengthen Uruguay's institutions and provide GPGs through investment operations, analytical work and technical assistance and is fully aligned with the Uruguay Country Partnership Framework (CPF) FY23-FY27[7]. This operation is aligned with the CPF's High-Level Outcome (HLO) 1 ("Increased Environmental Outcomes and Resilience to Shocks"), through its Pillar 1, and with its HLO 2 ("More and Better Job Opportunities"), through its Pillar 2. It also directly reflects the Government of Uruguay's program and international environmental commitments including its NDC under United Nations Framework Convention on Climate Change (UNFCCC) and the Convention on Biological Diversity (CBD). This operation builds on operations such as the ongoing Uruguay Agro-Ecological and Climate Resilient Systems Project (P176232) that followed the Sustainable Management of Natural Resources and Climate Change Project (P163444) addressing many dimensions of climate risk in the agricultural sector. Relevant analytics include the WB Green Growth: Towards a Strategy for Uruguay (P161012), and more recently Promoting Cleaner and Sustainable Energy Systems (P166823) and work undertaken jointly with the Ministry of Economy and Finance (MEF) to develop a model to consider long-term economic impacts of climate change on the Uruguayan economy. It also builds on technical assistance to the Commission for the Promotion and Defense of Competition (Comisión de Promoción y Defensa de la Competencia, CPDC) to upgrade the competition institutional framework, and analytical projects conducted in Uruguay and other Mercosur countries on the impact of reduced external tariffs.

10. This operation is consistent with IBRD guidance on countries with income above the Graduation Discussion Income level, focusing on the strengthening of institutions as well as provision of GPGs, knowledge, and best practices for developing countries. The World Bank Group (WBG) has a history acting as a facilitator for international best practices and innovation stemming from Uruguay, which become GPGs later replicated in other member countries through analytical activities or lending projects. Bank support to Uruguayan institutions and

[7] World Bank. Uruguay - Country Partnership Framework for the Period FY23-FY27 (English). Washington, D.C.: World Bank Group. http://documents.worldbank.org/curated/en/099525011112230801/BOSIB0f20149f30f10959805255d4935301 discussed by the Board on 6th December 2022

utilities has resulted in knowledge-sharing with countries like the Kazakhstan and Papua New Guinea on energy, Panama and Argentina on water provision, and Bolivia, Nicaragua, Paraguay and most recently, Botswana, Namibia and the Kyrgyz Republic on sustainable agriculture and animal traceability. The proposed program builds on, and contributes to, that tradition, starting with the innovative mechanism for performance-based reduction of interest payments linked to climate-related targets. In addition, the policy measures supported by this operation focus on institutional strengthening including enhancements to the competition framework by empowering the CPDC, provision of GPGs of biodiversity and blue carbon through a marine conservation effort that within a year will rank Uruguay among the top ten nations for marine protection[8], regulations to promote organic production, coordination of trade integration measures with regional partners, incentives for the conservation of native forests, leveraging innovation in green technologies, and enhancing the ambition of the country's (and global) GHG emission goals.

2. MACROECONOMIC POLICY FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

11. The economy continued to recover in 2022 but ended on a negative note that continued into 2023, affected by a historic drought heading into the peak agricultural season. After a 5.3 percent expansion of GDP in 2021, GDP increased 4.9 percent year-over-year in 2022, but contracted 0.5 percent in the first semester of 2023. The contraction was led by *Agriculture, fishing, and mining* (-18.4 percent year-over-year), and *Electricity, gas, and water,* all of which had been severely affected by the strong drought of the 2022/23 season. On the demand side, gross fixed capital formation was the main driver of the contraction, which decreased 2.3 percent in the same period, as the extraordinary contributions of investment in the new pulp mill come to an end. Private consumption continued to expand.

12. Under improved economic activity and living conditions, labor market outcomes reached pre-pandemic levels in 2021 and continued improving in 2022 and 2023. Unemployment fell to 7 percent in December 2021, the lowest level since 2017. Into 2022, unemployment increased mainly among men (from 5.7 percent in December 2021 to 7.3 percent in December 2022), while remaining relatively unchanged for women in the same period (8.5 percent and 8.6 percent respectively). Despite labor market improvements, underlying structural disparities in human capital and job opportunities across population groups and regions remain. Population in northern departments where informality reaches 30 to 40 percent, above the national average of 21 percent, are particularly vulnerable.

13. Although the economic recovery helped poverty recede in 2021 and 2022, it was not enough to bring it down to pre-pandemic levels. The poverty rate under the international poverty line for upper-middle income countries is estimated at 6.4 percent in 2022 (down from 7.2 percent in 2020 and 6.7 percent in 2021, but still above 5.1 percent in 2019). Sectors affected by the pandemic –domestic services, transportation, entertainment, restaurants, and hotels– have still faced limited recovery. Meanwhile, sectors employing more skilled workers –health, education, banking, and professional activities– showed a strong recovery, generating new jobs and better

[8] Marine Conservation Institute - Marine Protection Atlas. According to the Marine Protection Atlas only 7 countries have 10 percent or more of their marine area fully or highly protected from fishing. https://mpatlas.org/countries/list

salaries.

14. The cyclical recovery was underpinned by progress on a structural reform agenda to address underlying growth bottlenecks and help build resilience in the face of shocks. Despite the urgencies related to the COVID response, the Government of Uruguay has advanced a development reform agenda based on its electoral program. The UY COVID Response and Economic Recovery DPL (P172796) in 2020 supported the response measures and early advances in the structural agenda. The reform impulse continued into 2022, including measures to enhance the country's integration into the global economy, improve the competition framework, promote de-dollarization and credit in domestic currency -including specific programs for women-, and promote energy security. At the same time, it has advanced initiatives to promote global public goods, and protect its natural endowments, the basis of the country's development. These measures are supported by the proposed operation.

15. After a moderate spike in 2022 inflation declined to an eighteen-year low, despite a history of relatively high inflation. Uruguay has historically operated under a relatively high inflation rate, averaging 8.1 percent since 2010 (Figure 1). Committed to curbing inflation dynamics, the Central Bank of Uruguay (*Banco Central del Uruguay*, BCU) implemented measures since 2020 to modernize the monetary policy framework, including the narrowing of the inflation target range from 3-7 percent to 3-6 percent in September 2022, the establishment of the interest rate as its main policy tool, more frequent meetings of the Monetary Policy Committee, and a more transparent decision-making process. In addition, the BCU adopted a strong anti-inflationary policy stance. The BCU hiked its benchmark rate to 11.50 percent in December 2022 for a 700 basis points cumulative increase since July 2021, contributing to a strong Uruguayan peso. As a result, the inflation spike in 2022 was modest, from 7.7 percent in 2021 to 9.1 percent in 2022 due to the acceleration of food and fuel prices. Inflation has since receded rapidly, reaching 4.1 percent in August 2023, the lowest since 2005.

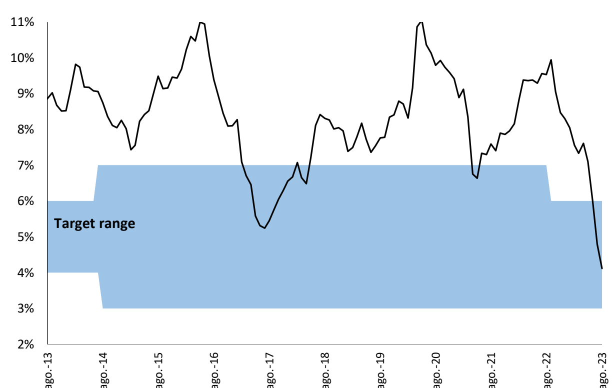
16. Aided by the fall in inflation, real wages increased by 3.4 percent through August Year-To-Date, after a 0.6 percent decrease in 2022. The employment rate increased 0.5 pp. in 2023H1, yet unemployment increased from 7.8 percent in 2022H1 to 8.5 percent in 2023H1 due to a higher labor market participation rate.

17. Fiscal accounts continued to improve in 2022, largely due to an un-winding of COVID related programs and a cyclical recovery in expenditures, but slightly deteriorated in 2023. The deficit of the non-monetary public sector fell from 5.3 percent of GDP in 2020 to 2.7 percent in 2022 (Figure 2), mostly driven by a spending decline as a share of GDP but increased to 3.4 percent of GDP in the rolling year to August 2023, as the sharp deceleration of inflation and the impact of the drought weighed on revenues in the face of rigid expenses in wages, pensions, and transfers.

18. Growth, fiscal discipline, and the appreciation of the Uruguayan peso led to a decline in the public debt-to-GDP ratio. Public debt spiked to 67.6 percent in 2020 following the sharp increase in the fiscal deficit, economic contraction, and the depreciation of the Uruguayan peso. The reversal of these trends helped bring the ratio down to 61.8 percent in 2021, and 61.1 percent of GDP in 2022. The trend continued into 2023, as the appreciation of Uruguayan peso pushed the ratio further down to 60.1 percent in June 2023. Uruguay has had the lowest country spreads in Latin America for over a year, with an average interest rate of 5.1 percent in June 2023 for US Dollar-denominated debt, and 8.9 percent for debt denominated in Uruguayan pesos. The average maturity of debt was 12.6 years in June 2023.

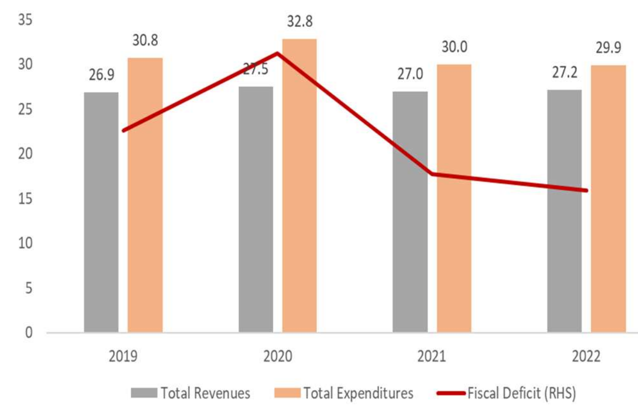
19. The fiscal framework is underpinned by the country's three-pillar fiscal rule. The first pillar of the fiscal rule, implemented in 2020, is a structural fiscal balance target for the central government and social security administration, which abstract from the influence of business cycles and extraordinary revenues and expenditures on fiscal accounts. The second pillar caps the growth rate of real primary expenditure with the growth rate of potential GDP. The third pillar sets a net-indebtedness ceiling, set annually and subject to an escape clause for up to an additional 30 percent from the budgeted amount. All three pillars were achieved in 2022 for the third consecutive year. The new fiscal institutional framework implemented in 2020 was enhanced in 2021 and 2022, with the creation of an independent Fiscal Council to advise the MEF on the fiscal rule and debt sustainability, and an Expert's Committee to provide technical inputs for output gap estimation.

Figure 1. Consumer Price Index Inflation and Inflation Target Range, percent



Source: National Institute of Statistics (*Instituto Nacional de Estadística*, INE) and BCU.

Figure 2. Revenues, Expenditures, and Fiscal Deficit, percent of GDP



Source: MEF and WB estimates
Corresponds to Non-Monetary Public Sector.

20. Uruguay's external accounts remain solid, underpinned by a flexible exchange rate regime and sizeable reserves. Uruguay's flexible exchange rate regime has been the first line of defense against external shocks, without generating excessive stress on balance sheets in the private sector. The current account has displayed moderate deficits, even in the face of larger foreign direct investment (FDI) inflows owing to a US$3 billion pulp mill project in the works since 2019.[9] The current account deficit reached 3.7 percent of GDP in 2022, despite higher export prices following Russia's invasion of Ukraine, since they were more than offset by the hike in import prices (mainly fuel), for a 3.8 percent fall in the terms of trade. The current account balance remained at 3.7 percent of GDP in the first half of 2023. At around US$15.4 billion as of September 2023, gross reserves cover roughly the equivalent of 10 months of imports.

[9] This plant from the UPM-Kymmene Corporation situated in Paso de Los Toros, is the second large investment from the Finnish firm in Uruguay, following one in Fray Bentos in 2007, which currently produces 1.3 million tons of cellulose. The large scale of these types of plants has significant macroeconomic effects in a country the size of Uruguay during their construction process and as they start to produce and export.

21. Uruguay's financial system is sound, but relatively small and dominated by the banking sector. Financial sector assets reached around 107 percent of GDP in 2023H1, of which banks represented about two-thirds. The banking sector consists of two state owned banks (*Banco de la República Oriental del Uruguay*, BROU, and *Banco Hipotecario del Uruguay*, BHU) and nine foreign-owned banks. Loans represent a small share of the banking sector's assets and are predominately funded by residents' deposits. The banking sector is highly dollarized with half of loans and 72 percent of deposits in US dollars. Access to finance is limited for the productive sector. Although financial inclusion has improved over the years (74 percent of the adult population has access to an account), credit provision is low. Commercial banks' credit to the private sector is around 30 percent of GDP, of which lending to Small and Medium-Sized enterprises represented 6 percent of GDP in 2020. According to the Enterprise Survey (2017), 40 percent of firms reported access to finance as a major constraint. Non-performing loans are likely to rise due to the substantial increase in interest rates, but the limited banking credit, adequate bank profitability and capital buffers, and large liquidity buffers mitigate risks. The Fintech sector has been growing rapidly, particularly lending through electronic platforms (which includes companies that advance checks and others that provide mortgage loans) which represents about 30 percent of Uruguay's Fintech sector.

22. Capital markets remain underdeveloped, and the capital market instruments available in Uruguay are limited. The market capitalization of the two local stock exchanges represented less than 0.5 percent of GDP in September 2021, with only 7 listed companies. Out of US$40 billion securities issued (around 70 percent of GDP) in 2021, more than 90 percent are public sector securities with half of the stock held by non-residents (85 percent of government debt in foreign currency and 15 percent of government debt in pesos). The majority of operations in the primary market are related to certificates of deposit issued by private banks in the stock market and Monetary Regulation Bills, which are traded over the counter. Trading in the secondary market is also driven by Monetary Regulation Bills.

23. Uruguay's macroeconomic fundamentals are in general strong, but the country is vulnerable to the increasing intensity and severity of different types of shocks, as the recent drought illustrates. Uruguay is a small economy relying on a relatively small basket of exports grounded in its natural capital, such as agricultural goods, livestock, and tourism, historically exposed to external shocks, including climate events, or swings in relative prices and world demand. For example, the Ministry of Livestock, Agriculture and Fisheries (MGAP) estimates over US$1.8 billion in direct losses (around 2.5 percent of GDP) in foregone revenue from grain and livestock production during the 2022-23 drought. However, sound macroeconomic management, particularly since the 2002 crisis, has improved the country's fundamentals and risk profile. In addition, exports of global services have strongly boosted in recent years, surpassing traditionally strong tourism inflows and much more resilient to price and regional volatility events. Yet, as climate-related shocks (mostly droughts and floods) become more frequent and intense, and as global uncertainty heightens, Uruguay needs to continue in its efforts to support a stronger, more sustainable, and resilient growth process.

Table 1: Uruguay Key Macroeconomic Indicators, 2020-2026

	2020	2021	2022	2023e	2024p	2025p	2026p
Real Economy	**Annual percentage change, unless otherwise indicated**						
Nominal GDP in local currency	3.1	18.6	9.6	7.3	8.9	8.0	7.7
Real GDP	-6.3	5.3	4.9	1.5	3.2	2.6	2.6
Private Consumption	-6.8	2.9	6.0	2.2	2.5	2.2	2.1
Government Consumption	-7.1	8.4	1.6	0.7	0.3	0.6	1.0
Gross Fixed Capital Investment	1.2	16.5	9.5	2.1	4.1	6.5	6.5
Exports, Goods and Services	-16.3	11.7	11.1	0.5	5.9	1.0	1.0
Imports, Goods and Services	-12.2	18.2	12.5	2.0	3.2	1.5	1.5
Unemployment rate[1]	10.4	9.3	7.9	…	…	…	…
CPI (average)	9.8	7.7	9.1	6.0	5.6	5.3	4.7
Fiscal Accounts	**Percent of GDP**						
Non-Financial Public Sector (NFPS) [2]							
Primary expenditures	30.2	27.9	27.8	27.4	27.1	27.4	27.1
Total revenues	27.5	27.0	27.2	26.8	26.9	27.3	27.2
Primary Balance	-2.7	-0.9	-0.6	-0.7	-0.3	-0.2	0.0
Overall Balance	-5.3	-3.0	-2.7	-2.9	-2.6	-2.6	-2.4
NFPS Debt	67.6	61.8	61.1	59.7	58.8	59.0	59.3
Selected Monetary and Financial Indicators	**Annual percentage change, unless otherwise indicated**						
Base Money	5.8	2.0	-2.4	…	…	…	…
Credit to non-government	12.3	8.2	8.3	…	…	…	…
Interest (key policy interest rate, avg)[3]	4.5	4.9	9.1	…	…	…	…
Balance of Payments	**Percent of GDP**						
Current Account Balance	-0.8	-2.5	-3.7	-3.6	-2.5	-2.2	-2.2
Imports	21.3	24.6	26.5	25.0	24.3	24.0	23.7
Exports	25.8	31.8	31.7	29.6	29.5	29.0	28.5
Foreign Direct Investment[4]	-1.9	-2.4	-4.5	-1.3	-1.3	-1.2	-1.2
Gross Reserves (in billion US$, eop)	16.2	17.0	15.4	…	…	…	…
As % of GDP	30.2	27.6	21.3	…	…	…	…
In months of next year imports	14.6	18.1	9.9	…	…	…	…
Terms of Trade (percent change, eop)[5]	-0.6	11.2	-3.8	…	…	…	…
Exchange rate (average)	42.0	43.6	41.2	…	…	…	…

Source: Ministerio de Economia y Finanzas, Banco Central de Uruguay, Instituto Nacional de Estadisticas (INE) and WBG staff calculations.
Uruguay is classified as an high income country for the purpose of IBRD lending classification.
[1] Soruce: INE.
[2] Excluding "cincuentones".
[3] The Central Bank changed the monetary policy instrument, from monetary aggregates to interest rates starting on September 4, 2020.
[4] Following the Asset-Liability criterion (MBP6).
[5] Includes exports of goods and services.

2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

24. **GDP growth is projected to decelerate in 2023 due to the drought, and later converge closer to its potential growth rate.** The drought, which has already affected growth figures for 2022, will continue to be a drag on economic activity in 2023 and its impact is likely to spread out through the years, mostly due to the life cycle of livestock. The direct effect of the drought through the years is estimated at US$1.8 billion, but its scope and indirect impacts are still uncertain. A strong tourism season, dynamic service exports, and the opening of the new pulp mill are expected to more than offset agricultural losses, for a positive contribution of exports to economic growth. Real GDP is expected to expand 1.5 percent in 2023 and converge closer to potential GDP growth by 2025.

25. **Inflation is expected to remain within the target range in 2023 and beyond**. The BCU is expected to sustain relatively high interest rates to underpin the successful disinflation effort going forward. Inflation is thus expected to remain within the 3-6 percent target range by end-2023. The Uruguayan peso is expected to remain strong in the baseline scenario, supported by high terms of trade and tight monetary policy. [10]

26. **Receding inflation and the expected pick-up in economic activity increase the prospects for welfare improvements in 2023 and 2024.** Poverty under the international line (US$6.85 per day, purchasing power parity 2017) is expected to fall to levels around 6 percent in 2023. Simultaneous improvements in employment and real salaries have helped household per capita income grow by 7.9 percent in Montevideo and 6 percent in the interior areas of the country in 2023H1 year-over-year.

27. **Fiscal accounts are projected to continue to improve, with primary expenditures capped by potential economic growth as established in the fiscal rule**. The primary deficit of the non-monetary public sector is expected to improve from 0.6 percent of GDP in 2022 to 0.0 by 2026. The fiscal consolidation is expected to be driven by expenditures, mainly through the continued face-out of COVID related expenditure (which in 2022 still reached US$407 million a small decline in capital expenditures as a share of GDP, and minor other savings, particularly in the purchase of public goods and services, which are expected to decline slightly as a share of GDP. The indicative structural fiscal balance targets and primary expenditure caps are expected to be met under the baseline scenario in the forecast horizon. A pension reform to improve the system's long-term sustainability was approved in May 2023.

28. **The current account deficit is expected to narrow going forward as exports remain strong and the extraordinary imports related to the construction of the pulp mill come to an end**. Exports are expected to decelerate due to the drought but remain positive in 2023 as the new pulp plant starts producing and tourism normalizes further. Imports are projected to moderate going forward given the lower domestic expenditure dynamism. Terms of trade are expected to improve in the baseline scenario, as the gradual fall in oil prices outpaces agricultural commodity prices. In this context, trade balance trends are expected to dominate the deficit in primary income, for a gradual reduction in the current account deficit in the forecast horizon. The narrowing current account deficit is expected to be more than met by FDI. International reserves are expected to remain stable in the medium term.

[10] *Informe de Política Monetaria, Cuarto Trimestre de 2022, Banco Central del Uruguay.*

Table 2: Balance of Payments Requirements and Sources (in million US$)

	2020	2021	2022	2023e	2024p	2025p	2026p
Financing requirements (US$)	**9,104**	**10,638**	**9,667**	**9,691**	**9,758**	**10,176**	**10,930**
Current account deficit	435	1,551	2,620	2,734	1,941	1,754	1,750
Debt amortizations, public and private	7,039	8,244	8,625	6,757	7,618	8,222	9,380
Gross reserve accumulation	1,630	843	-1,578	200	200	200	-200
Financing Sources (US$)	**9,104**	**10,638**	**9,667**	**9,691**	**9,758**	**10,176**	**10,930**
FDI	-1,016	-1,493	-3,175	-964	-992	-993	-993
Portfolio investment	1,478	1,084	1,877	1,000	800	900	900
Multilaterals	1,527	600	571	350	250	250	250
Other capital investment	7,115	10,447	10,394	9,305	9,701	10,020	10,773

Source: IMF's Article IV, WBG staff calculations and budget balance of GOU

Table 3: Key Fiscal Indicators

	2020	2021	2022	2023e	2024p	2025p	2026p
1. Central Government (CG)[2]+ Social Security Institution (BPS)			**Percent of GDP**				
Total Revenues (and grants)	**26.4**	**25.3**	**26.0**	**25.8**	**26.1**	**26.3**	**26.3**
Central Government	**19.2**	**18.8**	**19.2**	**18.8**	**19.0**	**19.2**	**19.2**
Tax revenues	16.5	16.2	16.5	16.1	16.2	16.5	16.6
Taxes on international trade	1.0	1.1	1.1	1.1	1.1	1.1	1.0
Other income	2.2	1.9	1.7	1.7	1.8	1.7	1.7
Social insurance contributions	**6.7**	**6.2**	**6.7**	**6.9**	**7.0**	**7.0**	**7.0**
Expenditures	**32.2**	**29.4**	**29.2**	**28.9**	**28.6**	**28.7**	**28.6**
Current expenditures	31.0	28.3	27.7	27.8	27.6	27.3	26.8
Wages and compensation	5.2	4.7	4.6	4.6	4.6	4.5	4.3
Goods and services	4.0	4.3	3.9	3.5	3.5	3.3	3.2
Interest payments	2.8	2.2	2.3	2.5	2.4	2.4	2.3
Current transfers	19.0	17.1	16.9	17.2	17.1	17.1	17.0
Capital expenditures	1.3	1.1	1.6	1.2	1.1	1.4	1.8
Overall Balance	**-5.8**	**-4.1**	**-3.2**	**-3.2**	**-2.7**	**-2.4**	**-2.3**
of which: Primary balance	-3.0	-1.9	-0.9	-0.7	-0.3	0.0	0.1
2. Non-Financial Public Sector (NFPS)[3]			**Percent of GDP**				
Total Revenues	**27.5**	**27.0**	**27.2**	**26.8**	**26.9**	**27.3**	**27.2**
Tax revenue	26.7	26.5	26.5	26.2	26.3	26.6	26.5
Other revenues	0.8	0.5	0.6	0.6	0.6	0.6	0.6
Primary expenditures	**30.2**	**27.9**	**27.8**	**27.4**	**27.1**	**27.4**	**27.1**
Current expenditures	28.2	26.1	25.4	25.2	24.9	25.2	25.0
of which: Wages and compensation	9.2	9.0	8.5	8.5	8.6	8.7	8.6
Capital expenditures	2.0	1.8	2.4	2.2	2.2	2.2	2.1
Interest payments	**2.7**	**2.1**	**2.1**	**2.3**	**2.4**	**2.5**	**2.5**
Overall balance	**-5.3**	**-3.0**	**-2.7**	**-2.9**	**-2.6**	**-2.6**	**-2.4**
of which: Primary balance	**-2.7**	**-0.9**	**-0.6**	**-0.7**	**-0.3**	**-0.2**	**0.0**
3. Gross public Debt NFPS	**67.6**	**61.8**	**61.1**	**59.7**	**58.8**	**59.0**	**59.3**

Source: Ministerio de Economia y Finanzas, Banco Central de Uruguay and WBG staff calculations.

[1] Excluding "cincuentones".

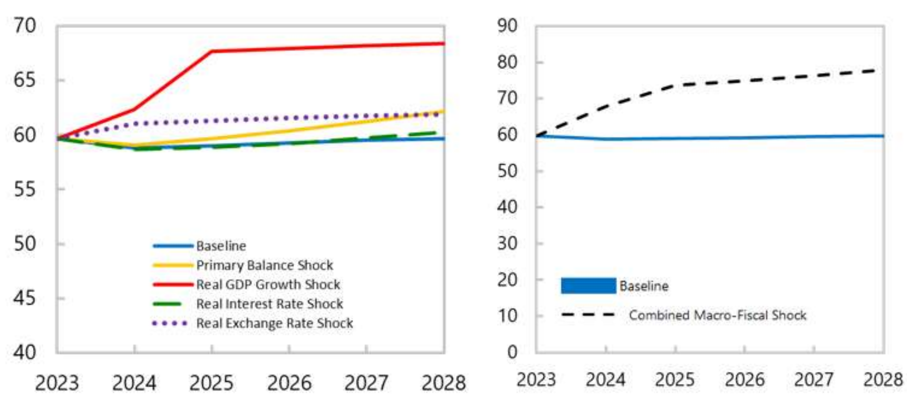
[2] Central Government currently only comprises core central administration; from 2021 deconcentrated entities will be included in the Central Government accounts. Excludes contributions to Social Insurance Fund.

[3] Includes CG, Local Governments, Social Insurance Funds, Decentralized entities and SOEs.

29. Public debt is sustainable under the baseline scenario, and robust to standard shocks. The debt sustainability analysis conducted for this operation shows that, under the baseline scenario described in this section, the debt-to-GDP ratio of the non-financial public sector is projected to fall from 61.1 percent in 2022 to 59.3 percent by 2026 as economic growth endures and fiscal accounts continue to improve (Figure 3). Stress test scenarios suggest that the dynamic of public debt is relatively robust to standard macroeconomic shocks triggered by, for example, climate events, terms of trade swings, or changing financial conditions, including a steeper increase in interest rates. The baseline scenario is most sensitive to a growth shock (negative growth in 2024 and 2025). A combined shock, which adds a shock to the real interest rate and a worse primary balance path would increase the debt-to-GDP ratio to 74.9 percent of GDP by 2026.

30. The outlook is subject to large uncertainties and risks. A stronger deceleration of global economic growth or a global recession could depress international trade and increase uncertainty beyond that envisioned in the baseline scenario. Financial turbulence in international credit markets could induce capital outflows from emerging economies, increasing sovereign spreads, currency depreciation, and higher inflation. The extent of the indirect impacts of the drought on the whole economy are still uncertain. These uncertainties add to the downside risks. Climate shocks in the form of droughts, floods or heatwaves that affect agricultural and beef production, labor productivity, or infrastructure, could reduce exports and domestic incomes, depressing economic activity and affecting labor and welfare outcomes. Misalignment between the real exchange rate and its fundamentals is another source of risk to activity, driven by capital flows, shallow FX markets and high interest rates to sustain the disinflation process. Macroeconomic shocks to trading partners, particularly China, could represent both a downside and upside risk, with its effects on agricultural commodity prices and the overall demand for Uruguayan products.

Figure 3. Debt Sustainability Analysis. Debt-to-GDP ratio, percent of GDP



Source: Own estimates.

31. Relevant factors mitigate downside risks. Rollover risks appear limited – even under adverse scenarios – given Uruguay's debt structure and low financing needs. Uruguay benefits from a long maturity profile of public debt, low average interest rates, the lowest country spreads in the region, a banking sector with abundant liquidity, and low financial needs, which reduce refinancing risk. The fact that Uruguay relied on capital markets at favorable rates at the height of the COVID pandemic serves as a relevant precedent for access to international markets under stress. Moreover, direct contagion risks from neighboring countries have substantially diminished since the sovereign stress of the early 2000s, further protecting Uruguay's access to international debt markets. For example, non-resident deposits in Uruguay, whose withdrawals had triggered the financial crisis in 2002, have declined from 32 percent of total deposits in 2001 to 9 percent in June 2022.

32. Uruguay's macroeconomic policy framework is deemed adequate for this operation. Uruguay's fiscal position is expected to improve in the forecast horizon, underpinned by a pledge to prudence and an enhanced fiscal framework, ratified in 2022 by a referendum to the Law of Urgent Consideration (*Ley de Urgente Consideración*, LUC) a programmatic omnibus law. The BCU has consistently shown a strong commitment to rein inflation, including by strengthening its monetary policy framework, which enables it to keep inflationary pressures from the international commodity price spike contained. External imbalances are low and financed by FDI. An established flexible exchange rate regime and sizeable international reserves are relevant lines of defense against external shocks. In addition, public debt management is sound, and the debt trajectory is sustainable and relatively robust to standard shocks. The financial sector is sound. In addition, Uruguay's solid social compact limits policy response uncertainty and provides a strong backbone to channel conflicts effectively.

2.3. IMF RELATIONS

33. The government maintains a close dialogue with the International Monetary Fund (IMF) on monetary, fiscal, debt management, external and structural policies. There is no program in place between the IMF and Uruguay. The IMF Board approved the latest Article IV Consultation for Uruguay in May 2023. Annex 2 contains a copy of the press release.

3. GOVERNMENT PROGRAM

34. The operation is aligned with the government program embodied in its electoral coalition platform "*Compromiso por el País*" that was followed by the LUC at the outset of its mandate in 2020 that included a broad set of reforms. The subsequent Annual Budget Execution Statements (*Rendición de Cuentas y Balance de Ejecución Presupuestal,* RCBEPs) presented every year to Congress includes policies that are part of this operation. The LUC included many measures for institutional reform that covered economic, social, and environmental agencies and regulations. Among the key areas of focus of the LUC, aligned with this operation, have been the establishment of a new Ministry of Environment (*Ministerio de Ambiente*, MA) from a dispersed group of agencies, reform of the public sector education system, strengthening the Energy and Water Regulatory Unit (*Unidad Reguladora de Servicios de Energía y Agua*, URSEA), and market competition oversight through the CPDC under the MEF. As highlighted in the recent CPF, there is a long-standing shared vision in Uruguay regarding key long-term priorities that include macro stability and access to financial markets, a focus on export through new and high-quality markets, good stewardship of natural assets focusing on sustainability and low-impact production. Along these lines another program that is also aligned with this operation is the "*Uruguay Natural"* country brand that seeks to promote its natural beauty and resources for tourism and inclusive income generation and job creation.

35. In March 2022 the opposition called for a referendum on the LUC which showed continued support for the government priorities and reform agenda. Following the ratification of its reforms by the electorate, the government continues to advance along the same lines at present with its pillars focused on fiscal, social security, and educational reform as well as renewable energy, universal water and sanitation, logistics, agroecology, and sustainable production with strong participation of the private sector, climate adaptation, and conservation. Over the past three years the government has advanced several programs along these lines that are precursors to the current operation including the adoption of a Long-Term Strategy on climate change, advancing a carbon tax, and a land-use planning law to reduce the impact of plantation forests on biodiversity and natural grasslands (also important for carbon storage) in late 2021 among others.

36. Uruguay's commitment to GPGs' provision and sound debt management was reflected in an innovative issuance of a Sovereign Sustainability-Linked bond (SSLB) in October 2022. The issuance linked a two-step coupon structure tied to nature-based targets drawn from Uruguay's first NDC, namely: a reduction of GHG emissions per unit of GDP, and the maintenance of native forest areas, a proxy for carbon capture. If the government over-achieves either or both specified performance targets, it will benefit from a coupon rate step-down. If it fails to meet the targets, the government will be penalized with a coupon step-up. Uruguay commits to the enhanced reporting and independent verification capabilities required under such a framework. The issuance reached US$1.5 billion in sovereign dollar-denominated bonds and was oversubscribed. The coupon step-down in case of target overachievement was set at 15bps for each target (30bps total). The step-up in case of non-achievement is symmetric. Targets will be observed in 2025 and verified in 2027. The operation covered financing needs for 2022, reduced re-financing risks, increased the average maturity of debt, and diversified the country's investor base.

37. The first pillar policies promote and advance the government's vision of green growth through improved environmental and social management and strengthened institutions. This is especially focused on the agriculture, livestock production, forestry, hydrogen energy generation, and tourism sectors that make up a large part of the economy and are more significantly impacted by climate change. The policies supported by this operation are consistent with the National Climate Change Plan, and its complementary strategy on Gender and Climate Change 2020-2025[11], the First NDC (2017) under the Paris Agreement (with approval of the Second NDC a prior action under this operation), as well as biodiversity commitments under the CBD. It also aligns with the National Plan for Production Based on Agroecology[12] and the MGAP Strategic Plan for 2020-2024 in the agriculture sector. This strategic plan includes several key areas relevant to the policy actions supported by this operation including institutional strengthening, rural development through generation of public goods including investments in climate adaptation and prevention of human and animal disease while advancing gender inclusion in this sector.

38. The second pillar focuses on making growth more robust and resilient to multiple types of crises that are interrelated and have been an important focus of the government since the establishment of the LUC early in its mandate. The government programs in addition to the LUC framework objectives with which this pillar is aligned include the Financial Inclusion Program. The LUC and associated programs seek stronger and more diversified economic growth, resilience and strengthening of the institutions for more efficient public services, stronger competition, broader access to food, and the provision of financial services through remote and digital systems to facilitate universal access even under situations of limited mobility of people, as occurred with the recent COVID pandemic or heatwaves and floods, which are becoming more frequent as a result of climate change impacts.

4. PROPOSED OPERATION

[11] https://www.gub.uy/ministerio-ambiente/politicas-y-gestion/genero-cambio-climatico-uruguay
[12] https://www.gub.uy/ministerio-ganaderia-agricultura-pesca/comunicacion/publicaciones/plan-nacional-para-fomento-produccion-bases-agroecologicas/plan-nacional

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

39. The proposed standalone DPL supports the government's forward-looking program advancing ESG oriented policies for sustainable economic growth and resilience. The Program Development Objective is to promote i) greening of the economy, and ii) stronger and more resilient growth. These policy reforms follow Uruguay's vision for sustainable, inclusive economic growth and development in the face of climate and other global challenges and shocks, including the lessons learned from the COVID pandemic, recent recurrent droughts, and global instability linked to international crises and conflict. The policies supported by the operation seek to follow a green-growth paradigm that generates high-quality goods and services for global markets while protecting natural resources, with greater inclusion of women and underserved populations. It also seeks to generate resilience of public and private systems and services, to ensure that the economic growth is supported by a safety net that minimizes social and environmental impacts, facilitating access to goods and services under changing conditions.

40. This operation is aligned with the goals of the Paris Agreement. First, the DPL reform program is consistent with the country's climate commitments. The approval of Uruguay's second NDC in late 2022 informed by a technical assistance from the WB, is included in the policy actions (PA 1) and constitutes a critical long-term commitment towards achievement of global GHG emission reduction goals, and climate resilience and adaptation targets. Furthermore, on adaptation, the actions are also consistent with the strategies included in the National Adaptation Plan, particularly the Agriculture Adaptation Plan. Second, on mitigation goals, only PA 6 (external tariff adjustment) might lead to increased emissions as a consequence of increased volume of transported goods, however, the risks are reduced to low levels through the decarbonization strategies the country has currently in place, in particular for the transport sector. All other prior actions are not likely to cause a significant increase in GHG emissions or any persistent barriers to transition to low-GHG emissions. Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs. These GPGs include blue carbon and conservation of biodiversity through the expansion of MPA (PA 3), green carbon and globally important biodiversity through protection of native forests through tax incentives (PA 2), as well as the promotion of agro-ecology and organic agriculture (PA 4) which will increase the potential of Uruguay's products to reach new and premium international markets, while increasing the sector's resilience to climate change and promoting carbon sequestration.[13] Protecting and improving management of the marine and land/soil resource base of the country is also critical to ensure long-term development by sustaining fisheries and reducing soil runoff to maintain crop productivity and reduce surface water pollution. This pillar also advances production of renewable energy (PA 5). Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competition, economic diversification, and development, and can be considered neutral from an emissions perspective. The measures included under this pillar support (i) easier access to imported food through reduction in tariffs and trade facilitation measures that diversify the input and goods markets that Uruguay depends on, promoting competitiveness and decreasing risks from relying on fewer providers (PA 6), (ii) a more competitive environment, through a strengthened competition framework (PA 7), (iii) a deeper financial sector to effectively promote and intermediate savings in domestic currency and help smooth shocks (PA 8), and (iv) increasing direct access to credit by rural women (PA 9). Third, on adaptation and resilience goals, only contributions to the Program Development Objective from PA 3 are likely to be at risk from climate hazards. However, risks under PA 3 are reduced through the design considerations which include management practices within the MPA intended to reduce the vulnerability of biodiversity habitats and to increase ecosystems' resilience. In conclusion, all prior actions of the proposed DPL

[13] https://www.inac.uy/innovaportal/v/9894/14/innova.front/programa-de-carne-natural-certificada-del-uruguay---pcncu

program are aligned with the mitigation and adaptation goals of the Paris Agreement. A detailed review is presented in Annex 5.

41. The operation, while not part of a series of DPLs, builds on the UY COVID Response and Economic Recovery DPL (P172796) from 2020 that responded to the pandemic by advancing longer-term changes that were delayed by the health crisis and that will provide resilience in the face of future shocks and stronger growth prospects. The previous operation included two prior actions that supported disaster risk preparedness through the effective functioning of the National Emergency System (*Sistema Nacional de Emergencias*, SINAE) as well as advancing the national agriculture adaptation plan to climate variability that strengthened the country's resilience within the long-term climate programs and NDC that are further supported under this operation. It also provided support to a reduction in tax expenditure to improve to build fiscal space, and measures to improve the business environment and promote competitiveness, in the spirit of the second pillar of the current operation.

42. The operation will include a proposed performance-based grant from the GPG Fund. This grant will be provided through an innovative mechanism that will allow the reduction of interest payments during the DPL repayment period based on performance in achieving targets for a Key Performance Indicator (KPI) related to climate mitigation. Building on the model of the SSLB issued by Uruguay in October 2022, the proposed mechanism responds to management's commitment set out in the WBG Evolution Roadmap[14] to develop approaches to providing concessionality to incentivize countries to address GPGs through introduction of long-term performance-based incentive mechanisms, including interest buydowns. The proposed mechanism introduces two innovative features: a) incorporating an interest buydown provision in the standard WB financing agreement; and b) extending WB capacity to incentivize GPGs outcomes beyond project closing. The operation will also be accompanied by two additional grants from the GPG Fund: (a) a grant of up to US$0.5 million to finance the retention by the Bank of an independent agency to perform the annual verification of the KPI; and (b) a grant of up to US$1.0 million to provide related technical assistance for improved livestock management practices that reduce the methane emission intensity of beef production and that are required to achieve the ambitious targets of the proposed interest buy-down.

43. In order to apply the proposed contingent reduction of interest payments, a waiver is proposed for the standard interest terms applicable to IBRD loans as set forth in the Bank Policy and the Bank Directive – Financial Terms and Conditions of Bank Financing effective as of March 13, 2023, specifically Annex 6 references to IBRD terms that are applicable to Uruguay. The proposed modifications of the loan interest terms for this operation reflect the contingent nature of the proposed financing, whereby reductions in the interest paid by the Borrower during the term of the Loan Agreement will be allowed contingent upon performance against the KPI, thus explicitly affecting IBRD financial terms. Under the proposed financial terms, performance-based reductions in the interest payable by the Borrower will be determined annually during a ten-year performance period of the IBRD loan repayment. These will be balanced by IBRD's use of equivalent amounts drawn from the GPG Fund.

44. The amount of the interest reduction will be determined such that achievement of the KPI targets in each year of the performance period will lead to a maximum US$12.5 million reduction in the total interest paid over the life of the IBRD loan.[15] The KPI proposed is as follows: reduction in the emissions intensity of methane per unit of live weight beef production with respect to the reference value of observation year 1990 (in percent). This

[14] Evolving the World Bank Group's Mission, Operations, and Resources: A Roadmap. WBG, December 2022

[15] Noting that the WB and the Government of Uruguay have agreed to consider the possibility of applying for additional financing as an incentive for early achievement of the KPI targets if new financing becomes available from one or more countries from Annex I of the United Nations Framework Convention on Climate Change.

KPI is highly relevant to achievement of Uruguay's climate mitigation goals, given that methane emissions from beef production account for 48.6 percent of national GHG emissions.[16] The reduction of interest payments will be determined annually over a ten-year performance period of IBRD loan repayment (from 2028-2037), incentivizing continuous achievement of the KPI targets and providing further additionality compared to the terms of the SSLB, for which performance is determined only once.

45. The target for the KPI reflects overachievement of Uruguay's NDC commitments, for which NDC 1 sets targets for 2025 and NDC 2 for 2030. For this KPI, NDC 1 establishes the target of a 32 percent reduction by 2025, while NDC 2 establishes a target reduction of 35 percent by 2030. The buydown will provide cumulative rewards based on overachievement of these targets, with one level of buydown available from 2028 onwards (corresponding to data from 2025 onwards)[17] for a reduction of 33 percent or more, and an incremental level of buydown available from 2033 (corresponding to data from 2030) for a reduction of 36 percent or more. To incentivize early achievement[18] of the higher target, the incremental level of buydown will be made available a year ahead of the NDC 2 target date (i.e., in 2032, corresponding to data for 2029), in which case the performance period will be reduced to nine years. Further flexibility will be provided such that if a KPI target is missed during the performance period, the nominal value of the foregone interest buydown amount maybe provided as a reduction of interest in year 11 of the repayment period, provided the missed KPI target is achieved in that year. These reductions in interest payments will be provided subject to the conditions that: (i) in no year may interest repayments become negative; and (ii) the total value of the interest repayments cannot exceed US$12.5 million. Monitoring, reporting and retention by the Bank of an independent agency for verification of the KPI will build on arrangements established for the SSLB, under which GHG emissions data are updated annually with UNDP providing verification of annual reports submitted by the government (see Annex 6 for further details).

4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

Pillar 1: Greening of the Economy

Prior Action 1: *To formalize Uruguay's climate commitments under the Paris Agreement, the Borrower has approved the second Nationally Determined Contributions (NDC) under the Paris Agreement framework, as evidenced by the UNCCS letter dated January 30, 2023, acknowledging submission of Uruguay's second NDC Submission.*

46. Rationale: Uruguay has been successful in achieving progress toward climate goals and the development of a regulatory framework to achieve these. Legal documents include the *National Climate Change Policy* (2017), as well as the *Long-Term Climate Strategy* (2022). As a signatory to the Paris Agreement, the country submitted its first NDC to the UNFCCC in 2017, establishing more than 100 adaptation and mitigation measures with specific goals for the period up to 2025.[19] Among these were the goals equivalent to a 50 percent reduction in carbon

[16] Uruguay NDC 2, December 2022.
[17] The KPI statistic is calculated on a truncated five-year rolling average to smooth inter-annual (primarily weather-based) variation, with the average for the central year incorporating data from the three preceding years plus the following year, with the maximum and minimum values excluded.[17] Allowing for an additional year to verify the data, the statistic at the start of the performance period in 2028 will relate to data for 2025, while the statistic in 2033 will relate to data for 2030.
[18] "Early Achievement" means the achievement of the KPI Target of 36 percent by the Borrower before December 31, 2030.
[19] The NDC was approved by Decree of the Executive Power Number 310 of November 3, 2017 (Decree n.310/017). See https://www.impo.com.uy/bases/decrees/310-2017

dioxide equivalent emission intensity per GDP unit while maintaining 100 percent of the area of native forests by 2025. To support these ambitious goals several key legal and institutional advances have been made, most notably with the creation of the MA in 2020 with the mandate to coordinate advances in climate policy. The 2017 NDC also established a comprehensive open measurement, reporting, and verification system, to track and monitor progress towards these targets.[20]

47. Substance of Prior Action: Under the Paris Agreement, Uruguay submitted its updated NDC in December 2022, with an increased level of ambition strengthening previous targets for climate change adaptation and mitigation. The elaboration of the NDC was informed by WB technical assistance, which helped the government build a model to assess the macroeconomic impact of different mitigation proposals. The NDC propose measures in line with Uruguay's recently approved Long-Term Climate Strategy, which establishes the goals of achieving net-zero CO_2 emissions by 2050 while stabilizing methane and nitrous oxide emissions by the same date. Uruguay accounts for 0.07 percent of global GHG emissions, emitting 34.36 million tons of carbon dioxide equivalent in 2019, with emissions principally from agriculture (72 percent) and energy-using sectors (17 percent). Measures in the updated NDC have been widely consulted with civil society and relevant stakeholders, including young people through workshops organized in collaboration with United Nations Children's Fund (UNICEF).[21]

48. Expected impacts: The second NDC represent increased ambition compared to the targets set in the 2017 NDC, in particular by: (i) setting a more ambitious goal for the reduction of the methane emission intensity of beef production, raising the target from 32 to 35 percent reduction compared to 1990, thus contributing to the reduction of Uruguay's overall emission intensity, given that methane emissions from livestock represent 48.6 percent of total GHG emissions;[22] (ii) shifting from GHG emission reduction objectives based on emissions intensity per unit of GDP in the first NDC to ones based on absolute emissions, implying a commitment from the government to limit GHG emissions regardless of GDP performance. Further, if Uruguay maintains its pre-COVID economic growth rate, the absolute GHG emissions targets presented in the second NDC represent a continued reduction of GHG emissions intensity beyond the target set for 2025 in the first NDC; (iii) having a greater scope in terms of the GHG considered, by adding a consumption reduction goal for hydrofluorocarbons .[23] In addition, the second NDC maintains the commitment to conservation by retaining the target of maintaining 100 percent of the 2012 area of native forests, implying zero deforestation.[24]

49. Implementation of the second NDC will reset the roadmap for economic growth along a greener and more resilient path, guiding policies for climate adaptation in productive sectors (especially agriculture), as well as through mitigation activities that will facilitate access to low-carbon markets, raise the potential for renewable energy exports, and provide access to climate finance and carbon markets. The results indicator is the approval of the second NDC by Decree. Baseline (2022): No. Target (2024): Yes.

[20] See: https://visualizador.gobiernoabierto.gub.uy/visualizador/api/repos/%3Apublic%3Aorganismos%3Aambiente%3Avisualizador_cdn.wcdf/generatedContent
[21] See https://www.unicef.org/uruguay/accion-climatica-joven
[22] NDC 1 set a mitigation objective for 2025 of 32 percent of reduction in CH4 emissions intensity per product unit (See Section I.I.i). NDC 2 reduction goal is 35 percent by 2030 (see Section 5.1.1.2)
[23] NDC 2 Section 5.1.1.1. sets a hydrofluorocarbons reduction goal of 10 percent by 2030 from the 2020-2022 average measurement.
[24] See NDC 2 Section 5.1.1.3.

Prior Action 2*: To enhance carbon sequestration, promote climate resilience, and protect biodiversity through the conservation of native forests, the Borrower has excluded native forests from the total property area that is used to calculate exceptions to various taxes, as evidenced by Articles 477, 478, and 491 of Law No. 20.075, dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*

50. Rationale: The conservation, registration and management of native forests or natural protective forests ("*bosques naturales protectores"*) in Uruguay are governed by the Forestry Law No. 15.939, dated December 28, 1987, which also prohibits deforestation. However, Uruguayan native forests continue to suffer pressures that could derive in degradation, deforestation and biodiversity loss as a result of illegal logging for firewood (especially in areas adjacent to population centers), as well as changes in water regimes and runoff linked to production processes and increasing pressures from invasive alien species.[25] The registration of forests with the General Forestry Directorate of the MGAP is voluntary, but it is a condition to access tax benefits that seek to incentivize the conservation of these forests. Almost all Uruguayan native forests are privately owned, and many of these owners have yet to register native forests areas and access existing tax exemptions, which points to barriers to registration and the utilization of tax incentives. Further, owners may perceive registration of forest areas as an opportunity cost in the form of foregone alternative forms of productive land use. While the coverage of native forest is close to 850,000 ha, only 580,000 ha are registered, and in 2016 only 154,000 hectares (27 percent of the total) were linked to any kind of tax exemption. To better incentivize the registration of native forests and promote their conservation, MEF proposes to create additional economic incentives through the RCBEP Law by adjusting regulations governing tax exemptions.

51. Substance of the Prior Action: The proposed reform will exclude native forest land (*bosques naturales protectores* as defined in article 8 the Forestry Law) from the total property area that is used to calculate exemptions to various taxes, including the rural real estate contribution, the primary education tax, and the agricultural wealth tax (*Contribución Inmobiliaria Rural, Impuesto a la Enseñanza Primaria, Impuesto al Patrimonio Agropecuario*). The proposed amendment provides that: (i) the area of native forest will not be counted towards the total area considered in the exemption benefiting owners with less than 200 hectares of land, who are exempt from the payment of the Rural Real Estate Contribution tax on the first 50 hectares of their property (Article 477); (ii) the area of native forest will not be counted towards the total area considered in the exemption benefiting owners with less than 300 hectares of land, who are exempt from the payment of the Primary Education Tax (Article 478); and, (iii) in the calculation of the value of rural real estate, the area of native forest will not be considered, allowing more owners of native forest to benefit from the exemption to the Agriculture Wealth Tax (Tax Law 16-9-96 (Article 491). These modifications became effective on January 1, 2023, following approval of the RCBEP Law.

52. Expected impacts: These measures will benefit those owners that cannot currently access these exemptions because consideration of their native forest area pushes their total landholding above the limit established for these incentives. Such landowners will be incentivized to protect and register native forest, as this will reduce the estimated area of their total landholding for the purposes of these taxes. Since registration is necessary to gain these tax advantages under Uruguayan law, it is anticipated that this policy will lead to an increase in native forest registrations, as well as improve native forest management, reducing deforestation and degradation. This

[25] Ministerio de Ganadería, Agricultura y Pesca (2018). *Estrategia Nacional Bosque Nativo*

measure will enhance carbon sequestration and strengthen biodiversity protection in the long term. The result indicator is area of native forest potentially covered by the new incentives. Baseline (2022): 0 hectares. Target (2024) 130,211 hectares.

Prior Action 3: *To conserve marine ecosystems and preserve blue carbon sinks, the Borrower, through Ministry of Environment (MA), has identified new Marine Protected Areas covering at least 10 percent of Uruguay's Exclusive Economic Zones ("EEZs"), established a strategy for the protection of 30 percent of Uruguay's EEZs by 2030, and identified new areas considered "relevant for conservation" covering an estimated 30 percent of Uruguay's EEZ, as evidenced by Ministerial Resolution No. 1152/022, dated December 12, 2022.*

53. Rationale: The distinctive oceanographic characteristics of Uruguay's marine EEZs make it among the most important sites for globally significant marine biodiversity, with at least 90 species of sharks and rays, several endemic, that are considered globally threatened. This marine zone is also host to five of seven known marine turtle species and 31 species of cetaceans, five of which are considered globally threatened, ranking Uruguay's marine area high in biological importance and in need for conservation. Uruguay, Argentina, and Brazil share a large coastline, but compete for resources with other countries' fishing fleets that are working within and outside of their exclusive and coastal fishery zones. Uruguay's fisheries show clear signs of exhaustion, and while these are a significant generator of food and export income valued at over US$117 million per year[26], production has been exhibiting a drastic drop in the last decade[27] falling from a high of 154 thousand tons in 1981 to around 63 thousand in 2020.[28] Marine ecosystems are also threatened by climate change, with more frequent and intense marine heat waves significantly impacting marine habitats, as well as by the potential impact of offshore energy development, including possible exploration for oil and gas and offshore wind generation. At the same time, healthy oceans are needed to provide key ecosystem services and to mitigate climate change. Models show that marine carbon uptake in the Southern Oceans is highly sensitive to the composition of the ecosystem.[29] The process of carbon storage and sequestration in marine habitats removes significant carbon dioxide from the atmosphere, with oceans accounting for about one-third of the carbon dioxide absorbed by carbon sinks on land and at sea.[30] This area in particular includes submarine canyons in which specific hydrodynamic processes occur that lead to downwelling and upwelling of deep waters, key process of marine carbon sequestration, favoring high rates of primary productivity with effects that are transferred in a cascade to the food web.[31] In the face of these threats to the integrity, biodiversity and productivity of its marine ecosystems, the Government of Uruguay announced the Uruguay Azul 2030 roadmap in June 2022. This establishes the goal of increasing Uruguay's MPA from only 0.7 percent to 10 percent of its EEZ within a year, as a first step towards protection of 30 percent of the EEZ (which covers over 140,000 km2) by 2030, in line with Uruguay's commitments to global targets under the CBD.

54. Substance of the Prior Action: To formalize the commitments made under Uruguay Azul 2030, the MA issued a Resolution in December 2022. The Resolution identifies priority areas for conservation that cover 10 percent of

[26] https://www.gub.uy/ministerio-ganaderia-agricultura-pesca/sites/ministerio-ganaderia-agricultura-pesca/files/2020-02/Bolet%C3%ADn%20Estad%C3%ADstico%20Pesquero%202016-2018.pdf
[27] Galli et al. *El complejo pesquero uruguayo: un modelo agotado*. Trabajo y Sociedad, 2022.
[28] https://datos.bancomundial.org/indicador/ER.FSH.PROD.MT?locations=UY based on FAO data
[29] Manizza M. et al. *Sensitivity of global ocean biogeochemical dynamics to ecosystem structure in a future climate*. Geophysical Research Letters, Vol. 37, L1307, 2010.
[30] Le Quéré, C. et al. *Trends in the sources and sinks of carbon dioxide*. Nature Geoscience 2, 831–836 (2009).
[31] Allen, S. E. and Durrieu de Madron, X.: *A review of the role of submarine canyons in deep-ocean exchange with the shelf*, Ocean Sci., 5, 607–620, https://doi.org/10.5194/os-5-607-2009, 2009.

the country's EEZ and is a milestone in the strategy towards the protection of 30 percent of the country's EEZ by 2030 which implies also (i) approving the S*trategy for Biodiversity Conservation*, and (ii) recognizing seven new sites relevant for conservation. To contribute to reaching the 30 by 2030 target, this Resolution recognizes seven new "areas of conservation relevance" (*sitios de relevancia para conservación)*[32], recommending the consequent approval of measures for their conservation and consideration in environmental impact assessments. To contribute to a more immediate target of increasing protected areas within the country's EEZs, the Resolution mandates the selection and delineation of three of these "areas of conservation relevance" to be established as MPA ("*Isla e Islote de Lobos", "Área de Cría Permanente de Merluza", "Margen Continental* and *Talud"*).

55. The measures included in the Strategy for Biodiversity Conservation are primarily focused on conserving marine biodiversity and promoting carbon removal and sequestration. They include protection of the deep sea reefs and seabed from disturbances (e.g., by bottom-trawling fishery) leading to reduced carbon emissions from disturbed sediments; protection of the water column and its associated fauna including through the restriction of emission of pollutants (e.g. sounds, light, solid waste, liquid effluents), and the development of activities that due to their modality and intensity could affect the conservation values of the highlighted sites. By putting in place meaningful protection for newly created MPA, Uruguay will also help ensure the continued effectiveness of its carbon-rich ocean habitats in providing powerful climate mitigation and adaptation.[33] The commitments announced by Uruguay are in accord with the draft of the Global Framework for Managing Nature Through 2030 released by the CBD in July 2021, which includes the milestone of conserving and protecting at least 30 percent of Earth's lands and oceans

56. Expected impacts: The establishment of MPAs within Uruguay's EEZ will serve to ensure the conservation of the ecosystems and species of its marine zone, many of which are threatened at a global level because of both climate change and direct human intervention. By putting in place meaningful protection for newly created MPA, Uruguay will not only conserve marine biodiversity, but will also help ensure the continued effectiveness of its carbon-rich ocean habitats. As the network of connected MPA is extended to cover 30 percent of Uruguay's EEZ, it will strengthen ecosystem resilience in the face of increased pressure on fishery stocks, and alterations in their composition and productivity due to climate change. Furthermore, the creation, management, and monitoring of new MPA in Uruguay's EEZ provides an important opportunity to contribute to global knowledge of marine carbon sequestration in these ecosystems, its linkage with marine ecosystem integrity, and the development of relevant carbon accounting methodologies. The Ministerial Resolution is a crucial first step for Uruguay in demonstrating commitment with respect to protecting its marine areas, and more broadly the country's long-term vision for its natural assets. In turn, this will provide powerful support for Uruguay's sustainable finance agenda, through which the country is actively seeking to diversify its investor base by boosting ESG-linked investments, including through issuance of sustainability linked SSLBs. The results indicator is number of new MPA created: Baseline (2022): 0. Target (2024): 1.

Prior Action 4: *To advance environmental and social sustainability and climate goals and expand trade opportunities for low-carbon organic agricultural products, the Borrower, through the Ministry of Livestock,*

[32] *"Banco Inglés", "Isla e islote de Lobos", "Restignas Pez Limón", "Pozo de Fango"," Zona de moluscos", "Área de Cría permanente de merluza" and "margen continental y talud"-*

[33] Fixed MPA, covering both the seabed and overlying water column play a vital role in building ecological resilience and help to long-term support for marine life to adapt to changing conditions, such those likely to occur due to climate change. Furthermore, conserving geographical features that are structurally complex (e.g., coral reefs, submarine canyons and seamounts) are likely to remain important to marine life even in a changing world (Tittensor et al. 2019).

Agriculture and Fisheries (MGAP), has systematized the certification of organic and integrated agricultural and aquaculture production, as evidenced by Decree No. 175/022, dated May 24, 2022 and published in the Official Gazette on May 31, 2022.

57. Rationale: In 2019, over 224,000 farmers in Latin America and the Caribbean managed nearly 8.3 million hectares under organic production (FAO, 2021).[34] In the same year, Uruguay had 2.1 million hectares under organic production (mostly grasslands and grazing areas), second only in the region to Argentina (3.7 million hectares) and among the top ten countries globally, constituting 15.3 percent of total agricultural land in the country. A principal export market for Uruguayan beef is the European Union, where organic products command a premium price.[35] Article 156 of Law 19.996, dated November 3, 2021, confirms that the Executive Branch regulates the certification of organic agricultural production, aquaculture, and integrated agricultural systems. Responsibility for this certification is assigned to the MGAP, through its General Directorate of Agricultural Services (DGSA), General Directorate of the Farm (DGG), General Directorate of Livestock Services (DGSG) and National Directorate of Aquatic Resources (DNRA).

58. Substance of the Prior Action: The Decree establishes the National System of Certification for Organic Production[36] and Integrated Production[37], in which producers can voluntarily participate. The Decree also: (a) creates a National Register of Certifiers (updated every two years); (b) sets norms for determining domestic organic production and organic imports; (c) establishes a Screening Committee that provides norms for determining certification for integrated production; and (d) establishes administrative procedures to formalize organic certification and permit organic labeling of products.

59. Expected impacts: Organic agricultural production is expanding rapidly in Uruguay, increasing in land area by 14 percent in 2018 in comparison to the previous year. Organic agriculture benefits the environment by avoiding synthetic fertilizers and chemicals and is less energy intensive, reducing its carbon footprint while promoting practices that increase farm biodiversity and soil carbon.[38] The Decree harmonizes organic certification across the agricultural sector, establishes a national registry of certifiers, and increases transparency in the procedures required to obtain certification. The result indicator is the number of certifiers of organic agricultural production registered under the national system. Baseline (2022) 0; Target (2024) 3.

[34] https://www.fibl.org/fileadmin/documents/shop/1150-organic-world-2021.pdf
[35] At present and prior to PA 5, organic beef certification in UY has been driven by specific value chains, e.g., Wegmans' Food You Feel Good About Organic Beef program(https://en.integracionagropecuaria.com/post/uruguay-is-one-of-the-best-source-for-grass-fed-organic-beef-forbes-1). Uruguay's strong (and mandatory) cattle traceability also greatly facilitates this and will serve as a benchmark for organic certification of other agricultural produce.
[36] Methods of sustainable production with management practices that preserve natural Resources, biodiversity, and the environment without use of synthetic chemical inputs or genetically modified organisms or their derivatives.
[37] Focused on ecological management practices, integrated production practices use their on-farm interaction and the surrounding landscape to optimize resource use, minimize external inputs, and encourage environmentally friendly technology packages.
[38] Given that organic certification requires both traceability and verification, there are additional transaction costs vis-à-vis conventional agricultural production. Farmers' decisions to pursue (and maintain) organic certification will be informed by perceived differentials in margins, compared to existing non-organic market opportunities. In terms of climate impacts organic agriculture generally does not allow petroleum-based fertilizers and synthetic chemical pesticides which lowers its carbon footprint.

Prior Action 5: To foster the production and use of green hydrogen as a clean fuel to decarbonize freight *heavy industry and agriculture, the Borrower, through Ministry of Industry, Energy and Mining (MIEM), has created the program "Fondo Hidrógeno Verde" to promote innovation and research in Green Hydrogen and its derivatives, as evidenced by the agreement between the MIEM, Uruguay Technological Laboratory (LATU), and National Agency of Research and Innovation (ANII), dated March 30, 2022.*

60. Rationale: Since 2008, Uruguay has almost fully decarbonized its electricity generation, with 97 percent of its electricity matrix provided by renewable energy sources. To continue the subsequent phase of its decarbonization transition, Uruguay seeks to reduce emissions in other economic activities (i.e., transport and industry) through the adoption and use of greener productive processes. Green hydrogen and its product derivatives have emerged as a potential source of energy with high value-added and export potential within this new phase of Uruguay's transition. However, competitive green hydrogen production is at its nascent stages and technological innovation is key. Uruguay historically reports low levels of expenditure in research and development, which is highly cyclical and mainly carried out by the public sector (close to 70 percent of all expenditures). This underperforming innovation ecosystem hinders the use, adoption, and spillover of new technologies within productive processes, which can constrain Uruguay's potential to transform into a key exporting player for Green Hydrogen in the long run (2040). To foster the low-carbon transition and address the persistent challenges regarding innovation, the government has in the past taken actions to promote innovation in sustainable energy sources, including the creation of sector programs, such as the Energy Sector Fund (*Fondo Sectorial de Energía)* and the Circular Economy Sector Fund *(Fondo Sectorial de Economía Circular)* , focused at tackling innovation challenges associated with energy and circular technologies, and improving the institutional framework around clean technologies. In addition, the government has developed a roadmap for Uruguay to position itself within the global Green Hydrogen market by 2040[39], with estimated sales of up to US$2.1 billion annually (around 20 percent of current exports) and the capacity to generate close to 35 thousand jobs.

61. Substance of the Prior Action: This operation supports the government's efforts to promote the development of Green Hydrogen (GH2)-related technologies, to better understand its complexities and build safeguards and capacities that would allow for an effective regulation of a sector with potential comparative advantages. To this end the MIEM, LATU, and the ANII have created the program, "*Fondo Hidrógeno Verde"* (Green Hydrogen Fund) to finance projects associated with research, innovation, and development of Green Hydrogen and related products for up to US$10 million.[40] This program builds a transparent, rules-based institutional framework to crowd-in private investments in green hydrogen projects, fosters Uruguay's transition to cleaner energy, promotes innovation in emerging technologies, and builds state capacity around a nascent technology of potential critical importance in the future. The fund will finance these innovation projects, which will be selected from an ongoing open call for proposals directed at the private sector, organized, and evaluated by the ANII.[41] The operation of this program will be similar and builds from previously implemented programs, such as the Energy Sector Fund (*Fondo Sectorial de Energía*), which helped the country promote its first energy transition since 2008. These previously implemented programs supported projects that aided Uruguay's decarbonization of its electricity matrix through pilot projects in wind and solar energy.[42] The program has already launched the call-for-proposals and has selected

[39] MIEM (2022), "Hoja de ruta del hidrógeno verde en Uruguay", junio 2022.
[40] In 2022, this fund carried out a call for project proposals within the Green Hydrogen innovation space. The ANII selected a project to receive funding for US$10 million. The fund's beneficiary will develop the project for a period of at most 13 years, with a maximum of three years allocated to a pre-operations phase and a maximum of 10 years allocated to operations.
[41] The selection criteria will take into account administrative, financial, and technical aspects, made public in https://www.anii.org.uy/apoyos/innovacion/303/convocatoria-a-proyectos-de-hidrogeno-verde/
[42] For example, the pilot of the Installation of an Aerogenerator in Uruguay resulted in a very high penetration of wind energy, with a

the first project which will benefit from the fund. The project was chosen based on its potential to dynamize innovation in renewable energies and its ability to help build the capacities required to catalyze Uruguay's Green Hydrogen sector.

62. Expected impacts: The policy measure will support the investment in activities critical to establishing the initial stages of this new industry, and in the process help Uruguay build capacities and understand the technologies to better regulate the sector in the future. This will help Uruguay to continue its decarbonization process through a higher dependance on Green Hydrogen, but also help dynamize the innovation ecosystem associated with greener and circular technologies. While still nascent in terms of markets and technology, this action can be considered MFD enabling as the Government seeks to promote private investment into this new industry. The proposed result indicator is the issuance of regulation specific to GH2 activities, informed by the new capacities that are generated by the program's beneficiary projects. Baseline (2021): No regulation specific to green hydrogen production and derivatives. Target (2024): Issuance of regulations specific to green hydrogen production and derivatives.

Pillar 2: Stronger and more Resilient Growth

Prior Action 6: *To promote food and essential goods price resilience against climate and global shocks and foster a competitive tradable sector, the Borrower, through MEF, has: (i) reduced its common external tariff on average by 10 percent in agreement with its Mercosur partners, as evidenced by Decree* No. *369/022, dated November 11, 2022, and published in the Official Gazette on November 24, 2022, that adopted Mercosur's Common Market Council Decision No. 8/22; and (ii) reduced the import charges for assessing regulatory conformity for imported food items from 1.5 percent to 0.5 percent, as evidenced by Decree No. 194/022, dated June 14, 2022, and published in the Official Gazette on June 20, 2022.*

63. Rationale: Uruguay's economy is relatively closed to trade with limited integration into global value chains (GVCs). The average import tariff was 10.3 percent in 2021, well above the level of regional comparator countries, such as those in the Pacific Alliance with an average tariff of 5.3 percent for the same year.[43] Non-tariff measures (NTMs) further restrict trade flows. A large number of imports are subject to NTMs in Uruguay: based on 2018 data, over half of all product categories (53 percent of HS 6-digit product codes) are subject to at least one NTM.[44] These trade barriers hinder the country's growth potential, hamper export diversification, limits investments as well as the country's ability to smooth shocks such as those linked to climate change, which are already affecting food production and distribution systems throughout the world.[45] The current global food crisis and Uruguay's dependence on the agriculture sector, which is itself climate-vulnerable, can place additional pressure on food prices if no measures are put in place. To address these challenges, the government has advanced negotiation in free trade agreements (FTAs)—including concluded FTAs with the European Union and the European Free Trade

installed capacity of 1.514 MW. Likewise, the pilot of the Installation of the Photovoltaic Solar Plant helped develop local capacities, train professionals and technicians, and evaluate the performance of this solar technology within the electricity matrix. Furthermore, it helped develop the first call for the large-scale introduction of photovoltaic solar energy, which resulted in the subsequent installation of 228.3 M W.

[43] WTO, ITC, UNCTAD (2022). The average for the Pacific Alliance is the simple average of Peru (2.4 percent), Colombia (5.8 percent), Chile (6 percent), and Mexico (7.1 percent).

[44] Staff calculation from UNTACD TRAINS data. This share of products subject to NTMs is higher than in more GVC-integrated regional peers such as Mexico (47 percent) and Costa Rica (38 percent).

[45] Brenton, P., Chemutai, V., & Pangestu, M. (2022). Trade and food security in a climate change-impacted world. *Agricultural Economics*, 53, 580– 591. https://doi.org/10.1111/agec.12727

Association, an expanded bilateral FTA with Chile, and ongoing negotiations, among others, with South Korea and Singapore—and implemented trade reforms, among them the reduction of certain import tariffs below the Mercosur levels. Uruguay applies the common external tariff (CET) as part of Mercosur, but it can set tariffs independently of the CET for a determined number of tariff lines.[46] Additionally, special regimes currently applied under the Mercosur allow for deviations from the CET for tariff lines identified in the Mercosur schedule as information and telecommunication products and as capital goods. Based on these flexibilities, Uruguay set tariffs below the CET in 2021 for 1,154 tariff lines, including a wide range of capital and intermediate goods. More recently, together with Brazil, Uruguay has extended duty-free treatment for products originating in either country's special economic zones (previously only granted temporarily and to certain zones), if the traded goods meet the Mercosur's rules of origins.[47] This would drop tariffs charged in Brazil to Uruguayan exports from all its special economic zones, as well as tariff barriers in Uruguay for imports from the Manaus special economic zone, further integrating bilateral trade with Brazil.

64. Substance of the Prior Action: This operation supports the government's efforts to continue improving supply-side measures to promote food and essential goods price resilience against climate and global shocks and foster a competitive tradable sector. In July 2022, the parties to the Mercosur agreed to the first significant tariff reform since the incorporation of their CET in 1995. This is an extensive tariff reform whereby Uruguay reduces import tariffs for about 86 percent of tariff lines with nonzero duty rates. The resulting CET is on average 10.3 percent lower than prior to these reductions by Uruguay (not including deviations to the CET from the application of national exceptions or other flexibilities). In addition to tariffs, imports of food and beverages are subject to technical requirements (in the form of sanitary, phytosanitary, or technical standards) that were charged a para-tariff of 1.5 percent for attesting conformity and issuing the necessary import certificates, which has been reduced under the prior action to 0.5 percent. This same reform also creates an inter-ministerial working group to introduce risk management criteria for all government bodies with control functions in import operations of food and beverages.

65. Expected impacts: The reduction of tariffs, para-tariffs, and controls for imports can be particularly beneficial for firms that import inputs as it has the potential to substantially reduce uncertainty and trade costs, increase efficiency, and boost firm competitiveness. Moreover, as Uruguay is a net importer of edible vegetables and prepared foodstuff and beverages, the elimination of trade barriers will promote food security, by reducing prices for imported foodstuff and attenuating price volatility[48]. The proposed result indicator is the share of imports, by value, subject to reduced import tariffs, certificate fees and risk-management controls. Baseline (2021): 0 percent. Target (2024): 58 percent.

Prior Action 7: *To strengthen its competition policy framework, increase market contestability and foster legal certainty, the Borrower, through MEF, has: (i) created and operationalized a network of regulators with competition enforcement powers, to reinforce interinstitutional cooperation and promote information sharing as evidenced by a Framework Collaboration Agreement signed on November 22, 2022; and (ii) strengthened merger control rules by enabling more thorough analysis in problematic cases and approving technical norms clarifying*

[46] Tariff lines under the Mercosur's nomenclature involves about 10,300 products at the 8-digit level (revision VI).
[47] Additional Protocol No. 83 to the Economic Complementation Agreement between Brazil and Uruguay (ACE No. 2) under the Latin American Integration Association (ALADI). This agreement has been approved in Uruguay via Decree No. 226/22 of July 19, 2022, and it would enter into force after a similar decree is issued in Brazil.
[48] Brenton, P., Chemutai, V., & Pangestu, M. (2022). *Trade and food security in a climate change-impacted world*. Agricultural Economics, 53, 580– 591. https://doi.org/10.1111/agec.12727

key elements of the regulatory framework, as evidenced by Article 147 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022, and Resolution No. 175/022 dated August 23, 2022.

66. Rationale: Competition tends to foster cost reductions, innovation, productivity, and economic growth,[49] shift market share toward more efficient producers and induce firms to become more efficient.[50] Additionally, firms in competitive markets are more likely to succeed in international markets. Yet, Uruguayan markets are perceived to feature weaker anti-monopoly enforcement levels than peer countries in the region including Mexico, Brazil, and Argentina[51] and enforcement against anticompetitive practices, notably cartels, has been limited. Between 1980 and 2021 in Uruguay only four cartels have been sanctioned. Two factors contributed to these results: (i) since 2007 and until November 2021, sector regulators were responsible for enforcing the Competition Law in their respective industries, an institutional arrangement that proved inefficient, as they were rarely active or effective in sanctioning anticompetitive practices; and (ii) merger control powers were limited. Thus, economic concentrations did not systematically benefit from a review of their competition impact. In the past few years, key reforms to the Competition Law tackled these concerns by transferring to the CPDC the mandate to investigate and sanction anticompetitive practices in regulated sectors while regulators kept their mandate to review mergers and acquisitions; and expanding the mandate to control anticompetitive effects of mergers and acquisitions. On the one hand, these reforms opened the door for more effective antitrust enforcement in Uruguayan markets. On the other hand, they require additional measures to support effective implementation, especially by promoting interinstitutional cooperation between the CPDC and sector regulators.

67. Substance of the Prior Action: Developing secondary legislation to support the effective implementation of the recent changes to the competition policy framework incorporated in LUC for fighting anticompetitive practices and strengthening merger control. First, the creation and operationalization of a network of regulators with a competition mandate promotes cooperation between CPDC and the sector regulators drawing on their respective expertise and supports effective implementation of the competition law. Sector regulators in particular play a vital role in identifying anticompetitive practices which may later be referred to the CPDC for investigation. Conversely, merger control in regulated sectors could benefit from the CPDC's experience and expertise in the implementation of the Competition Law. The Memorandum of Understanding is a framework agreement that created and operationalized a network of regulators with competition enforcement powers, that provide a mechanism for this information sharing to take place. This is a key step to building solid decisions and can also help embedding competition principles in regulated sectors. Second, with respect to merger control, this Prior Action reforms the Competition Law to allow the CPDC to "stop the clock" in more complex mergers (i.e., those that have moved to additional scrutiny through a Phase II review due to potential concerns in terms of market impact). This measure, which follows the approach of leading jurisdictions such as the European Union, will enable merging parties to respond adequately to information requests and ensure that potentially problematic mergers are analyzed without statutory deadlines being the reason for risking the robustness of merger decisions. In addition, the CPDC

[49] Bassanini and Ersnt, 2002; Acemoglu et al., 2007; Aghion and Griffith, 2008; Bloom, Draca and Von Reenen, 2011.
[50] Kitzmuller and Licetti, 2013; Buccirossi et al., 2009; Voigt, 2009.
[51] WEF Global Competitiveness Report (GCR)

clarified after public consultations key technical terms which are essentially measures to protect the rights of the parties and increase legal certainty and predictability such as the definition of business assets and relevant turnover for notification, as well as the concept of modification of control and potential exemptions from merger review.

68. Expected impacts: Global estimates suggest that the presence of a cartel increases consumer prices by an average of 49 percent, and prices can rise by as much as 80 percent when cartels are especially strong.[52] Solid merger control frameworks can generate significant consumer savings. Strengthening the ability of the CPDC to tackle anticompetitive practices, notably cartels, and limit anticompetitive effects of problematic mergers and acquisitions will thus be key to lower prices, improve the quality of key staples, and promote economy-wide efficiency, food security, and economic resilience. The measures supported in this prior action are expected to increase the number of antitrust decisions and advocacy opinions issued: Baseline (average 2021-22): 14. Target (average 2023-24):17.

Prior Action 8: *To promote investment and credit in domestic currency and longer-term financial instruments, the Borrower has issued measures to: (i) homogenize rates for returns in indexed and nominal Uruguayan Pesos; (ii) reduce tax rates for returns in local currency and longer-term investments; and (iii) homogenize tax rates and terms for returns on investments in bank deposits and market instruments, as evidenced by Articles 485 and 487 of Law* No. *20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*

69. Rationale: Credit to the private sector in Uruguay is low (at 30 percent of GDP, it compares poorly with regional peers such as Peru, Colombia, Brazil, and Chile, which show figures between 50 and 80 percent of GDP), thus limiting the effectiveness of financial intermediation, hindering productivity gains, and limiting the possibilities for families and firms to buffer the negative effects of shocks. Moreover, 75 percent of bank deposits and 90 percent of the corporate sector debt are in US Dollars, and around 95 of total bank deposits are short-term (below 1 year). [53]A highly dollarized financial system is an obstacle to capital market development since high dollarization prevents investors from having a reliable benchmark for investments in nominal peso beyond the short term. [54] The BCU and the MEF are carrying out a strategy to promote financial deepening and de-dollarize the economy, with complementary measures at the macro and micro level. At the macro level, the BCU has committed to curbing the historically high levels of inflation, which hinder the development of credit markets in domestic currency. It has done so by imposing a tight monetary policy stance, a reduction in the inflation target range, and institutional reforms to bring the BCU closer to best practices. It has also reduced legal reserve requirements for peso deposits. At the micro level, it has mainly focused on three aspects: changes in debt policy such as reducing public debt issuance in foreign currency, the promotion of de-dollarization of domestic prices (particularly durable goods) in coordination with private stakeholders, and micro reforms in the financial system. [55] On the latter, in

[52] World Bank. 2021. Fixing markets, not prices. Policy options to tackle economic cartels in Latin America and the Caribbean.
[53] Half of total banking sector loans (including households and corporates) is in US Dollars, as households hold most of their loans in local currency.
[54] Almost all domestic securities with maturities beyond 2 years are either denominated in US Dollars or indexed to inflation/wage growth, with the (limited) exception of the 4-year notes issued by the government. The money market is the only segment where the peso is the main currency used.
[55] Public sector securities represent 90 percent off all traded securities (US$40 billion or 80 percent of GDP). The share of FX-denominated government securities stands below 50 percent (compared to almost 95 percent in the early 2000's). Currently, all government securities

addition to measures to boost the development of derivatives' markets, the authorities identified the need for adjustments to tax incentives for investments in financial instruments as a relevant element of the overall strategy to foster long-term peso financing.

70. Substance of the Prior Action: Prior to the introduction of Law N° 20.075, some tax rates applicable to investments in dollars were of the same magnitude as for investments in local currency. Moreover, by having the same tax rate across some instruments in nominal and indexed pesos, the income tax scheme penalized investments in nominal peso relative to indexed peso. The reason is that the tax base differs in both situations: nominal interest income in the case of nominal peso investments, real interest income in the case of indexed investments. Since nominal returns are higher than real returns for any positive level of inflation, having the same tax rate discriminated against nominal peso investments. In addition, tax rates for longer term instruments were sometimes of the same magnitude as for short term ones. Finally, there were differences in the applicable tax rates for returns on investments in bank deposits and on market instruments. Articles 485 and 487 of Law N° 20.075 substitute Title 7, Article 26 and Title 8, Article 14 of the *Texto Ordenado* from 1996 (Decree N° 338/996), respectively, homogenizing tax rates and terms across different financial instruments, and providing tax incentives for investment in local currency and longer-term instruments (see details in the Table below). The reduction of fiscal revenues resulting from these measures is estimated at US$2.6 million per year.

71. Expected impacts: The tax adjustments aim at expanding the saving base that can be channeled to credit in peso, thus reducing the exposure of the real economy and the financial sector to external shocks,[56] and at expanding the supply of longer-term financing, which is beneficial for the financial management of local companies. Therefore, the proposed results indicator is the share of bank deposits (both nominal and indexed peso) over total deposits (in any currency). Baseline (average 2022): 25.5 percent. Target (average 2024): 27.5 percent.[57] Furthermore, this prior action is MFD enabling as the improved/harmonized tax regime is expected to have a positive impact on local currency and longer-term investments in the short- to medium-term.

Table 4. Income tax rates applicable to returns on investments in financial instruments (in %)

issued domestically are denominated in (mostly indexed) peso.

[56] A reduction in vulnerabilities associated to dollarization allows the financial sector and the real economy to better withstand other shocks, such as those derived from climate risks.

[57] Baseline and target are expressed in December 2022 prices using the Uruguayan Consumer Price Index for series in Uruguayan Pesos, and the US Consumer Price Index for series in US Dollars. Series in real US Dollars are then expressed in Uruguayan Pesos using the average exchange rate for December 2022 (40.07 Uruguayan Pesos per US Dollar) to avoid fluctuations due to exchange rate swings.

Income tax rates applicable to returns on investments in financial instruments (in %)								
	Before Law 20.075				After Law 20.075			
Type of instrument	**Term**	**USD**	**Indexed pesos**	**Nominal pesos**	**Term**	**USD**	**Indexed pesos**	**Nominal pesos**
Bank deposits	<1 year	12	12	7	<1 year	12	10	5.5
	>1 year	12	7	7	Between 1 and 3 years	12	7	2.5
					>3 years	7	5	0.5
Market instruments	<3 years	12	12	12	<1 year	12	10	5.5
	>3 years	7	7	7	Between 1 and 3 years	12	7	2.5
					>3 years	7	5	0.5

Prior Action 9: *To provide risk mitigation and expand financing for rural and agricultural family businesses led by women, the Borrower, through National Development Agency (ANDE) and National Financial Corporation Administrator of Investment Funds SA (CONAFIN AFISA), has operationalized the Guarantee Fund for the Implementation of Rural Development Policies (FOGADER), by executing two agreements with financial entities, as evidenced by the agreement executed between CONAFIN AFISA and Uruguayan Foundation for Solidarity Cooperation and Development (FUNDASOL), dated March 10, 2022, and the agreement executed between CONAFIN AFISA and República Microfinanzas S.A, dated March 8, 2022.*

72. Rationale. One of the barriers encountered by Micro, Small and Medium Enterprises in accessing capital is the lack of a financial instrument suited to the sector, followed by the lack of collateral. Further, according to ANDE the number of credits granted, the sophistication of financial products accessed, and the amounts allocated are on average significantly lower for women than for men. The financial gender gap is particularly prevalent in the agriculture and livestock sectors where women represent 44 percent of individuals in the Family Production Registry as of 2020. [58] Furthermore, Florit et al. (2013) found important gender gaps within the registered owners of family farms applying for subsidies, as 87 percent of male owners were also the main decision-makers, compared to only 34 percent of female owners. Bernheim (2018) surveyed women working in dairy farms, horticulture and cattle raising and found that 44 percent participate “little or nothing” in decision-making, and that 28 percent wished they could participate more. Among the main factors limiting women’s access to credit are cultural and social barriers, guarantee requirements, lack of self-confidence, lack of role models, and scarcity of credit products aimed at women. Previously existing credit guarantee schemes (i.e., SiGa) helped ease access to finance for firms that do not have the necessary amount and type of assets that could serve as collateral for the loan. However, those are not designed to cover individuals without a constituted firm (i.e., without a taxpayer ID number). Given the multiple barriers that women, particularly in the rural sector, face to constitute their business into a legal entity, facilitating credit to support their economic activities can actually help them develop to grow into a business entity and then access other available instruments.

73. Substance of the Prior Action. Within the framework of the National Plan on Gender Policies in Livestock and Agriculture, the Rural Women Guarantee Fund, co-financed by the MGAP, the ANDE and the MEF, was launched on 31 May 2021.[59] Its objective is to increase the proportion of women who receive State support for agricultural and livestock production, by providing partial guarantees to credits from microfinance institutions to women in the rural and agriculture sectors, enrolled in the MGAP Registry of Family Producers.[60] The US$500,000 Fund,

[58] UN Women (2021), Mapping the status of impact investments with a gender perspective in Uruguay. Montevideo
[59] But it started operating in the second half of 2021.
[60] Unlike the credit guarantee scheme under SiGa, which requires the taxpayer ID number of the company, this program only requires the personal ID card of the final beneficiary.

managed by a dedicated trust, has a leverage ratio of 1.5 and a coverage ratio of up to 70 percent, giving it a financial capacity to support up to US$1 million in credit to women's productive enterprises. Credit amounts vary between US$1,500 and US$9,000,[61] with terms between 3 and 60 months. Credits guaranteed by this program are subject to the maximum interest rate cap for micro-enterprises set by the BCU. The referred agreements signed by CONAFIN AFISA, and financial institutions represent the execution stage of the policy. To date, five microfinance institutions have signed participating agreements, and two of them have already provided guaranteed credits to rural women.

74. Expected Results and Indicators. The prior action will allow microfinance institutions to increase credit to women in family farms and small rural firms. In a country with 3.4 million inhabitants and predominantly urban (95.6 percent of the population in 2021), the universe targeted with this program is relatively small in absolute numbers. Yet its aim to close financial and gender gaps for this relegated group is relevant, particularly in the medium term, where a direct and sustainable link is expected to be generated between women and financial institutions. The credit guarantee fund is available to more than 16,000 women enrolled in the MGAP Registry of Family Producers. The implementation of this fund is expected to help reduce the gender gap in access to financing in family farms and rural Micro, Small and Medium Enterprises. In addition, the prior action is Private Capital Enabling (PCE) through these credits that are advanced. The proposed results indicator is the cumulative credits granted to rural women. Baseline (2022): 138. Target (2024): 300.

Table 5: DPL Prior Actions (PA) and Analytical Underpinnings.

PA	Analytical Underpinnings
Pillar 1: Greening of the Economy	
1.	Uruguay's fourth Biennial Update Report to the UNFCCC (2021) shows percent of global emissions, emitting 34.36 million tons of carbon dioxide equivalent. Also, emissions from sector and gas such as from agriculture (72 percent) and energy-using sectors (17 percent).[1] *WBG Country Partnership Framework Uruguay 2022*. The framework includes as objective tracking progress on decarbonization and resilience to climate change.
2.	In its first NDC, approved by Decree No. 310/017, Uruguay committed to maintaining 100 percent of its native forest from a 2012 baseline (849,960 ha) through 2025 unconditionally, and conditional on additional support, increase it by 5 percent to 892,458 ha by 2025. Uruguay is a recipient of the Forest Carbon Partnership REDD+ Readiness Fund which is enhancing its capacity on REDD+ through demonstration activities and baseline assessments, including a forest reference emissions level. The key drivers of deforestation and degradation in Uruguay have been identified as the expansion of the agricultural and forestry frontier, livestock management, illegal logging, infrastructure projects, urbanization, and extraction of aggregates. These causes are distributed according to the type of forest and regions of the country. According to the report on the assessment of tax policies associated with native forests produced by the REDD+ Project in Uruguay (2019), the existing system of tax exemptions could be improved to better adapt existing tax incentives to support forest conservation by making them more coherent in certain cases and facilitating their utilization in others. One of their key recommendations was to exclude the area of native forest in the determination

[61] These amounts are higher than those under the Rural Microcredit Program (managed by the MGAP), which has a maximum credit amount of around US$1,500.

	of existing cut-off values for tax exemptions whose taxable base is related to the property or the area of the establishment, to encourage the conservation of existing native forest in private lands and their registration, which would further enable the regulation and monitoring of their management.[3] While economic valuations of ecosystem services from forests have not yet been carried out in Uruguay, international meta-analyses point to ranges of values that are much higher than the expected tax burden (estimated as US$3 million per year for registered forests) from these fiscal incentives for its biodiversity, water conservation, and carbon sequestration services.
3.	According to the International Union for Conservation of Nature data that evaluated 223 species from the Patagonian region, Uruguay's marine EEZ houses 90 endangered species of sharks and rays and 5 endangered species of cetaceans. Sullivan Sealey K, Bustamente G (1999) describe the marine biodiversity of Argentina and Uruguay as characterized by high biological productivity, and one of the geographic priorities for marine conservation in Latin America. CBD data highlights that Uruguay's coasts are characterized by high productivity in biological terms, with a marked increase in productivity occurring in a west-east trajectory (towards the Atlantic Ocean), resulting from the confluence of mainland and oceanic waters, while overfishing during some periods represents a major threat to region's biodiversity. Roberts et al. (2017) argue that marine reserves and protected areas represent a viable low-tech, cost-effective climate adaptation strategy. In addition, the process of carbon storage and sequestration in marine habitats removes significant carbon dioxide from the atmosphere, with oceans accounting for about one-third of the carbon dioxide absorbed by carbon sinks on land and at sea (Le Quéré, C. et al., 2009). Kelp in particular, is estimated to be a significant contributor to global carbon sequestration and may be a critical component of global climate mitigation. (K. Filbee-Dexter et al., 2020). Galli et al. (2022) evaluate the current state of over-exploitation and poor management of Uruguay's fishing resources. Gianelli et al. (2019) provides quantitative evidence of the ocean warming increasingly affecting Uruguayan industrial fisheries during the past decades and highlight the subsequent need to consider environmental changes to properly manage fish stocks, particularly those shared with neighboring countries.
4.	Uruguay's agriculture sector accounts for 77 percent of the country's export earnings and is key to national growth and global competitiveness. Over the period 2005-2015, exports averaged 26 percent of GDP, while in 2020 even during the COVID pandemic, agricultural product exports (notably, beef and soya) remained together at around 37 percent of total exports. Rapid export growth has been accompanied by job creation in export sectors, and about 13 percent of jobs are currently linked to primary and agro-industrial production. Uruguay is strongly committed to building a more efficient, resilient, inclusive, and sustainable agricultural sector. The agro-ecological Law No. 19.717, dated December 21, 2018, declared of national interest the promotion and development of production, distribution, and consumption systems based on agro-ecological principles. A National Honorary Commission was created to prepare, coordinate, and supervise the implementation of the National Agroecology Plan.
5.	The "*Hoja de Ruta del Hidrógeno Verde*" (MIEM, 2022) provides a roadmap that places the production of Green Hydrogen and its derivatives as a key instrument to foster Uruguay's second stage of energy transformation, which seeks to decarbonize the entire energy sector. Promoting the production of Green Hydrogen at national level will contribute to the diversification of the national productive matrix, by creating additional value through the production of this energy source and increasing the country's export competitiveness in this sustainable product. The RCBEP Law (2021) reports that innovation in Uruguay is underperforming relative to peer countries, and it is mainly carried out by the public sector. Furthermore, there are weak innovation linkages between the private sector and public research institutions. At the same time, the said RCBEP Law posits that green technologies associated

	with renewable energy sources, such as green hydrogen, are priority areas of innovation as the country seeks to increase innovation and, at the same time, transition into a less carbon intensive economy.
Pillar 2: Stronger and more Resilient Growth	
6.	Zaclicever and Pellandra (2018) use firm-level data for Uruguay over the period 1999-2008 that shows that imports can enhance domestic firms' performance and be a principal channel for productivity growth. Uruguayan manufacturing firms exhibited positive productivity gains from increased access to intermediate input varieties, which can be larger with respect to imports with larger technology embodied from the most advanced countries. World Bank (2019) shows that trade can be a pathway to development for many countries in the Latin America and the Caribbean region and estimates positive economywide effects for Uruguay from engaging in a deep trade agreement, like the recent agreement with the European Union, that liberalizes trade in Uruguay. Estrades and Santos (2020) identify the liberalization of the Mercosur trade regime and domestic reforms to consolidate trade facilitation, reduce duties and charges to trade, and to attract foreign investment as principal actions to undertake in Uruguay.
7.	*Banco Mundial (2015) Notas de política Uruguay: Desafíos y Oportunidades 2015-2020. Capítulo: Alentar el buen funcionamiento de los mercados en Uruguay a través de un marco de políticas de competencia mejorado*. Argues that if Uruguay had a more effective competition policy framework, the functioning of the markets could be improved by facilitating entry and guaranteeing that all companies interact under equal conditions, as well as penalizing and preventing anti-competitive conduct. Based on the analysis of international best practices and the specific context of Uruguay, two recommended pillars to achieve this objective are: promoting regulations that favor competition in key markets and improving the regulatory framework for competition. *World Bank (2015) Uruguay: Towards a More Effective Regulatory Framework for Competition Law*. The design and implementation of the regulatory framework established by the competition law still lacks some crucial elements to foster procompetitive and open markets. Divided mandates on competition enforcement require strengthened interinstitutional cooperation between the Commission and sector regulators to embed competition policy principles in Uruguay's regulatory environment as well as to strengthen antitrust enforcement. The Uruguay regulatory framework on merger control could be strengthened and clarified, in line with international practice. *WBG Country Partnership Framework Uruguay 2022*. The framework includes competition policy projects relevant to fostering productivity and shared prosperity in the country.
8.	Financial Sector Outlook in Uruguay Financial and Private Sector Advisory to Support Growth (P175555) on overall financial sector diagnostics. Ongoing Uruguay Financial Sector Assessment Program Update (P178097) includes technical notes on capital markets and access to finance.
9.	Florit and others[62] found important gender gaps within the registered owners of family farms applying for subsidies, as 87 percent of male owners were also the main decision-makers, compared to only 34 percent of female owners. Bernheim[63] surveyed women working in dairy farms, horticulture and cattle raising and found that 44 percent

[62] Florit et al. (2013). Estudios de financiamiento rural y asistencia técnica con perspectiva de género. Montevideo: REAF-AECID.
[63] Bernheim,(2018). Estrategias de adaptación al cambio climático y género. *Estudio para el Plan Nacional de Adaptación a la variabilidad y cambio climático para el sector agropecuario*. Anuario OPYPA, Ministerio de Ganadería, Agricultura y Pesca. https://descargas.mgap.gub.uy/OPYPA/Anuarios/Anuario%202018/ANUARIO%20OPYPA%202018%20WEB%20con%20v%C3%ADncu-lo.pdf.

	participate "little or nothing" in decision-making, and that 28 percent wished they could participate more. Female rural workers routinely contribute to social security under the "helping spouse" modality (*cónyuge colaborador*)[64]. The evidence across regions and countries shows that credit constraints on households negatively impact agricultural productivity, household income and vulnerability. In middle-income countries, microcredit interventions tend to be too small to impact income diversification and non-financial asset accumulation.

4.3. LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY

75. The proposed operation is fully aligned with the Country Partnership Framework FY23-FY27, and the WB GRID and GCRF frameworks. This operation supports CPF's HLO 1 of Increased Low Carbon Growth and Resilience to Climate Change, under which its objective 1 focuses on "Greening of the Economy", supported through Pillar 1 of this DPL with several actions including the updated of Uruguay's climate commitments as a basis and roadmap for green growth, while the native forests and MPA actions protect the terrestrial and marine natural resources to retain blue and green carbon, soil nutrients, and avoid runoff to protect drinking water supplies, surface, and groundwater quality. HLO 2 on "More and Better Job Opportunities" which seeks the creation of inclusive markets under its objective 4 is integrated into Pillar 2 on resilience and inclusion through the actions on trade and competitiveness ensuring greater market access and diversified exports (including green certified exports). Furthermore, this operation's policy actions are aligned with the GRID approach and the four pillars of the GCRF in the following way: prior actions 4 and 6 are aligned with the GCRF's pillar 1 "Responding to Food Insecurity"; prior actions 7, 8, and 9, align with pillar 2 " Protecting People and Preserving Jobs'; prior actions 2, 3 and 5 align with pillar 3 "Strengthening Resilience", and prior action 1 with pillar 4 "Strengthening Policies, Institutions and Investments for Rebuilding Better".

76. The operation directly supports the WB's corporate goals reflected in the WBG Climate Change Action Plan 2021-2025, the World Bank Roadmap for Climate Action in Latin America and the Caribbean 2021-2025, and the Gender Strategy (FY16-23). Many of the prior actions in this DPL are directly focused on building climate resilience against increasing impacts of climate shocks such as drought and floods, protecting natural capital and preventing land degradation, and advancing in the decarbonization agenda through the development of renewable energy. The operation is also aligned with the upcoming Update to the WBG Gender Strategy (FY2024–2030). Specifically, updated Pillar 2 which will emphasize creating more and better jobs in alignment with the structural transformation and green transition; and updated Pillar 3 which will encompass natural assets in addition to economic assets. Moreover, the expansion of financial access is high on the list of the recommended policies by the WBG Gender Strategy and the Strategy Update.

77. This DPL is also aligned with the operational and analytical portfolio of the WBG that has evolved over the current years and previous CPF cycles. An operation that complements this DPL is the recently effective Uruguay Agro-Ecological and Climate Resilient Systems Project (P176232). The operation was preceded by the recently closed Sustainable Management of Natural Resources and Climate Change Project, DACC (P124181). Both these operations have successively tackled the issues of climate resilience in the agriculture and livestock production sectors. The current operation will advance the concept of agro-ecology which is complemented by the legislation on organic agriculture supported by this operation. This DPL is also complementary to International Finance

[64] Santos (2016). Cónyuge colaborador, breve análisis de situación. Actualización, en: Asesoría General en Seguridad Social, Comentarios de Seguridad Social N.º 52 2.° Trimestre 2016, pp. 41-49. https://docplayer.es/163729026-Conyuge-colaborador-breve-analisis-de-situacion-soc-silvia-santos.html

Corporation's (IFC) investment on energy transition in Uruguay, with its support to green hydrogen offshore developments from the National Administration of Fuel, Alcohol, and Cement (*Administración Nacional de Combustibles, Alcohol y Portland*, ANCAP).

78. Analytical work the Bank has sponsored recently has informed the current operation. This work includes an assessment on the impact of climate policies in Uruguay, developed with MEF, a study on the macro-fiscal impacts of climate shocks that provided input for the finalization of the second NDC's. The forestry sector analyses supported by the Bank through the Forest Carbon Partnership Facility program (FCPF-REDD+) are linked to the policy actions on tax reform to protect native forests. The work on Competition has been informed by the Uruguay Systematic Country Diagnostic Update 2022, and by an ongoing technical assistance to upgrade the institutional framework of the CPDC on promoting competition, dismantling cartels, and controlling mergers and acquisitions with implications on market competition.

4.4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

79. Consultations: The government has undertaken consultations on the key actions under this operation. A key piece of legislation under which several measures fall is the RCBEP Law (Law N° 20.075), an Annual Budget Review law that currently includes the native forests, financial markets, and chronic disease measures, as well as part of the competition prior action. The RCBEP is a high-profile annual law, extensively debated in the National Congress prior to its passage. The NDC second update had an exhaustive and extensive consultation process with the participation of the relevant stakeholders from different sectors such as livestock and energy[65]. Particularly relevant was the engagement with the youth. The government, along with UNICEF, organized a series of workshops to consult a representation of 40 young people under 22 years old across different sectors. The planning process for the expansion of MPA was initiated in December 2021 at the 51st Session of the National Advisory Commission of the National System of Protected Areas. The planning process provides information on the conservation values of the proposed MPA and protection measures, and ensures the participation of the productive fisheries sector, civil society, academia, and government authorities with competence in marine matters. Prior action 9 on promoting long-term credit markets in domestic currency is part of an efforts led by the BCU and MEF to pursue the de-dollarization of the economy, which includes analytical studies[66] and continued consultations with the private sector and outreach activities to help coordinate the use of the Uruguayan peso as a unit of account. The definition of technical terms to from the CPDC was the result of a formal public consultation process that included potential stakeholders subject to regulations from the competition authority. Measures to facilitate trade were agreed with Mercosur partners (reduction in the CET) and a long-standing requirement by food importers (reduction in the custom tariff for foodstuff).

80. Collaboration with other development partners: The IFC's investment portfolio aligns very closely to the measures supported by this operation, especially the NDC among other policies, with a strong focus on decarbonization through renewable energy and electromobility and on sustainable agricultural sector investments in the dairy sector. It is also considering trade and logistics investments that could be complementary to the trade and competitiveness policies supported by this operation.

[65] See https://plataformaparticipacionciudadana.gub.uy/processes/segunda-cdn
[66] Alvarez and Licandro (2022). *Incentivos microeconómicos a la dolarización*. Mimeo, Banco Central del Uruguay.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

81. The policy measures supported by this DPL are expected to play a role in strengthening Uruguay's institutions and environmental management to promote greening of the economy and stronger and more resilient growth. As such, the overall reform package supported is expected to contribute to enhancing the possibilities of sustainable growth and improved capacities of the government to respond to future shocks, that, in general, affect disproportionally the most vulnerable groups of the society.

82. By promoting the greening of the economy, the policy program under Pillar 1 is expected to generate public goods including investments in climate adaptation and the prevention of human and animal diseases. Specifically, the following impacts are expected for each of the measures:

- Prior action #1 is not expected to directly impact poverty and inequality in the short and medium terms. In a broad perspective, strengthening the scope of framework legislation for climate change is expected to encompass vulnerability and distributional impact assessments which would help address potential regressive effects of decarbonization policies and increase climate adaptation.
- Prior action #2 is not expected to have an impact on poverty or inequality in the short or medium term. However, In the long run, fiscal policies that help reduce deforestation are expected to have positive effects on climate change mitigation and adaptation, water and food security, and the reduction of poverty.
- Prior action #3 is not expected to have a negative distributional impact, as the priority areas identified for potential MPA predominantly lie beyond the twelve-mile coastal zone likely to affect artisanal and small-scale fishers. The Uruguayan commercial fisheries sector is an important socio-economic resource for the country, generating a total gross production value of US$172 million[67] in 2016; however, employment in the fishing industry has decreased significantly over the past ten years (from around 3,000 in 2011 to roughly 1,600 in 2022). The creation of MPA can play a crucial role in sustaining fish stocks, thereby helping to maintain employment in the sector (on average, 27 jobs were created for every ton of fish landed in 2021).[68]
- Prior action #4 has the potential to impact positively poverty reduction and shared prosperity by increasing market efficiency. To the extent that certification of organic products reduces information asymmetry along the marketing channel from producer to consumer, it makes the market more efficient and entails welfare gains.
- Prior action #5 measures to promote innovation in green hydrogen production are not expected to have short term effects on poverty and equity. The scale and scope of the pilot activities (US$10 million per project) are unlikely to have broad social effects or distributional impacts.

Policies supported under Pillar 2 are aimed at developing stronger and more resilient growth.

[67] Supply and Utilization Tables published by BCU in 2016: the total gross production value of the fisheries sector (catch plus processing) amounted to about US$172 million.
[68] Current situation, prospects and opportunities for the development of the National Fishing Industry, report March 2023.

- Prior action #6 is expected to have positive effects on poverty reduction and distributive outcomes mainly through productivity gains and lower prices. But also, potentially small but negative short-term adverse effects to the bottom 40 through employment fall in the sectors facing elimination of import tariffs.
- Prior action #7 is expected to have a positive impact on poverty and shared prosperity, in the medium term. Measures that support the strengthening of competition in domestic markets are expected to contribute to poverty reduction and welfare increases for the poorest four deciles of the income distribution, primarily through its effect on consumer savings due to lower prices.
- Prior action #8 is not expected to have a direct impact on poverty in the short term.
- Prior action #9 is expected to have positive social impact and effects on poverty reduction in the medium term. The policy is expected to reduce existing gender gaps and positively impact poverty and vulnerability reduction through increased access to credit improving household income for rural family producers, increased productivity, diversification of economic activities, and employment creation.

5.2. ENVIRONMENTAL, FORESTS, AND OTHER NATURAL RESOURCE ASPECTS

83. The Prior Actions (PAs) supported through the Uruguay Green and Resilient Growth Development Policy Loan are likely, in aggregate, to have a positive impact on Uruguay's environment, forests, or other natural resources. Actions under all policy areas supported by the operation are either positive or neutral in their potential environmental effects and no significant impacts are expected from the policy actions. Furthermore, the national legal framework incorporates the necessary mitigation measures for adequate management of any potential effects, as reflected in Annex 5.

84. Pillar 1: Greening of the Economy. This pillar deals largely with promoting conservation and investment in a lower-carbon energy matrix. The Prior Actions under this pillar are expected to lead to positive environmental impacts when considering Uruguay's environmental management system, strong oversight and enforcement capacity, and robust environmental regulatory framework, which are adequate to mitigate any potential adverse impacts that could result from eventual extension of agroecological production (PA 4), and the green hydrogen projects (PA 5). Prior Action 1 deals with raising Uruguay's ambition to foster conservation and reduce GHG emissions through the submission of an updated NDC to the UNFCCC. Activities under this pillar will establish economic incentives for native forest registration (PA 2), and increased protection of marine areas (PA 3), contributing to positive outcomes for Uruguay's environment while also supporting the provision of global public goods. In addition, activities under this pillar aim to promote innovation by creating a fund named "*Fondo Hidrógeno Verde*" to promote research in clean energy, aiming to reduce GHG emissions (PA 5). While inadequate management of projects supported under the fund "*Fondo Hidrógeno Verde*" may have the potential to generate adverse environmental impacts, Uruguay's robust environmental regulatory framework includes measures to manage and prevent such negative risks, in particular through the enforcement of the: (i) the Environmental Impact Assessment regulations (Ley No. 16,466); (ii) Art 17 of the Environmental Protection Law (Ley No. 17,283), which prohibits releasing or emitting into the atmosphere, directly or indirectly, materials or energy above specified limits; and (iii) the Air Quality Regulation (No. A 29, dated May 4, 2021), which establishes limits. In addition, project selection for the green hydrogen fund was conducted in coordination with the environmental authority. To further enhance environmental management of this emerging sector, the government is developing a "Guide on Environmental Impact Studies for Hydrogen and Derivatives Projects" and building capacity through training programs with both German and Japanese cooperation, coordinating with the National Council of

Innovation, Science and Technology (*Consejo Nacional de Innovación, Ciencia y Tecnología,* CONICYT) to identify potential capacity gaps.

85. Pillar 2: Stronger and more Resilient Growth. Overall, the prior actions supported by this pillar are not expected to have significant negative effects on the environment, forests, and other natural resources. The pillar will support policies aimed at: (i) promoting trade and competition (PA 6 and 7); (ii) promoting capital markets development, (PA 8); and (iii) expand financial opportunities for rural women (PA 9). There could be indirect negative environmental impacts from emissions generated from the transportation and disposal of new imported trade products (PA 6). The Borrower has strong environmental legislation and institutional capacity to supervise and mitigate potential negative impacts. The MA is the national regulatory entity in charge of formulating, implementing, and orienting environmental, conservation and use of natural resources projects and with a robust environmental impact system to mitigate potential harm, and provide oversight and regular monitoring of environmental indicators, especially pollution. The MA was created in 2020, and centralizes sustainable development and climate change, as well as old competencies given to the National Directorate of the Environment (*Dirección Nacional de Medio Ambiente,* DINAMA) and to the National Water Directorate (*Dirección Nacional de Agua*, DINAGUA). The environmental impact assessment and licensing has been a requirement since 1994 (Ley No. 16,466) and Uruguay is considered among the top ranked countries globally based on environmental performance[69], and on environmental regulation and enforcement.[70]

5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS

86. Public finance management (PFM). PFM systems in Uruguay are well designed and are supported by an adequate legal framework. The most recent comprehensive assessment of country's PFM systems, the Public Expenditure and Financial Accountability review report, dates to 2012[71] and is thus outdated. As a result, additional analysis has been done through the review of various reports and diagnostics[72], and this later analysis indicates that the conclusions of the Public Expenditure and Financial Accountability review report are still largely relevant. The major strengths of the PFM systems include the transparency of public finances and predictability and control in budget execution, which are reasonably aligned with international standards and practices. However, there are still some major challenges which negatively affect the functioning of the system, particularly in the areas of accounting and recording of the financial transactions of the central government.

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[69] Ranked #6 according to the 2018 Environmental Performance Index. See: Wendling, Z. A., Emerson, J. W., Esty, D. C., Levy, M. A., de Sherbinin, A., et al. (2018). 2018 Environmental Performance Index. New Haven, CT: Yale Center for Environmental Law & Policy. https://epi.yale.edu/

[70] Ranking 0.5 above the average on regulation and enfocerment.2020 Environmental Governance Indicators for Latin America and the Caribbean. The Inter-American Development Bank and the World Justice Project https://publications.iadb.org/publications/english/document/Environmental-Governance-Indicators-for-Latin-America--the-Caribbean.pdf

[71] Uruguay Public Expenditure and Financial Accountability Review Report published on December 18, 2012 (Report No. ACS4022).

[72] The following reports and documentation were considered: Uruguay 2021 Country Policy and Institutional Assessment (CPIA); Uruguay Budget's Law (*https://www.impo.com.uy/bases/leyes/19924-2020*) and *Rendición de Cuentas y Balance de Ejecución Presupuestal* (*https://www.gub.uy/ministerio-economia-finanzas/comunicacion/publicaciones?field_tipo_de_publicacion_target_id=1345&year=all&month=all&field_tematica_target_id=All&field_publico_target_id=All*); Uruguay's Open Budget Portal (*https://transparenciapresupuestaria.opp.gub.uy/*); IDB report on the status of IPSAS adoption in https://www.focal.red/system/files/2018-01/Uruguay.pdf); and Uruguay (and Supreme Audit Institutions Independence Index: 2021 Global Synthesis Report (*https://openknowledge.worldbank.org/handle/10986/36001*).

87. Legal framework. The legal framework for PFM is anchored in Uruguay's constitution[73] and the Consolidated text on Accounting and Financial Administration[74] (*Texto Ordenado de Contabilidad y Administración Financiera*, TOCAF). The TOCAF compiles the statutory rules on financial management and has undergone modifications according to the various laws that have been passed over the years, particularly the laws on the different five-year budgets and presentation of the yearly accounts, which has resulted in a highly flexible and complex financial management regulatory framework.

88. Budget credibility. In terms of budget reliability and transparency, as provided in its constitution, Uruguay has a five-year budget that coincides with the government term and operates in practice as a medium-term fiscal framework that can be modified through several legal procedures. The main tool for modifying budgeted allocations is the RCBEP made publicly available[75] and submitted to congress for approval. Budget Law No. 19.924 for the period 2020-2024 passed by parliament in December 2020 is also publicly available.[76] Policies and priorities are broadly reflected in the budget since the government uses a program-based budgeting. [77] The Presidency's Office of Planning and Budgeting (*Oficina de Planeamiento y Presupuesto,* OPP) plays a leading role in the budget formulation process and in the monitoring and evaluation of public policies and programs to ensure public resources are allocated to government priorities and objectives. Budget execution reports are periodically publicly available at the government website open budget portal. Uruguay's classification system is consistent with the United Nations Classification of the Functions of Government 10 main government functions. It allows for tracking of spending by administrative, economic, and program classification. The classification is used for budget formulation, execution, and reporting. The budget system therefore provides an adequate framework for the allocation of the country's resources to its priorities, and the budget itself constitutes an effective tool to discipline public expenditure.

89. Accounting and financial reporting. The National General Accounting Office (C*ontaduría General de la Nación,* CGN) is responsible for managing the Integrated Financial Information System (S*istema Integrado de Información Financiera,* SIIF) and the operational aspects of the budget management and execution. CGN prepares the RCBEPs that are submitted annually to the legislative assembly by June 30 of the following year.[78] Although the CGN prepares the RCBEPs, the quality of information included therein is compromised by the absence of an operational and functioning accounting module within the Financial Management Information System and by the single-entry registry. The RCBEP thus do not include financial information that would be prepared in line with international accounting standards and that would constitute the government's annual and consolidated financial statements.[79] This constitutes a key deficiency in the availability of high-quality financial information for decision making and for holding officials to account for the management of public resources. The accounting standards used in Uruguay[80] are not in line with the International Public Sector Accounting Standards (IPSAS)[81], with the risk that government financial transactions may not be captured in an effective way. Despite these weaknesses, Uruguay's budget documentation is quite extensive and RCBEPs are quite comprehensive and include information on all

73 Constitution of the Republic (CR) adopted in 1967 and subsequent amendments made by plebiscite in 1989, 1994, 1996 and 2004.
74 TOCAF was approved by Decree N° 150/012, as amended from time to time, and is publicly available at: *https://www.impo.com.uy/bases/tocaf2012/150-2012*
75 *https://www.gub.uy/ministerio-economia-finanzas/tematica/rendicion-cuentas-balance-ejecucion-presupuestal*
76 *https://www.impo.com.uy/bases/leyes-originales/19924-2020*
77 The 2020-2024 budget has 22 programmatic areas linked to budgetary programs with results indicators and budgetary allocations.
78 The 2021 RCBEP was received by Parliament on June 30, 2022 and submitted to the TdC on July 5, 2022.
79 Financial Statements comprising: (a) a statement of financial position; (b) a statement of financial performance; (c) a statement of changes in net assets/equity; and (d) a cash flow statement are not prepared by the central government.
80 Accounting practices used by the central government recognized expenses when incurred and revenues on a cash basis.
81 IDB report on the status of IPSAS adoption in https://www.focal.red/system/files/2018-01/Uruguay.pdf)

central government budget transactions, revenues, expenditures and financial assets and liabilities. It is worth mentioning that the government is working on the revamping of the Financial Management Information System. Once the financial information system is fully operational, it is expected to allow government financial accounting and preparation of government financial statements consistent with the International Public Sector Accounting Standards (IPSAS).

90. External oversight. The execution of the budget is externally overseen by the Uruguay Court of Accounts (T*ribunal de Cuentas*, TdC) that functions as the country's supreme audit institution. It has functional autonomy and financial independence granted by the Constitution. It conducts the annual audit of the RCBEP[82] and issues an opinion based on international audit standards. [83] The legislative assembly undertakes a follow-up of audit recommendations is publicly available. [84]

91. Foreign exchange control environment. The last IMF safeguards assessment was conducted in 2005 and is therefore outdated. To assess the strength of the foreign exchange control environment, the Bank reviewed the IMF's report on the 2022 review of the central bank transparency code review.[85] In that report, the IMF expressed satisfaction with the effectiveness of the quality of information and the transparency practices for foreign exchange reserve management, particularly given the adequate disclosures related to the governance framework for managing international reserves. In addition, the Bank reviewed the BCU's financial statements for the last three years and confirmed that they are prepared in accordance with relevant accounting standards and banking principles.[86] The financial statements were audited by an internationally recognized audit firm and, for 2019 and 2020, by the TdC. The resulting audit reports are publicly available[87] and include an unqualified audit opinion on the financial statements for all three years. Based on the assessment, the control environment of the BCU is acceptable and there are arrangements in place to ensure that the loan proceeds will reach the country's official foreign exchange reserves, before being credited to an account of the government to finance budgeted expenditures.

92. Procurement in Uruguay is regulated by TOCAF which is the main legal text in this area. TOCAF addresses the procurement of goods, works and services applying equally the same rules and procedures for any of these types of expenditures, even for consultancy services. Equally important to note is the fact that there are many complementary legal texts regulating different aspects of procurement (laws, decrees, regulations, and international agreements).

93. Savings could be achieved through better public procurement policies and strategies. In 2019, the Bank carried out a public expenditure review (PER), and the result of the analysis of procurement data in a five-year period (2014-2018), facilitated the quantification of potential savings that could be achieved through improvements in procurement processes, such as better public procurement policies and strategies. The support from the Bank provided capacity building to enhance technical knowledge in implementing the strategic sourcing methodology. As a result, Uruguay started working in different initiatives using procurement data to identify areas

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[82] The TdC issued an unqualified opinion on the RCBEP for fiscal year 2021 jointly with a disclaimer (absence of opinion) on government cash flow statements on July 27, 2022 (seven months after the end of the reporting period).
[83] These standards are issued by the International Organization of Supreme Audit Institutions (INTOSAI).
[84] Parliament's follow-up of TdC's recommendations: https://parlamento.gub.uy/camarasycomisiones/asambleageneral/observaciones-tc
[85] Uruguay: Central Bank Transparency Code Review: https://www.elibrary.imf.org/view/journals/002/2022/234/article-A001-en.xml?ArticleTabs=fulltext
[86] Uruguay's national accounting standards and following recommendations of the Association of Central Banks of Latin America and the Caribbean (CEMLA, for its acronym in Spanish)
[87] BCU's audited financial statements: https://www.bcu.gub.uy/Acerca-de-BCU/Paginas/Estados-Contables-del-BCU.aspx

for improvement, savings, best practices, expenditures to be applied through framework agreements, among other aspects. These initiatives are being led by the development of a strategy prepared by the Public Procurement Regulatory Agency (*Agencia Reguladora de Compras Estatales,* ARCE) for the use of procurement data to improve public expenditure efficiency and promote transparency. This strategy will aim to provide a structured framework to measure the results of the different approaches in procurement, as well as to identify areas for improvement, supplier´s performance, among others. Reports derived from the strategy will also allow for the monitoring of public expenditure efficiency and will particularly allow better informed decision making.

94. Additionally, prior to the design of the strategy, and as part of its LUC, the borrower has introduced new regulations to improve public procurement processes, including the creation of a single regulatory agency for public procurement, ARCE, attached to the Presidency. These reforms aimed to: (i) centralize the design of policies and system on public procurement and supervise their implementation; and (ii) unify, harmonize, and modernize procurement processes and regulations, in line with good international practices. The implementation of the agency's mandate should result in enabling potential fiscal savings as identified by the bank's study, by higher efficiency and transparency in procurement processes. Recently, Uruguay has also modified the institutional design of this central agency to include a central procurement unit in the ARCE, as the implementing agency for centralized procurement. This change was carried out with the aim to support efficiency in the procurement of specific goods strategically identified.

95. Fiduciary risk. There are no risks to the achievement of the development objectives stemming from any identified weaknesses in the PFM system. As a result, no additional fiduciary arrangements will be put in place for the operation. The overall integrated fiduciary risk of this operation is rated as Moderate.

96. Disbursement arrangements. To determine whether to make the disbursement under this DPL, the Bank will assess the adequacy of the government's compliance with the policy program, its observance of the legal instruments supported by the operation, and the adequacy of the borrower's macroeconomic policy framework at the time of disbursement. Disbursement will not be linked to any specific purchases. The Bank will disburse the loan proceeds to a new US$-denominated account belonging to MEF. This account forms part of the country's official foreign reserves, held at the BCU. Upon receipt of the loan proceeds in the US$-denominated account, the borrower will promptly account for the receipt of the proceeds in the country's SIIF in an account used to finance budgeted expenditures using the country's regular or established procedures for such accounting. Recording and accounting for the receipt of the funds will be done in Uruguayan Pesos (*pesos uruguayos)*, and the exchange rate to be used is the rate that will be in effect on the date MEF receives the funds. If the loan proceeds or any part thereof are used for excluded expenditures as defined in the loan agreement, the WB will require the borrower to refund an equivalent amount.

97. Written confirmation. Within 30 days after receipt of the loan proceeds, the borrower, through MEF, will confirm in writing to the bank: (i) the exact amount of loan proceeds received into the BCU account; and (ii) that an equivalent amount has been recorded in Uruguay's accounting and budgeting management system/records.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

98. The MEF will be responsible for the overall monitoring, evaluation, and results framework. MEF will also coordinate with the relevant ministries and agencies of this operation monitoring and evaluation. The agencies responsible for the implementation of the prior actions listed in this operation include, for pillar 1: (i) MA, (ii) MIEM, and MGAP. Pillar 2 agencies include: (i) BCU, (ii) MIEM, (iii) Ministry of Social Development (*Ministerio de*

Desarrollo Social, MIDES) and (iv) CPDC. The capacity for monitoring, evaluation, and accountability is considered good given the strong governance ranking of the public sector institutions in Uruguay. Furthermore, the monitoring, reporting and verification of the KPI builds on a partnership with the United Nations Development Program (UNDP). This is in line with one of the main conclusions drawn from the 2023 Annual Meetings, which emphasizes the importance of exploring collaborative approaches to revitalizing and enhancing partnerships with other multilateral development organizations while building on the approach of the existing private-sector SLB to provide independent external verification of achievement of targets. The WB will also regularly monitor the implementation of the program through supervision missions and work with MEF to follow the program. The results framework is presented in Annex 1.

99. ***Grievance Redress.*** Communities and individuals who believe that they are adversely affected by specific country policies supported as Prior Actions or tranche release conditions under a World Bank Development Policy Financing may submit complaints to the responsible country authorities, appropriate local/national grievance mechanisms, or the Bank's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Project affected communities and individuals may submit their complaint to the Bank's independent Accountability Mechanism (AM). The AM houses the Inspection Panel, which determines whether harm occurred, or could occur, as a result of Bank non-compliance with its policies and procedures, and the Dispute Resolution Service, which provides communities and borrowers with the opportunity to address complaints through dispute resolution. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate GRS, please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the Bank's Accountability Mechanism, please visit https://accountability.worldbank.org.

6. SUMMARY OF RISKS AND MITIGATION

100. The overall risk to achieving the Program Development Objective of this operation is assessed as Moderate. All risk categories have been assessed as Moderate, except for Environment and Social, which has been rated as Low. With the most pressing uncertainties from the COVID pandemic having dissipated, a fiscal consolidation process underway, and sizeable public and external buffers, the Macroeconomic risk for this operation is assessed as Moderate, notwithstanding the downside risks explained above, as the implementation of the supported measures and achievement of the results indicators is unlikely to be affected by macroeconomic developments in the near future. Risks related to Sector Strategies and Policies have also been assessed as Moderate, with the current administration over three years into its tenure and a reform program that was endorsed by a referendum.

101. The risk categories for Political and Governance, Technical Design of the Program, Institutional Capacity for Implementation and Sustainability and Stakeholders are rated as Moderate. In terms of political and governance, Uruguay has a strong social compact with a core of a stable system of political parties, a tradition of democratic debate of ideas and a continuous search for consensus. Regarding technical design and institutional capacity, Uruguay has a track record in implementation success and DPL programs. As regards to stakeholders, the strong social compact described above was successfully put to test during the COVID outbreak, where the government did not impose mandatory lockdowns, but civic responsibility was the norm, and mitigation measures were implemented and accepted without social unrest. Also, civil society did not push for disruptive measures such as unsustainable deficit spending or the use of private pension savings funds, for example.

Table 6: Summary Risk Ratings

Risk Categories	Rating
1. Political and Governance	Moderate
2. Macroeconomic	Moderate
3. Sector Strategies and Policies	Moderate
4. Technical Design of Project or Program	Moderate
5. Institutional Capacity for Implementation and Sustainability	Moderate
6. Fiduciary	Moderate
7. Environment and Social	Low
8. Stakeholders	Moderate
9. Other	
Overall	Moderate

ANNEX 1: POLICY AND RESULTS MATRIX

DETAILED RESULTS FRAMEWORK

Prior Actions	**Results**		
	Indicator Name	Baseline	Target
Pillar 1: Greening of the Economy			
Prior Action #1: To formalize Uruguay's climate commitments under the Paris Agreement, the Borrower has approved the second Nationally Determined Contributions (NDC) under the Paris Agreement framework, as evidenced by the UNCCS letter dated January 30, 2023, acknowledging submission of Uruguay's second NDC Submission.	Results Indicator #1: Second NDC approved by presidential decree	No (2022)	Yes (2024)
Prior Action #2: To enhance carbon sequestration, promote climate resilience, and protect biodiversity through the conservation of native forests, the Borrower has excluded native forests from the total property area that is used to calculate exceptions to various taxes, as evidenced by Articles 477, 478, and 491 of Law No. 20.075, dated October 20, 2022 and published in the Official Gazette on November 3, 2022.	Results Indicator #2: Area of native forest potentially covered by the new incentives.[88]	0 (2022)	130,211 hectares (2024)
Prior Action #3: To conserve marine ecosystems and preserve blue carbon sinks, the Borrower, through Ministry of Environment (MA), has identified new Marine Protected Areas covering at least 10% of Uruguay's Exclusive Economic Zones ("EEZs"), established a strategy for the protection of 30 percent of Uruguay's EEZs by 2030, and identified new areas considered "relevant for conservation" covering an estimated 30 percent of Uruguay's EEZ, as evidenced by Ministerial Resolution No. 1152/022, dated December 12, 2022.	Results Indicator #3: Number of new Marine Protected Areas created.	0 (2022)	1 (2024)
Prior Action #4: To advance environmental and social sustainability and climate goals and expand trade opportunities for low-carbon organic agricultural products, the Borrower, through Ministry of Livestock, Agriculture and Fisheries (MGAP), has systematized the certification of organic and integrated agricultural and aquaculture production, as evidenced by Decree No. 175/022, dated May 24, 2022 and published in the Official Gazette on May 31, 2022.	Results Indicator #4: Number of certifiers of organic agricultural production registered under the national system.	0 (2022)	3 (2024)
Prior Action #5: To foster the production and use of green hydrogen as a clean fuel to decarbonize freight heavy industry and agriculture, the Borrower, through Ministry of Industry, Energy and Mining (MIEM), has created the program "Fondo Hidrógeno Verde" to promote innovation and research in Green Hydrogen and its derivatives, as evidenced by the agreement between the MIEM, Uruguay Technological Laboratory (LATU), and National Agency of Research and Innovation (ANII), dated March 30, 2022.	Results Indicator #5: Issuance of regulations specific to green hydrogen production and derivatives	No (2022)	Yes (2024)
Pillar 2: Stronger and more Resilient Growth			

[88] Based on estimates from the Forestry Division of MGAP.

Prior Action #6: To promote food and essential goods price resilience against climate and global shocks and foster a competitive tradable sector, the Borrower, through MEF, has: (i) reduced its common external tariff on average by 10 percent in agreement with its Mercosur partners, as evidenced by Decree No. 369/022, dated November 11, 2022, and published in the Official Gazette on November 24, 2022, that adopted Mercosur's Common Market Council Decision No. 8/22; and (ii) reduced the import charges for assessing regulatory conformity for imported food items from 1.5 percent to 0.5 percent, as evidenced by Decree No. 194/022, dated June 14, 2022, and published in the Official Gazette on June 20, 2022.	Results Indicator #6: The share of imports, by value, subject to reduced import tariffs and certificate fees and risk-management controls.	0% (2021)	58% (2024)
Prior Action #7: To strengthen its competition policy framework, increase market contestability and foster legal certainty, the Borrower, through MEF, has: (i) created and operationalized a network of regulators with competition enforcement powers, to reinforce interinstitutional cooperation and promote information sharing as evidenced by a Framework Collaboration Agreement signed on November 22, 2022; and (ii) strengthened merger control rules by enabling more thorough analysis in problematic cases and approving technical norms clarifying key elements of the regulatory framework, as evidenced by Article 147 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022, and Resolution No. 175/022 dated August 23, 2022.	Results Indicator #7: Number of antitrust decisions and advocacy opinions issued	14 (average 2021-2022)	17 (average 2023-2024)
Prior Action #8: To promote investment and credit in domestic currency and longer-term financial instruments, the Borrower has issued measures to: (i) homogenize rates for returns in indexed and nominal Uruguayan Pesos; (ii) reduce tax rates for returns in local currency and longer-term investments; and (iii) homogenize tax rates and terms for returns on investments in bank deposits and market instruments, as evidenced by Articles 485 and 487 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022.	Results Indicator #8: Share of bank deposits (both nominal and indexed peso) over total deposits (in any currency).[89]	25.5% (Average 2022)	27.5% (Average 2024)
Prior action #9: To provide risk mitigation and expand financing for rural and agricultural family businesses led by women, the Borrower, through National Development Agency (ANDE) and National Financial Corporation Administrator of Investment Funds SA (CONAFIN AFISA), has operationalized the Guarantee Fund for the Implementation of Rural Development Policies (FOGADER), by executing two agreements with financial entities, as evidenced by the agreement executed between CONAFIN AFISA and Uruguayan Foundation for Solidarity Cooperation and Development (FUNDASOL), dated March 10, 2022, and the agreement executed between CONAFIN AFISA and República Microfinanzas S.A, dated March 8, 2022.	Results Indicator #9: Cumulative credits granted to rural women[90]	138 (2022)	300 (2024)

[89] Baseline and target are expressed in December 2022 prices using the Uruguayan Consumer Price Index for series in Uruguayan Pesos, and the US Consumer Price Index for series in US Dollars. Series in real US Dollars are then expressed in Uruguayan Pesos using the average exchange rate for December 2022 (40.07 Uruguayan Pesos per US Dollar) to avoid fluctuations due to exchange rate swings.
[90] FOGADER guarantees plus women that operate through the "*Programa Microcrédito Rural*". Target is the sum of years 2022, 2023, and 2024.

RESULTS INDICATORS BY PILLAR

Baseline	Closing Period
Greening of the Economy	
Second NDC approved by Decree (Yes/No)	
Oct/2022	Oct/2024
No	Yes
Area of native forest potentially covered by new fiscal incentives (Hectare(Ha))	
Oct/2022	Oct/2024
0	130211
Number of new Marine Protected Areas created (Number)	
Oct/2022	Oct/2024
0	1
Number of certifiers of organic agricultural production registered under the national system (Number)	
Oct/2022	Oct/2024
0	3
Issuance of regulations specific to green hydrogen production and derivatives (Yes/No)	
Jul/2022	Jul/2024
NO	YES
Stronger and More Resilient Growth	
The share of imports, by value, subject to reduced import tariffs and certificate fees and risk-management controls (Percentage)	
Oct/2021	Oct/2024
0	58
Number of antitrust decisions and advocacy opinions issued (Number)	
Oct/2022	Oct/2024
14	17
Share of bank deposits (both nominal and indexed peso) over total deposits (in any currency). (Percentage)	
Dec/2022	Dec/2024
25.5	27.5
Cumulative credits granted to rural women (Number)	
Oct/2022	Oct/2024
138	300

ANNEX 2: FUND RELATIONS ANNEX

PRESS RELEASE

PR23/157

IMF Executive Board Concludes 2023 Article IV Consultation with Uruguay

FOR IMMEDIATE RELEASE

Washington, DC – May 17, 2023: The Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Uruguay on May 15, 2023.

After reaching pre-pandemic levels in mid-2021, real GDP grew by 4.9 percent in 2022 mainly driven by strong commodity exports and the service sector, including tourism. However, the economy decelerated in the second half of the year due to adverse external conditions and the effects of the most severe drought in forty years. Inflation remained above the target range in 2022 but, after peaking in September 2022 at 9.95 percent, it started to decline towards the end of the year, reaching 7.3 percent in March 2023.

In response to increased inflationary pressures, the Banco Central del Uruguay (BCU) appropriately tightened monetary policy during 2022. The BCU markedly raised the policy rate from 5.75 percent in December 2021 to 11.5 percent in December 2022. The BCU implemented an interest rate cut of 25 basis points in its April 2023 meeting, citing declining inflationary pressures. The fiscal deficit and government debt declined substantially over the last two years, reflecting the authorities' efforts to stay within the targets of the fiscal rule, while protecting the most vulnerable. After peaking at 68.1 percent of GDP in 2020, gross non-financial public sector (NFPS) debt reached 59.3 percent of GDP at the end of 2022, below its pre-pandemic level amid historically low sovereign spreads. The health of the financial sector remains sound, and banks have weathered the pandemic well.

The economy is expected to decelerate in 2023, with real GDP growth projected at 2 percent. Despite external headwinds, tighter financial conditions, and the impact of the drought, growth would be supported by a strong tourism season, increased cellulose production and exports, and robust private consumption as real wages recover. The growth outlook after 2023 is positive, but subject to external and domestic risks. Main macroeconomic risks are derived from a worsening of external financial conditions, deterioration of international geopolitical tensions, and the impact of the drought. Inflation is expected to decline to 7 percent in 2023 and fall within the target range in 2024. The authorities' strong track record of implementing sound macroeconomic policies in a challenging environment has improved the country's resilience to shocks. Overall fiscal risks are low.

Executive Board Assessment[2]

Executive Directors commended Uruguay's robust institutions and sound policies, which have supported the economy's resilience to shocks. Directors noted that the outlook, while positive,

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

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is subject to downside risks, including related to the current drought. They emphasized the need to consolidate progress made in upgrading the fiscal, monetary, and financial frameworks and continue with ambitious structural reforms to maintain Uruguay's strong resilience and support sustainable and inclusive growth.

Directors commended the authorities for meeting the fiscal rule targets for three consecutive years despite a challenging economic environment and concurred that the fiscal framework has strengthened policy credibility. They emphasized that continued strong compliance with the current fiscal rule is the priority in the current juncture. At the same time, many Directors considered that a more explicit debt objective could be a useful component of a medium-term fiscal strategy.

Directors agreed that a modest fiscal impulse is appropriate in 2023 and encouraged measures to put the debt on a downward path once the effect of the drought abates. They recommended measures to further rationalize tax expenditures, improve the targeting of subsidies, and reduce the wage bill, while continuing to take steps to preserve social cohesion. Directors also welcomed the recently approved pension reform, which should help to stabilize long-term pension spending.

Directors emphasized the need to maintain a tight monetary stance until price pressures and inflation expectations converge to the target band. They highlighted that this along with efforts to strengthen de jure central bank independence would help to further strengthen monetary policy credibility and support efforts to reduce dollarization. Directors agreed that the exchange rate should continue to act as a shock absorber and that FX interventions should be limited to responding to disorderly market conditions.

Directors welcomed that the financial sector remains resilient and healthy. They indicated that efforts to further enhance financial supervision are essential to bolster resilience to shocks and improve confidence in the financial system. Directors also encouraged steps to promote domestic capital market development and encouraged continued progress in implementing the recent FSAP recommendations and toward creating a comprehensive AML/CFT national plan.

Directors noted that structural reforms remain critical to improve productivity and reinvigorate growth. They welcomed the recent reforms in the education system and indicated the need for further efforts to address long-standing human capital erosion and skill gaps. Directors also supported efforts to improve the efficiency and productivity of state-owned enterprises and enhance trade integration.

Directors commended Uruguay's leadership in climate change policy and recognized the authorities' efforts to integrate climate policies into their overall policy agenda, noting the successful issuance of a Sovereign Sustainability-Linked Bond. They recognized the significant progress in reducing greenhouse gas emissions intensity and encouraged the authorities to continue their efforts to transform Uruguay into a climate-resilient, green, and sustainable economy.

3

Uruguay: Selected Economic Indicators

			Projections	
	2021	2022	2023	2024
Output, prices, and employment				
Real GDP (percent change)	5.3	4.9	2.0	3.0
GDP (US$ billions)	61.4	71.2	76.5	80.5
Unemployment (in percent, pa)	9.4	7.9	8.2	8.1
Output gap (percent of potential output)	-2.0	-0.4	-0.6	-0.2
CPI inflation (in percent, end of period))	8.0	8.3	7.0	5.7
		(Percent change, unless otherwise specified)		
Monetary and banking indicators 1/				
Base money	9.1	1.7	...	...
M2	16.2	1.7	...	...
Growth of credit to households (in real pesos)	4.4	6.4	...	...
Growth of credit to firms (in US$)	7.0	19.1	...	...
Bank assets (in percent of GDP)	74.2	67.1	...	...
Private credit (in percent of GDP) 2/	27.0	26.1	...	...
		(Percent of GDP, unless otherwise specified)		
Fiscal sector indicators 3/				
Revenue CG-BPS (A)	27.0	27.1	26.1	26.5
excluding cincuentones	26.7	27.0	26.1	26.5
Primary expenditure CG-BPS (B)	27.9	27.8	27.3	27.5
Primary balance of local governments (C)	0.1	0.1	0.1	0.1
Primary balance of BSE (D)	0.1	0.0	0.2	0.2
Primary balance NFPS (A-B+C+D)	-0.6	-0.5	-1.0	-0.7
excluding cincuentones 4/	-0.9	-0.6	-1.0	-0.7
Interest NFPS	2.0	2.0	1.9	2.0
Overall balance NFPS	-2.6	-2.5	-2.9	-2.7
excluding cincuentones 4/	-3.0	-2.7	-3.0	-2.8
Gross debt NFPS	63.4	59.3	61.6	61.9
Net debt NFPS	53.3	50.5	52.9	53.3
External indicators				
Merchandise exports, fob (US$ billions)	15.7	17.2	15.5	16.6
Merchandise imports, fob (US$ billions)	11.2	13.6	13.3	14.5
Terms of trade (percent change)	1.9	-4.7	1.0	0.7
Current account balance	-2.5	-3.2	-3.2	-3.0
Total external debt + non-resident deposits	79.4	78.0	79.1	77.4
Of which: External public debt	34.7	29.1	33.6	32.4
External debt service (in percent of exports of g&s)	57.7	53.7	61.8	52.7
Gross official reserves (US$ billions)	17.0	15.1	16.1	16.3
In months of imports of goods and services	13.7	9.7	10.4	9.8
In percent of:				
Short-term external (STE) debt	221	169	221	215
STE debt plus banks' non-resident deposits	298	265	249	243

Sources: Banco Central del Uruguay, Ministerio de Economía y Finanzas, Instituto Nacional de Estadística, and Fund staff calculations.
1/ Percent change of end-of-year data on one year ago.
2/ Includes bank and non-bank credit.
3/ Non-financial public sector (NFPS) includes the Central Government, Banco de Prevision Social, Banco de Seguros del Estado, and Non-Financial Public Enterprises.
4/ Temporary proceeds resulting from the pension reform that allowed workers above 50 years old (and with certain income level) to voluntarily move back to the public pension system. Proceeds are projected to end in 2022.

ANNEX 3: LETTER OF DEVELOPMENT POLICY

Ministerio
de Economía
y Finanzas

Montevideo, 8 de octubre de 2023

SEÑOR
AJAY BANGA, PRESIDENTE
BANCO MUNDIAL
WASHINGTON D.C., 20433, USA

Tengo el agrado de dirigirme a usted en representación del Gobierno de la República Oriental del Uruguay, con el objeto de solicitar el apoyo de vuestra institución para continuar fortaleciendo las políticas de crecimiento verde y desarrollo sostenible del país.

Estas políticas se encuentran en el centro de la agenda de reformas de desarrollo del Gobierno de Uruguay, coherente con los lineamientos estratégicos incluidos en nuestro *Compromiso por el País*. A pesar de las urgencias relacionadas con la respuesta a la pandemia del COVID-19, y apoyada por un préstamo oportuno del Banco Mundial, el Gobierno avanzó en la aprobación de la Ley de Urgente Consideración (LUC), dándole fuerza de ley al compromiso asumido.

Por otra parte, el Gobierno de Uruguay está comprometido con la buena gestión de la deuda públicay la provisión de bienes públicos globales. Ambos objetivos se reflejaron en la innovadora emisión, en octubre del 2022, de un Bono Soberano Indexado a Indicadores de Cambio Climático (SSLB, por su sigla en inglés). Este Bono vincula la tasa de interés a pagar por Uruguay con la consecución de objetivos de mitigación de los efectos del cambio climático y de conservación de la naturaleza, alineados con los compromisos en la primera Contribución Determinada a nivel Nacional (CDN) de Uruguay ante el Acuerdo de Paris.

Asimismo, existe una visión compartida de larga data en Uruguay con respecto a las prioridades a largo plazo que incluyen la estabilidad macroeconómica y el acceso fluido a los mercados financieros, el desarrollo del capital humano, la diversificación de la canasta de exportación a través delacceso a mercados nuevos y productos de alta calidad, así como la producción agropecuaria ambientalmente sostenible y la buena gestión de los recursos naturales. Sobre estas bases se construyó el nuevo Marco de Alianza País con el Banco Mundial para el periodo 2022-2026 en la cual se identifican tres áreas temáticas: i) más y mejores oportunidades de trabajo, ii) mejores resultados medioambientales y resiliencia a los *shocks,* y iii) mejor acceso a servicios públicos de calidad.

Con estos objetivos como guía de la acción del Gobierno, nos dirigimos a usted a los efectos de solicitar el apoyo del Banco a través del otorgamiento de un Préstamo de Políticas de Desarrollo por un monto de US$350 millones, para apoyar transformaciones que promuevan un crecimiento verde y resiliente en Uruguay.El gobierno está comprometido con la promoción del crecimiento económico y la integración de los principios ambientales, sociales y de gobernanza(ESG por su sigla en inglés). En este sentido, se ha venido desarrollando una operación de préstamo que respalda estos esfuerzos al apoyar medidas que mitiguen las emisiones de gases de efecto invernadero (GEI), promuevan la biodiversidad, y contribuyan a los bienes públicos globales y la reducción de riesgos climáticos. Además, se ha trabajado en medidas estructurales que mejoran la competitividad y la resiliencia de la economía frente a shocks negativos, así como fortalecer la integración del Uruguay a la economía global.Estas medidas están respaldadas por la operación propuesta, cuyos aspectos principales se presentan a continuación.

El objetivo del Préstamo de Políticas de Desarrollo es apoyar al Gobierno en: **i)promover una economía verde y ii) un crecimiento más sólido y resiliente**. El primer pilar de la operación incluye medidas para promover el desarrollo de una economía verdea través de políticas que generen bienes públicos globales. Incluidos en este pilar se encuentran la elaboración y presentación de la segunda CDN de Uruguay ante el Acuerdo de Paris, el desarrollo de la producción ganadera y agrícola orgánica que sea climáticamente inteligente y sostenible, la protección del hábitat y biodiversidad terrestre y marina, y medidas para promover la innovación y la generación de capacidades estatales en la producción de hidrógeno y otros combustibles verdes.

Como signatario del Acuerdo de París, la República Oriental del Uruguay presentó su primera CDN a la Convención Marco de las Naciones Unidas sobre el Cambio Climático (CMNUCC) en 2017, estableciendo más de 100 medidas de adaptación y mitigación al cambio climático con metas específicas y un horizonte temporal a 2025.Para formalizar la continuidad de dichos compromisos climáticos, Uruguay ha presentado la segunda CDN en el marco del Acuerdo de París, con objetivos cuantitativos planteados a 2030. Esto se demuestra en la nota enviada por el Secretario Ejecutivo de la CMNUCC al Gobierno de Uruguay en enero de 2023, agradeciendo por la presentación de la segunda CDN. La elaboración de la segunda CDN de Uruguay fue apoyada por una asistencia técnica del Banco Mundial, que ayudó al Gobierno a construir un modelo para evaluar el impacto macroeconómico de diferentes medidas de mitigación de gases de efecto invernadero. Esta segunda CDN presenta un mayor nivel de ambición ya que fortalece los objetivos anteriores para la adaptación y mitigación del cambio climático, incluyendo (i) el establecimiento de unameta más ambiciosa para la reducción de la intensidad de las emisiones de metano y óxido nitroso de la producción de carne vacuna, (ii) un compromiso del gobierno para limitar las emisiones de gases de efecto invernadero en términos absolutos (independientemente del desempeño del PBI),(iii) agregando una meta de reducción de consumo de hidrofluorocarbonos (HFC) y (iv) continuando el compromiso de deforestación cero con la meta de mantener el 100 por ciento del área de bosque nativo.

Uruguay mantiene un firme compromiso con una producción agropecuaria de bajo impacto ambiental, y la producción de carne vacuna es un ejemplo de ello. A través de una ganadería que se realiza mayormente sobre pastizales, principal ecosistema natural del país, Uruguay apuesta a la implementación y extensión de tecnologías y prácticas que permitan a los productores aumentar su rentabilidad al mismo tiempo que reducen la intensidad de emisiones de GEI de la actividad y aumentan la resiliencia al clima y biodiversidad en sus predios. El proyecto piloto denominado "Ganadería y Clima", es una prueba de que lo anterior es posible.

Asimismo, la producción agrícola orgánica se está expandiendo rápidamente en Uruguay. Este tipo de agricultura es clave para una transición hacia un crecimiento económico más sostenible, ya que beneficia al ambiente al evitar los fertilizantes y productos químicos sintéticos, consume menos energía, lo que reduce su huella de carbono y promueve prácticas que aumentan la biodiversidad agrícola y la conservación de carbono en el suelo. Para avanzar en las metas de sostenibilidad ambiental, social y climáticas y ampliar las oportunidades comerciales de productos agrícolas orgánicos bajos en carbono, el Ministerio de Ganadería, Agricultura y Pesca (MGAP), ha sistematizado la certificación de la producción agrícola y acuícola orgánica e integrada, como lo demuestra el Decreto Presidencial 175/022 del 24 de mayo de 2022. El Decreto establece el Sistema Nacional de Certificación para la Producción Orgánica y la Producción Integrada, en el cual los productores pueden participar voluntariamente.

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Las características oceanográficas de la Zona Económica Exclusiva (ZEE) marina de Uruguay lo convierten en uno de los sitios más importantes a nivel mundial para la biodiversidad marina, con al menos 90 especies de tiburones y rayas, varias endémicas, que se consideran amenazadas a nivel mundial. Con el objetivo de conservar estos ecosistemas y preservar los sumideros de carbono azul, se han identificado áreas marinas prioritarias para la conservación que cubren al menos el 10% (diez por ciento) de la ZEE de Uruguay, se estableció una estrategia para proteger el 30% (treinta por ciento) de la ZEE de Uruguay para 2030, como lo demuestra la Resolución Ministerial Nº 1152/2022, de 12 de diciembre de 2022.Esta medida es un paso crucial para que Uruguay demuestre su compromiso con respecto a la protección de sus áreas marinas y, en términos más generales, la visión a largo plazo del país para preservar su capital natural. A su vez, esto puede brindar un apoyo para la agenda de finanzas sostenibles de Uruguay, a través de la cual el país busca activamente diversificar su base de inversores impulsando las inversiones vinculadas a criterios ESG, incluso a través de la emisión de bonos soberanos vinculados a la sostenibilidad.

Políticas e incentivos económicos que se implementan hace más de 30 años permiten que Uruguay registre hoy cero-deforestación en materia de bosque nativo, como lo demuestra la cartografía oficial correspondiente al año 2021. Este objetivo, que se vislumbra muy ambicioso al analizar la situación de los bosques naturales a nivel regional, se vuelve aún más exigente ante la competencia con otros usos del suelo que permiten actividades de mayor rentabilidad, así como por la amenaza de la tala ilegal. Para atender esta situación al mismo tiempo que proteger la biodiversidad, aumentar la captura de carbono y promover la resiliencia climática, a través de los Artículos 477, 478 y 491 de la Ley Nº 20.075, recientemente se reforzaron los incentivos tributarios para conservar los bosques nativos y mejorar los registros disponibles en Uruguay.

Para continuar la transición hacia la descarbonización, Uruguay busca reducir las emisiones de GElen los sectores Transporte e Industrial. El hidrógeno verde y sus productos derivados se perfilan como una fuente de energía con alto valor agregado y potencial de exportación dentro de esta nueva fase de transición de Uruguay. Sin embargo, la producción competitiva de hidrógeno verde se encuentra en sus etapas iniciales y avanzar en la innovación tecnológica es clave. Para fomentar la producción y el uso de hidrógeno verde como combustible limpio para descarbonizar el transporte de carga, industria y la agricultura, se ha creado el programa "Fondo Hidrógeno Verde" para promover la innovación y la investigación en Hidrógeno Verde y sus derivados, combustibles sintéticos en particular, como lo demuestra el acuerdo entre el Ministerio de Industrias, Energía y Minería (MIEM), el Laboratorio Tecnológico de Uruguay (LATU) y la Agencia Nacional de Investigación e Innovación (ANII), de fecha 30 de marzo de 2022.Como consecuencia se espera que esta medida apoye la inversión para establecer las bases de esta nueva fuente de energía renovables y, en el proceso, ayude a Uruguay a apuntalar capacidades y tecnologías para desarrollar el sector en el futuro.

El segundo pilar de la operación busca promover un crecimiento económico más fuerte y diversificado, a través de medidas de facilitación del comercio y un mejor acceso a los alimentos y otros bienes importados a través de la reducción de aranceles externos, un marco de competencia fortalecido, un sector financiero más robusto para promover e intermediar de manera efectiva el ahorro en moneda nacional y ayudar a suavizar los impactos de shocks externos, y mayores oportunidades de acceso directo al crédito por parte de las mujeres rurales.

La economía de Uruguay tiene una integración limitada en las cadenas globales de valor. Las barreras comerciales obstaculizan el potencial de crecimiento del país, dificultan la diversificación de las exportaciones, limitan las inversiones y la capacidad de adaptación, por ejemplo, para afrontar efectos relacionados con el cambio climático, que ya están afectando los sistemas de producción y distribución de alimentos en todo el mundo. Para promover la resiliencia de los precios de los alimentos y los bienes esenciales frente a los shocks climáticos y globales y fomentar un sector transable competitivo, se ha reducido el arancel externo común en un promedio del 10% (diez por ciento) de acuerdo con los socios del Mercosur, y se ha reducido el cargo de importación para evaluar la conformidad regulatoria para alimentos importados de 1,5% (uno coma cinco por ciento) a 0,5% (cero coma cinco por ciento), como lo demuestra el Decreto Nº. 369/022, de 16 de noviembre de 2022, para implementar la Decisión del Consejo del Mercado Común del Mercosur Nº. 08/022 y por el Decreto Nº. 194/022, de 14 de junio de 2022. Se espera con esta medida apoyar a las empresas que importan insumos reduciendo la incertidumbre y los costos comerciales, y aumentando su eficiencia y competitividad. Además, dado que Uruguay es un importador neto de vegetales comestibles y alimentos preparados y bebidas, la eliminación de las barreras comerciales promoverá la seguridad alimentaria, al reducir los precios de los alimentos importados y atenuar la volatilidad de los precios.

Un mayor número de oferentes en un mercado fomenta la reducción de costos, la innovación, la productividad y el crecimiento económico, e induce a las empresas a ser más eficientes para tener éxito. Con el objetivo de fortalecer el marco de la política de competencia, aumentar la misma y fomentar la seguridad jurídica, se ha creado y puesto en funcionamiento una red de reguladores con facultades de aplicación de la competencia para reforzar la cooperación interinstitucional y promover el intercambio de información, como lo demuestra un Memorando de Entendimiento firmado el 22 de noviembre de 2022. Asimismo, se fortalecieron las reglas de control de fusiones al permitir un análisis más profundo en casos problemáticos y aprobar normas técnicas que aclaran elementos clave del marco regulatorio, como lo demuestra el artículo 147 de la Ley Nº 20.075, de 20 de octubre de 2022 y la Resolución Nº 175/022.Se espera que las medidas apoyadas en esta acción aumenten el número de decisiones antimonopolio y opiniones de defensa y se generen importantes ahorros para los consumidores.

El crédito al sector privado en Uruguay es bajo en comparación con otros países de la región. Esto limita la efectividad de la intermediación financiera, dificulta las ganancias de productividad del sector corporativo y limita las posibilidades de las familias y las empresas de amortiguar los efectos negativos de shocks, como los climáticos. Además, Uruguay posee un sistema financiero altamente dolarizado que podría impedir que los inversionistas tengan una referencia estable de retornos para inversiones en pesos nominales más allá del corto plazo, creando un obstáculo para el desarrollo del mercado de capitales. Para promover la inversión y el crédito en moneda nacional e instrumentos financieros de mayor plazo, se han implementado medidas para homogeneizar las tasas de rendimiento de los depósitos e instrumentos financieros en pesos uruguayos indexados y nominales; reducir las tasas impositivas para rendimientos en moneda local e inversiones a más largo plazo; y homogeneizar las tasas y plazos del impuesto sobre los rendimientos de las inversiones en depósitos bancarios e instrumentos de mercado, tal como lo establecen los artículos 485 y 487 de la Ley Nº 20.075, de 20 de octubre de 2022.Se espera con estas medidas fomentar el ahorro en moneda local y lograr una mayor oferta de financiamiento en pesos, reduciendo así la exposición de la economía real y del sector financiero a shocks externos. También se busca ampliar la oferta de financiamiento a más largo plazo, beneficiando la gestión financiera de las empresas locales.

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Las mujeres son una de las principales fuerzas productivas y en el año 2020 representaban el 44% (cuarenta y cuatro por ciento) de las personas en el Registro de Producción Familiar. Sin embargo, hay una gran brecha de género en el acceso al financiamiento, a subsidios, y en la participación en la toma de decisiones, especialmente en el sector agropecuario. Para ampliar el financiamiento de las empresas familiares rurales y agropecuarias lideradas por mujeres, se ha operacionalizado a través de la Agencia Nacional de Desarrollo (ANDE) y de la Corporación Nacional Financiera Administradora de Fondos de Inversión S.A. (CONAFIN AFISA), el Fondo de Garantía para la implementación de Políticas para el Desarrollo Rural (FOGADER), y se han firmado dos convenios con entidades financieras, evidenciado por el convenio suscrito entre CONAFIN AFISA y FUNDASOL, de 10 de marzo de 2022, y el convenio suscrito entre CONAFIN AFISA y República Microfinanzas S.A., de 8 de marzo de 2022. Se espera que esta medida permita a las instituciones de microfinanzas absorber más riesgo, aumentando los créditos a mujeres en granjas familiares y pequeñas empresas rurales. A mediano plazo, se espera generar un vínculo directo y sostenible entre las mujeres y las instituciones financieras y que la implementación de este fondo contribuya a reducir la brecha de género en el acceso al financiamiento en la agricultura familiar y las MIPYMES rurales.

En vista de lo anterior, el Gobierno de Uruguay considera necesario y pertinente contar con el apoyo del Banco Mundial para llevar adelante las acciones antes señaladas e impulsar los logros de los ambiciosos objetivos estratégicos de desarrollo trazados por el Gobierno.

Sin otro particular, aprovecho la oportunidad para saludar a ud. muy atentamente,

Azucena Arbeleche
Ministro de Economía y Finanzas
República Oriental del Uruguay

ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior Actions (PA)	Significant positive or negative environmental effects	Significant poverty, social, or distributional effects positive or negative
Pillar 1: Greening of the Economy		
PA#1. *To formalize Uruguay's climate commitments under the Paris Agreement, the Borrower has approved the second Nationally Determined Contributions (NDC) under the Paris Agreement framework, as evidenced by the UNCCS letter dated January 30, 2023, acknowledging submission of Uruguay's second NDC Submission.*	**Positive impact**. A positive impact on the environment is expected from the reduction of GHG emissions in different key sectors such as AFLOU, and energy.	No direct impact on poverty expected in the short term.
PA#2. *To enhance carbon sequestration, promote climate resilience, and protect biodiversity through the conservation of native forests, the Borrower has excluded native forests from the total property area that is used to calculate exceptions to various taxes, as evidenced by Articles 477, 478, and 491 of Law No. 20.075, dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*	**Positive impact.** Positive impact is expected on the environment and biodiversity from the protection of native forest ecosystems. It is also expected to increase native forest cover and decrease deforestation and timber logging resulting from improved conservation and management of native forest, leading to increased capacity to capture emissions.	No direct impact on poverty or inequality is expected in the short term.
PA#3. *To conserve marine ecosystems and preserve blue carbon sinks, the Borrower, through Ministry of Environment (MA), has identified new Marine Protected Areas covering at least 10% of Uruguay's Exclusive Economic Zones ("EEZs"), established a strategy for the protection of 30 percent of Uruguay's EEZs by 2030, and identified new areas considered "relevant for conservation" covering an estimated 30 percent of Uruguay's EEZ, as evidenced by Ministerial Resolution No. 1152/022, dated December 12, 2022.*	**Positive impact.** Positive impact is expected on the marine environment and its biodiversity from the protection of the marine areas. In addition, protecting the marine ecosystem is expected to result in an increased sequestration capacity and better adaptation to climate effects.	No negative distributional impact is expected as the priority marine areas identified for protection predominantly lie beyond the areas of artisanal and small-scale fishers. In the medium run, the creation of MPA can play a crucial role in sustaining fish stocks, thereby helping employment in the sector.
PA#4. *To advance environmental and social sustainability and climate goals and expand trade opportunities for low-carbon organic agricultural products, the Borrower, through Ministry of Livestock, Agriculture and Fisheries (MGAP), has systematized the certification of organic and integrated agricultural and*	**Positive impact.** Positive impacts are expected from promoting and adopting sustainable organic and agroecological productive practices such as reducing methane emissions. However, potential negative	Potential of positive indirect impacts on poverty reduction and shared prosperity expected from increased market efficiency.

aquaculture production, as evidenced by Decree No. 175/022, dated May 24, 2022 and published in the Official Gazette on May 31, 2022.	environmental impacts may result from the eventual extension of trade opportunities due to increased livestock and agriculture, leading to a rise in AFLOU emissions. Nevertheless, the MGAP has a strong capacity to mitigate potential adverse effects and implement measures that promote low carbon emissions while increasing productivity.	
PA#5. *To foster the production and use of green hydrogen as a clean fuel to decarbonize freight heavy industry and agriculture, the Borrower, through Ministry of Industry, Energy and Mining (MIEM), has created the program "Fondo Hidrógeno Verde" to promote innovation and research in Green Hydrogen and its derivatives, as evidenced by the agreement between the MIEM, Uruguay Technological Laboratory (LATU), and National Agency of Research and Innovation (ANII), dated March 30, 2022.*	**Positive impact.** Positive impact is expected on the promotion of a fund that promotes innovation and research since it is expected to lead to creative solutions that may reduce emissions and foster environmental sustainability. Potential negative effects might result from hydrogen combustion and production. However, are expected to be adequality manage through the Uruguayan Environmental Protection Law N°. 17.283, 2000 , through the article 17 which prohibits releasing or emitting into the atmosphere, directly or indirectly, materials or energy above the limits; and the Environmental Assessment Law N° 16466, 1994, and Regulations of Environmental Impact Assessment and Environmental Authorizations, Decree N°.349/005, 2005, and the and the Air Quality Regulation (N°. A 29, dated May 4, 2021), which establishes the limits.	The scale and scope of the pilot activities (up to US$10 million per project) are unlikely to have broad social effects or distributional impacts.
Pillar 2: Stronger and more Resilient Growth		
PA#6. *To promote food and essential goods price resilience against climate and global shocks and foster a competitive tradable sector, the Borrower, through MEF, has: (i) reduced its common external tariff on average by 10 percent in agreement with its Mercosur partners, as evidenced by Decree No. 369/022, dated November 11, 2022, and published in the Official Gazette on November 24, 2022, that adopted Mercosur's Common Market Council Decision No. 8/22; and (ii) reduced the import charges for assessing regulatory conformity for imported food items from 1.5 percent to 0.5 percent, as evidenced by*	**Neutral**. Neutral environmental impacts are expected from the inclusion of risk management criteria for foodstuff imports, reducing import tariffs. Potential negative effects from transportation and disposal of trade products. The MA along with the MGAP have a strong institutional capacity to evaluate and mitigate potential environmental impacts from imported goods.	Expected positive effect on the welfare of the poor and distributive outcomes in the medium term mainly through productivity gains and lower prices. But also, potentially small but negative short-term adverse effects to the bottom 40 through

Decree No. 194/022, dated June 14, 2022, and published in the Official Gazette on June 20, 2022.		employment fall in the sectors facing elimination of import tariffs.
PA#7. *To strengthen its competition policy framework, increase market contestability and foster legal certainty, the Borrower, through MEF, has: (i) created and operationalized a network of regulators with competition enforcement powers, to reinforce interinstitutional cooperation and promote information sharing as evidenced by a Framework Collaboration Agreement signed on November 22, 2022; and (ii) strengthened merger control rules by enabling more thorough analysis in problematic cases and approving technical norms clarifying key elements of the regulatory framework, as evidenced by Article 147 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022, and Resolution No. 175/022 dated August 23, 2022.*	**Neutral.** Neutral environmental impact is expected from creating a network of regulators with enforcement capacity and strengthening merger control, or at the very least would not result in any significant increased impacts or risks.	Expected positive effect on poverty reduction in the medium term, primarily through consumer savings due to lower prices.
PA#8. *To promote investment and credit in domestic currency and longer-term financial instruments, the Borrower has issued measures to: (i) homogenize rates for returns in indexed and nominal Uruguayan Pesos; (ii) reduce tax rates for returns in local currency and longer-term investments; and (iii) homogenize tax rates and terms for returns on investments in bank deposits and market instruments, as evidenced by Articles 485 and 487 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*	**Neutral.** Neutral environmental impact is expected from homogenizing tax rates across bank deposits and market instruments.	No direct impact on poverty is expected in the short term but improving the structure of credit markets can have indirect positive effects on poverty and equity.
PA#9. *To provide risk mitigation and expand financing for rural and agricultural family businesses led by women, the Borrower, through National Development Agency (ANDE) and National Financial Corporation Administrator of Investment Funds SA (CONAFIN AFISA), has operationalized the Guarantee Fund for the Implementation of Rural Development Policies (FOGADER), by executing two agreements with financial entities, as evidenced by the agreement executed between CONAFIN AFISA and Uruguayan Foundation for Solidarity Cooperation and Development (FUNDASOL), dated March 10, 2022, and the agreement executed between CONAFIN AFISA and República Microfinanzas S.A, dated March 8, 2022.*	**Neutral.** Neutral environmental impacts are expected from the credit guarantee fund established.	Expected positive effects on women's economic autonomy and improved household income of small producers in rural areas.

1. **The PSIA was developed according to the WB guidelines and designed to provide an analysis of the potential poverty and social impacts of the policy actions outlined in the DPL**. The PSIA outlines the expected impacts from a gender-informed, social and distributional perspective. The assessment is meant to provide a robust analysis of the policy actions included in this operation.

2. **The policy measures supported under this DPL are expected to play an important role in generating public goods in climate change adaptation and strengthening resilience against multiple shocks**. Pillar 1 emphasizes strengthening the basis for green growth and investment in climate change adaptation. Pillar 2 supports measures that are expected to enhance and diversify economic growth while strengthening preparedness and resilience against health, sanitary, and climate shocks.

3. **The PSIA is informed by quantitative analyses of the specific policies supported by this operation, together with a literature review of previous studies relevant to the prior actions.** Useful information to define parameters and assumptions to perform the quantitative analysis, as well as to organize the literature review, was gathered from previous evaluations by the Bank and other multilateral organizations, and from academic research papers.

4. Expected individual impacts of prior actions under the specific pillars are summarized below:

Pillar 1: Greening of the economy

Prior Action 1: *To formalize Uruguay's climate commitments under the Paris Agreement, the Borrower has approved the second Nationally Determined Contributions (NDC) under the Paris Agreement framework, as evidenced by the UNCCS letter dated January 30, 2023, acknowledging submission of Uruguay's second NDC Submission.*

5. **This PA is not expected to directly impact poverty and inequality in the short and medium terms.** However, in a broad perspective, strengthening the scope of framework legislation for climate change is expected to encompass vulnerability and distributional impact assessments which would help address potential regressive effects of decarbonization policies and increase climate adaptation. Depending on the policy tool, the sector addressed, the design of the policy, and the initial socio-economic conditions of different population groups, individual climate policy measures can have very different distributional effects.

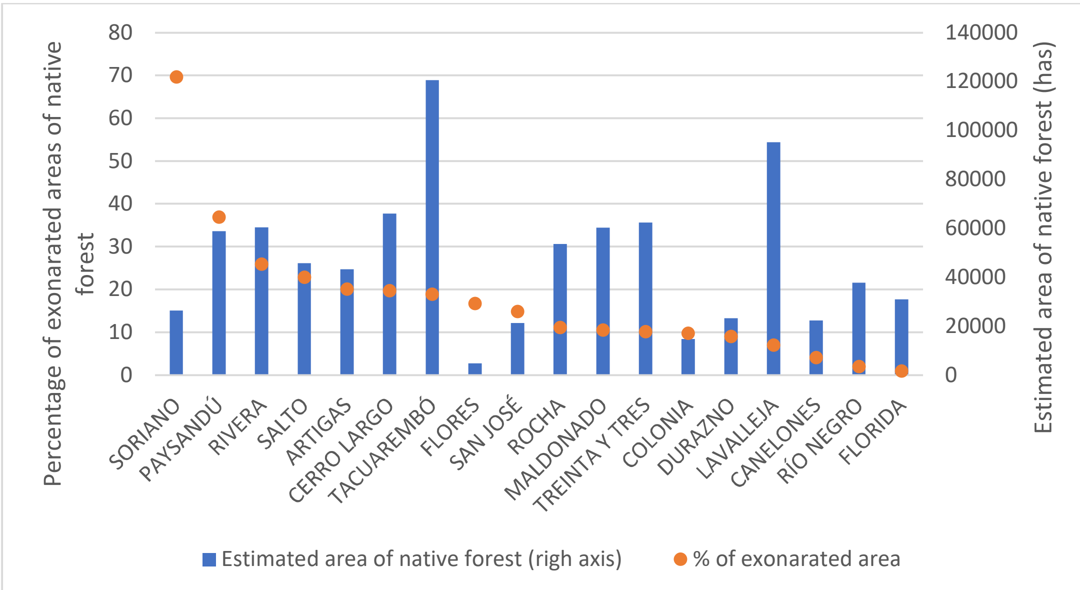
Prior Action 2: *To enhance carbon sequestration, promote climate resilience, and protect biodiversity through the conservation of native forests, the Borrower has excluded native forests from the total property area that is used to calculate exceptions to various taxes, as evidenced by Articles 477, 478, and 491 of Law No. 20.075, dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*

6. **In Uruguay practically 100 percent of the native forests are found on private property.**[91] A prospective analysis of the social and poverty impacts of the prior action is limited by the scarce information available. Forest registry information is not available in digital format and there is no database with the relevant information to carry out an analysis of the attributes of the registered native forest and its holders. While the results of the forest registry database's digitalization are awaited to extend the analysis, an exercise has been carried out with the exemption data for a specific year, 2016.[92] The estimations show Soriano as one of the departments with the

[91] National Strategy for Native Forests. MGAP. Uruguay. March 2018
[92] Ibid

highest percentage of native forest area that has obtained exonerations for the year 2016 (70 percent). It is followed by Paysandú with 37 percent, and the rest of the departments are below 25 percent.[93]

Figure A1. Extension of native forest with fiscal exemptions as a percentage of total estimated area of native forest, 2016



Source: Own elaboration based on Proyecto REDD+ Uruguay (2019)

7. **The total fiscal expenditure is not estimated to have indirect distributed effects of magnitude to consider.** Of the 580 thousand hectares of registered native forests, 27 percent applied for at least one tax exemption in 2016. These extensions represent 723 forests in 1897 lists (padrones), with a heterogeneous distribution by "*Departamentos"* (from 4 percent to 70 percent of the total extension of forest being exonerated). The fiscal expenditure associated with current tax benefits was estimated in about 3 million dollars in 2016 (0.03 percent of total tax revenues in 2016).[94]

8. **Tax incentives implemented under this PA will mostly affect medium-size landowners and are not expected to directly impact poverty and inequality in the short and medium term.** Data on the percentage of native forest within the total area to determine if a taxpayer is below or above the limit to access fiscal exemptions is not available. Nevertheless, an approximative exercise suggests that landowners of medium-size extensions would be those for whom the fiscal incentive is positive. Based on constructed hypothetical categories of land extensions with native forest constructed by P*royecto REDD+ Uruguay 2019* (see table A1), it is estimated that small landowners do not have incentives to register native forest, as the registering cost is higher than the fiscal benefit.[95] For this category of landowners, the adopted policies under PA 2 do not have implications as their land

[93] Native forest area estimated based on digital processing and interpretation of Landsat TM 2010 and 2011 images, information from the General Forestry Directorate and field support published in

[94] Proyecto REDD+ Uruguay (2019). Análisis tributario asociado al bosque nativo. Boccardo, A., Chiesa, V., García de Souza, M. L., Martino, D., Olivera, J. y Calleja, A. L. Ministerio de Ganadería, Agricultura y Pesca - Ministerio de Vivienda, Ordenamiento Territorial y Medio Ambiente. Montevideo.

[95] Estimations by Proyecto REDD+ Uruguay show that there are costs of registration associated with the requirement of a technical report by an authorized engineer of the MGAP, aerial pictures, stamps and documentation. There are also some certificates required by the tributary institutions. Assuming that these administrative and professional services costs are

is below the thresholds anyway. Although there may be variation depending on the proportion of native forest, registering the total land with native forest will not bring large landowners below the thresholds to be eligible for fiscal incentives (on average). In contrast, the average medium-sized landowner could at least get the exemption for the primary education tax (article 427) by registering native forest holdings.

Table A1. Hypothetical types of land extension and native forest areas, three simulated categories

	Simulated categories		
	Large	**Medium**	**Small**
Total average land area (ha)	1421	339	35
Native average forest area (ha)	113	46	16

9. **In the long run, fiscal policies that help reduce deforestation are expected to have positive effects on climate change mitigation and adaptation, water and food security, and the reduction of poverty.**[96] Although the empirical evidence on the costs and benefits of halting deforestation is not consistent, systematic literature reviews find significant important direct monetary benefits and thus an important element in the rationale for forest protection.[97] The estimates vary considerably with location and time and in relation to socio-economic conditions – for example, an increase in world demand for agricultural commodities would raise the opportunity cost of forest conservation.

Prior Action 3: *To conserve marine ecosystems and preserve blue carbon sinks, the Borrower, through Ministry of Environment (MA), has identified new Marine Protected Areas covering at least 10 percent of Uruguay's Exclusive Economic Zones ("EEZs"), established a strategy for the protection of 30 percent of Uruguay's EEZs by 2030, and identified new areas considered "relevant for conservation" covering an estimated 30 percent of Uruguay's EEZ, as evidenced by Ministerial Resolution No. 1152/022, dated December 12, 2022.*

10. **The establishment of MPA is often controversial, since excluding human activities from sea areas can have associated negative impacts on those sectors of the economy, or groups of society affected by the exclusion**.[98] It is commonly recognized that effectively managed MPA are an important tool to conserve critical habitats, ecosystem services, and the biodiversity that support human life. However, knowledge of ecosystem services and the benefits provided by offshore marine areas, including the welfare impacts from the establishment of MPA is still limited. Analytical exercises valuing the welfare impacts on population groups from offshore MPA show a wide array of ecosystem services provided by offshore habitats and the conservation benefits for the general public. For example, Pakalniete et al. 2021 show that in Latvia citizens' willingness-to-pay for preserving

distributed over a period of 10 years, the estimated total cost of registration for a small, medium and large landowner were US$156, US$146, and US$246 respectively in 2016. The estimated net benefit of registering for the corresponding type of landowners is US$116, US$314 and US$2914, respectively.

[96] World Bank (2021) "Designing Fiscal Instruments for Sustainable Forests", Washington, D.C. The World Bank and FAO. 2022. *The State of the World's Forests 2022*. Forest pathways for green recovery and building inclusive, resilient, and sustainable economies. Rome, FAO. https://doi.org/10.4060/cb9360en

[97] Rakatama, A., Pandit, R., Ma, C. & Iftekhar, S. 2017. The costs and benefits of REDD+: A review of the literature. *Forest Policy and Economics*, 75: 103–111. https://doi.org/10.1016/j.forpol.2016.08.006

Leblois, A., Damette, O. & Wolfersberger, J. 2017. What has driven deforestation in developing countries since the 2000s? Evidence from new remote-sensing data. *World Development*, 92: 82 102. https://doi.org/10.1016/j.worlddev.2016.11.012

[98] Ruiz-Frau, A.; Gibbons, J.M.; Hinz, H.; Edwards-Jones, G.; Kaiser, M.J. Preference classes in society for coastal marine protected areas. PeerJ. 2019, 7, e6672.

habitats in the Baltic Sea and environmental services supply exceeds their welfare losses from restrictions in economic activities.[99]

11. **PA 3 is not expected to have a negative distributional impact since the eventual protected areas are not those with economic activity of small-scale fisheries.** The priority areas identified for potential MPA predominantly lie beyond the twelve-mile coastal zone where artisanal and small-scale fishery are developed.

12. **In the medium run, the effect of sustaining fish stocks is expected to have positive impacts on poverty on household income generation and reduction of poverty.** The Uruguayan commercial fisheries sector is an important socio-economic resource for the country, generating a total gross production value of US$172 million[100] in 2016; however, employment in the fishing industry has decreased significantly over the past ten years (from around 3,000 in 2011 to roughly 1600 in 2022). The creation of MPA can play a crucial role in sustaining fish stocks, thereby helping to maintain employment in the sector (on average, 27 jobs were created for every ton of fish landed in 2021).[101]

Prior Action 4: *To advance* environmental and social sustainability and climate goals *and expand trade opportunities for low-carbon organic agricultural products, the Borrower, through Ministry of Livestock, Agriculture and Fisheries (MGAP), has systematized the certification of organic and integrated agricultural and aquaculture production, as evidenced by Decree No. 175/022, dated May 24, 2022 and published in the Official Gazette on May 31, 2022.*

13. **Certification of organic production for agriculture has the potential to positively impact poverty reduction and shared prosperity by increasing market efficiency.** To the extent that certification of organic products reduces information asymmetry along the marketing channel from producer to consumer, it makes the market more efficient and entails welfare gains. The potential in Uruguay is significant given the importance of its organic farmland area. In 2018, the area of organic farmland in Uruguay surpassed two million hectares, an increase of 14 percent in comparison to the previous year. That same year, Uruguay had the second largest organic farmland area in Latin America, ranking only behind Argentina.

14. **Expected effects on smallholder production systems in Uruguay are positive.** Evidence of certified organic production contributing to poverty reduction is mostly based on low and middle-income countries and shows that smallholder producers could benefit from price premium on certified organic produce through access to high-value markets; value addition on organic produce through processing and packaging; and surplus production caused by resulting from the change from conventional production to certified organic production.[102] Positive effects on poverty through these and other channels would not be realized if smallholders do not participate in organic production. Humphrey (2006) argues that stringent organic food safety standards may dissuade the participation of smallholder resource-constraint farmers in high-value markets and could lead to further exclusion.[103]

[99] Pakalniete, K.; Ahtiainen, H.; Aigars, J.; Andersone, I.; Armoškaite, A.; Hansen, H.S.; Strāķe, S. Economic Valuation of Ecosystem Service Benefits and Welfare Impacts of Offshore Marine Protected Areas: A Study from the Baltic Sea. *Sustainability* 2021, *13*, 10121. https://doi.org/10.3390/su131810121
[100] Supply and Utilization Tables published by BCU in 2016: the total gross production value of the fisheries sector (catch plus processing) amounted to about US$172 million.
[101] Current situation, prospects and opportunities for the development of the National Fishing Industry, report March 2023.
[102] IFOAM (International Federation of Organic Agriculture Movements) (2013). Productivity and profitability of organic farming systems in East Africa. Bonn, Germany.
[103] Humphrey, J. (2006). Policy implications of trends in agribusiness value chains. European Journal of Development Research, 18, 572–592.

Prior Action 5: *To foster the production and use of green hydrogen as a clean fuel to decarbonize freight heavy industry and agriculture, the Borrower, through Ministry of Industry, Energy and Mining (MIEM), has created the program "Fondo Hidrógeno Verde" to promote innovation and research in Green Hydrogen and its derivatives, as evidenced by the agreement between the MIEM, Uruguay Technological Laboratory (LATU), and National Agency of Research and Innovation (ANII), dated March 30, 2022.*

15. **Measures to promote innovation in green hydrogen production are not expected to have short term effects on poverty and equity.** The government's project funding pot for supporting research, innovation and training projects on green hydrogen aims to lay the foundations for the replication of entrepreneurship and business models contributing to accelerating the energy transition and the development of markets. The cost of producing green hydrogen is currently high-priced[104] and market-policies such as regulation, knowledge brokerage and innovation promotion could facilitate the uptake, for example by reducing the price of environmental goods and increasing the costs of conventional ones. In the short-term such repurposing of public resources is not expected to have distributional effects but more in-depth analysis is needed to appropriately assess potential effects in the long term.

16. **In the medium and long-run funding for research and development of hydrogen technologies is expected to contribute to the decarbonization of the energy production matrix and sustainable economic development.** Innovation promotion programs in other sectors in Uruguay show evidence of crowding-in of public support to innovation, and a larger probability in beneficiaries of successfully introducing new products and processes.[105] Evidence specific to green hydrogen is scarce as public policy in this area is only in the preliminary design stage, for example in Chile, the national green hydrogen strategy was recently launched, and the government has decided to earmark part of its public budget for what it has termed "R&D targeting national challenges".[106]

Pillar 2: Stronger and more Resilient Growth

Prior Action 6: *To promote food and essential goods price resilience against climate and global shocks and foster a competitive tradable sector, the Borrower, through MEF, has: (i) reduced its common external tariff on average by 10 percent in agreement with its Mercosur partners, as evidenced by Decree No. 369/022, dated November 11, 2022, and published in the Official Gazette on November 24, 2022, that adopted Mercosur's Common Market Council Decision No. 8/22; and (ii) reduced the import charges for assessing regulatory conformity for imported food items from 1.5 percent to 0.5 percent, as evidenced by Decree No. 194/022, dated June 14, 2022, and published in the Official Gazette on June 20, 2022.*

17. **The Prior Action is expected to have a positive welfare impact in the medium term.** The reduction of tariffs, non-tariff barriers, and controls for imports is expected to positively impact the bottom 40 percent of the population mainly through lower prices and productivity gains. The availability of lower-priced imported goods,

[104] Agaton, C. B., K. I. Talosig Batac and E. Medrano Reyes. 2022 "Prospects and challenges for green hydrogen production and utilization in the Philippines" International Journal of Hydrogen Energy, Vol 47, Issue 41.

[105] Bukstein, D., E. Hernandez and X. Usher. 2018. "Assessing the impacts on the innovation promotion programs aimed at the productive sectors: The case of ANII in Uruguay" *Estudios de Economía,* Vol. 45 no. 2 Diciembre 2018; pp. 271-299

[106] Economic Commission for Latin America and the Caribbean (ECLAC), Innovation for development: the key to a transformative recovery in Latin America and the Caribbean (LC/CCITIC.3/3), Santiago, 2022

particularly food, is expected to have positive effects on household disposable income, particularly among the poor people.

18. **Simulations by bank staff explore the expected effects of reduced import charges for food items[107][108] and find positive effects in the consumption of the lower portion of the distribution.** Potential effects range from the upper bound of a total pass-through scenario, to the potential lower bound of no pass-through (no effect in prices). We consider a total pass-through scenario, plus a partial pass-through scenario (100 and 15 percent pass-through to the final price respectively), since the lower bound of no pass-through is without changes from the baseline. The scenarios indicate market pass-through, i.e., changes in final prices for all of the market due to increased competition. The observed effect will depend on the market structure for each good, specifically on the weight of imports on final consumption[109]. Results indicate a reduction in the expenditure-income ratio ranging from 0.8 to 0.12 pp. For the first decile (table A3 and table A4). These results are 0.03 to 0.22 pp. For the highest income decile. Furthermore, the results show a reduction in the ratio between food expenditure and total expenditure from 0.42 pp. (Complete pass-through) to 0.06 pp. (Partial pass-through) for the first decile of income distribution (table A3 and table A4).

19. **The estimated potential positive effects of reduced import charges are important in the current context of inflation, which risk access and quality of food for low-income households.** Real wages are currently under pre-pandemic levels (in July 2022 real wages were 4 percent below the February 2020), and food inflation has been higher than general inflation (interannual inflation was 9.6 percent while the interannual food inflation was 11.5 percent in July 2022)[110]. These price increases have had a higher effect on lower-income households, as they allocate a higher proportion of their income to food. Food expenditure represents 32 percent of global expenditure for households in the first decile and 37 percent of their household income (while for the last decile these ratios are 15 percent and 10 percent respectively) (table A2).

20. **The presence of children is more concentrated in the lower deciles, implying a disproportionate effect of food price increases on children nutrition and development outcomes (figure A2).** 19 percent of children and adolescents live in poor households, compared with 10.6 percent for the overall population. Furthermore,

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[107] The first article of Mercosur's Common Market Council Decision No. 8/2022 establishes the reduction of CET for 6.886 codes (66 percent of total) from the Common Mercosur Nomenclature Annex I . The reduction of CET is 10 percent, except for products whose current CET is 2 percent, for which the new CET is 0 percent. This modification means that the average CET for codes in Annex I is reduced from 8.5 to 7.1 percent, and that the number of codes taxed 0 percent changes from 746 to 2869.
The second article of Decision No. 8/2022 allows Mercosur partners reduce the import tariff by 10 percent for products belonging to their respective annexes. For Uruguay, it includes 1409 codes from the Common Mercosur Nomenclature (Annex V) whose current average CET is 17,4 percent and could drop to 15,4 percent if the article was applied.
Additionally, the Decree No. 194/2022 reduced the tariff for attesting conformity and issuing the necessary import certificates for imported food and drinks, issued by LATU. This tariff decreased from 1.5 to 0.5 percent of the CIF value.

[108] The exercise assumes a CET of 8.5 percent, and a 1.5 percent LATU's rate for all foods and beverages prior to the enactment of the regulation. These tariffs are calculated over the final price including VAT. The exercise reduces the CET to 7,1 percent and LATU´s tariff to 0,5 percent for all foods and beverages.

[109] Share of imported products on household consumption varies greatly, from 3.2 percent for veal, to 82.2 percent for prepared or canned fruits and vegetables, according to data from BCU https://www.bcu.gub.uy/Estadisticas-e-Indicadores/Paginas/Utilizaci%C3%B3n-final-pc.aspx

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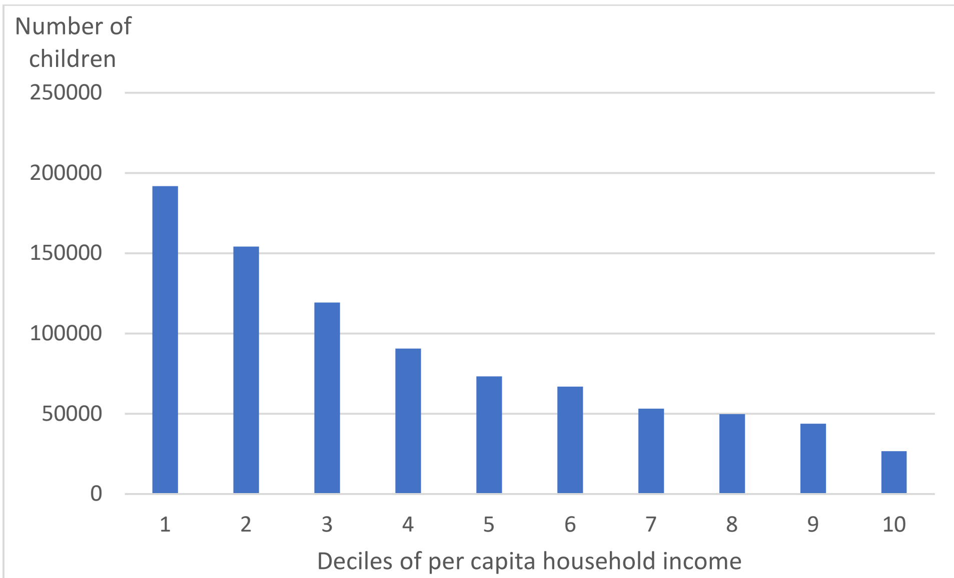
household typology analysis shows that 30.8 percent of children living in female single parent households are poor, which points to an unbalanced effect by gender[111]. The decrease in tariffs would reduce the final price of food and increase accessibility for lower income households, where most of Uruguay's children and adolescents live (54 percent of them are in the three first decile of the income distribution), disproportionately benefitting them, as well as single-mother households.

Figure A2. Number of children under 18 years of age, by income decile



Source: Continous Household Survey *(Encuesta Continua de Hogares)* (INE, 2021)

Table A2. Household expenditure and income ratio. Observed data (and pass-through 0%)

Deciles	Expenditure/Income	Food expenditure/ Expenditure	Food expenditure/Income
1	119.03%	32.11%	36.57%
2	89.40%	27.58%	23.82%
3	85.95%	25.57%	21.71%
4	84.25%	24.47%	19.64%
5	82.31%	23.07%	18.70%
6	79.58%	21.13%	16.19%
7	77.18%	20.84%	15.59%
8	76.02%	19.77%	14.36%
9	74.95%	17.12%	12.06%
10	69.14%	14.87%	9.86%

Source: Household Expenditure and Income Survey (*Encuesta de Gastos e Ingresos de los Hogares)* (INE, 2016-2017)

111 Continous Household Survey (*Encuesta Continua de Hogares*) 2021,INE

Table A3. Household expenditure and income ratio. Pass-through 100%

Deciles	Expenditure/Income	Food expenditure/ Expenditure	Food expenditure/Income
1	118.24%	31.69%	35.78%
2	88.88%	27.18%	23.30%
3	85.48%	25.18%	21.24%
4	83.82%	24.09%	19.21%
5	81.90%	22.71%	18.29%
6	79.22%	20.79%	15.83%
7	76.84%	20.50%	15.25%
8	75.71%	19.45%	14.05%
9	74.69%	16.83%	11.80%
10	68.93%	14.60%	9.65%

Source: Household Expenditure and Income Survey (*Encuesta de Gastos e Ingresos de los Hogares)* (INE, 2016-2017)

Table A4. Household expenditure and income ratio. Pass-through 15%

Deciles	Expenditure/Income	Food expenditure/ Expenditure	Food expenditure/Income
1	118.91%	32.04%	36.45%
2	89.32%	27.52%	23.74%
3	85.88%	25.51%	21.64%
4	84.19%	24.41%	19.58%
5	82.25%	23.02%	18.64%
6	79.52%	21.08%	16.13%
7	77.13%	20.79%	15.54%
8	75.97%	19.72%	14.31%
9	74.91%	17.07%	12.02%
10	69.11%	14.83%	9.83%

Source: Household Expenditure and Income Survey (*Encuesta de Gastos e Ingresos de los Hogares)* (INE, 2016-2017)

21. Potentially small but negative short-term adverse effects to the bottom 40 through employment fall in the sectors facing reductions of import tariffs. Direct employment effects in the sectors facing elimination of import tariffs are estimated to be small and contained, given the scale of tariff reductions and the sectors involved.[112]

Prior Action 7: *To strengthen its competition policy framework, increase market contestability and foster legal certainty, the Borrower, through MEF, has: (i) created and operationalized a network of regulators with competition enforcement powers, to reinforce interinstitutional cooperation and promote information sharing as evidenced by a Framework Collaboration Agreement signed on November 22, 2022; and (ii) strengthened merger control rules by enabling more thorough analysis in problematic cases and approving technical norms clarifying key elements of the regulatory framework, as evidenced by Article 147 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022, and Resolution No. 175/022 dated August 23, 2022.*

[112] For example, fuel, minerals, and chemicals represent the sectors with higher tariff reduction.

22. **Strengthening competition and reducing market frictions are expected to bring positive distributional impacts, although these would mainly materialize in the medium term.** Beyond the known effects on growth and productivity, strengthening market contestability could have important effects on poverty reduction. Having the right mechanisms to sanction, eliminate and deter anticompetitive behavior can generate substantial consumer savings, particularly for the poor people, who are typically the most affected by it.

23. **A solid institutional framework that prevents collusive behavior is expected to positively affect welfare via the price reduction mechanism, especially among households at the bottom of the income distribution. There is worldwide evidence of the negative distributional effects arising from a lack of competition as well as the positive outcomes associated with promoting competition as a mechanism for poverty alleviation.**[113] Both theoretical models and empirical work tend to suggest that a lack of competition in product markets stifles employment in the long term and/or on aggregate. The basic intuition is that less intense competition raises prices above marginal cost, reducing output demanded by consumers and, therefore, reducing labor demanded by producers. An increase in prices also reduces real wages, which can reduce the supply of labor.[114] Anticompetitive regulation and behavior can also harm low-income producers, for example by raising the cost of inputs. This is particularly the case when a lack of competition raises the price of agricultural inputs such as fertilizers, seeds and transport services.[115]

24. **The effects on welfare, especially among households at the bottom of the income distribution, are expected to take place through the price reduction mechanism.** An analytical empirical exercise for Mexico shows that impact of competition will depend on a combination of factors, including market structure, price elasticities and consumption patterns. More competition in the corn flour and mobile phone markets would reduce poverty and inequality. Estimates using WELCOM suggest that moving into perfect competition in the markets for corn flour and mobile communications would induce a combined reduction in poverty of 1.27 percentage points.[116] Because the consumption share of corn is higher among low-income households, gains from competition would disproportionally benefit the poor people. The results of the exercise in Mexico show that relative benefits of competition in the mobile market would be almost uniform across the distribution because households have lower price elasticity for mobile phones, and expenditure shares are similar across the income distribution. In previous evidence for Australia, Creedy and Dixon (1998) find that the welfare loss associated with monopoly power for 14 commodity groups in Australia is higher for low-income households than for high-income households. In particular, the loss is 46 percent higher for the lowest decile than for the highest. [117] Argent and Begazo (2015) find that in the case of Kenya, market reforms in the sugar and maize markets would increase the disposable income of consumers, especially the poorest, even after considering the dual role of households as producers and consumers of maize. They find that allowing sugar and maize prices to fall by 20 percent by relaxing trade barriers that shield the domestic sugar industry from competition and limiting government interventions that distort prices would lead to welfare gains for all income deciles, leading to a 1.5 percent fall in poverty in the case of sugar and 1.8 percent in the case of maize, with relatively higher gains for the poorest.[118]

[113] See World Bank Group; World Bank; Organization for Economic Co-operation and Development. 2017. A Step Ahead: Competition Policy for Shared Prosperity and Inclusive Growth. Trade and Development. Washington, DC: World Bank.
[114] See World Bank Group; World Bank; Organization for Economic Co-operation and Development. 2017. A Step Ahead: Competition Policy for Shared Prosperity and Inclusive Growth. Trade and Development. Washington, DC: World Bank.
[115] Begazo Gomez, Tania Priscilla; Nyman, Sara. 2016. Competition and poverty; note no. 350. Washington, D.C. : World Bank Group
[116] Abdelkrim A., S. Olivieri, C. Rodriguez Castelan and E. A. Malasquez Carbonel. 2017. "W*ELCOM:* **WEL**fare and **COM**petition Stata Package", World Bank. http://dasp.ecn.ulaval.ca/webwel/welcom.html
[117] Creedy, J., and R. Dixon. 1998. "The Relative Burden of Monopoly on Households with Different Incomes." Economica 65 (258): 285–93.
[118] Argent, Jonathan, and Tania Begazo. "Competition in Kenyan markets and its impact on income and poverty: a case study on sugar and maize." World Bank Policy Research Working Paper 7179 (2015).

25. **Recent empirical evidence shows that competition law enforcement is an important complement to traditional poverty reduction programs such as conditional cash transfers to the poor people.** Tackling anticompetitive behavior -especially in the food and basic goods sectors- is key in preventing public transfers to the poor people from leaking into anti-competitive profits, given the significant proportion of cash transfers that tends to be spent in these sectors.[119] For the case of the Dominican Republic, evidence shows that entry of new grocery stores into a defined market leads to significant reduction in prices (without change in quality) of products consumed by beneficiaries of governmental cash transfers.[120] In South Africa, reduction in overall poverty across household goods from tackling only four cartels on staple food products was 0.40 percentage points, equivalent to around 202,000 individuals – an impact more than 30 times larger than those achieved by cash transfer programs in the country, considering the difference in public funds invested on each policy.[121]

26. **Institutional and regulatory reforms to the competition policy framework that allow detecting and deterring price-fixing cartels will be better able to protect the poor people from anti-competitive overcharges.** The introduction of leniency programs has been shown to be associated with an increase in the number of cartels investigated and punished by around 60 percent and deterrence on the formation of cartels in the same proportion.[122] Such cartel agreements charge on average 49 percent higher prices. [123] Additional sector-specific measures, e.g., In telecommunications, have the potential to increase coverage of critical connectivity services for the bottom 40 percent.

Prior Action 8: *To promote investment and credit in domestic currency and longer-term financial instruments, the Borrower has issued measures to: (i) homogenize rates for returns in indexed and nominal Uruguayan Pesos; (ii) reduce tax rates for returns in local currency and longer-term investments; and (iii) homogenize tax rates and terms for returns on investments in bank deposits and market instruments, as evidenced by Articles 485 and 487 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*

27. **Measures to improve the monetary policy framework and develop the peso credit market are not expected to have a direct impact on poverty in the short term but the structure of credit markets can affect poor people indirectly**. Credit markets and safe asset markets for saving are major instruments for coping with income volatility. Eliminating distortions in these markets can support availability of credit to the private sector and the ability of the population to follow consumption smoothing patterns. Two main channels could have indirect effects on the vulnerable. First, de-dollarization of the economy is expected to reduce external inflation pressures, which could in turn reduce inflation and have positive effects on the vulnerable, considering that they are disproportionately affected by inflation[124]. Second, a deeper peso credit market is expected to decrease

[119] Urzua, C. 2013. "Distributive and Regional Effects of Monopoly Power." *Economia Mexicana NUEVA EPOCA* 22 (2): 279–95. Atkin, Faver and Gonzalez-Navarro, 2015.
World Bank, 2017. *A Step Ahead: Competition Policy for Shared Prosperity and Inclusive Growth*. Washington, DC: World Bank.
[120] Busso, M., and S. Galiani. 2014. "The Causal Effect of Competition on Prices and Quality: Evidence from a Field Experiment." NBER Working Paper 20054, National Bureau of Economic Research, Cambridge, MA.
[121] See Purfield, Catriona Mary; Hanusch, Marek; Algu, Yashvir; Begazo Gomez, Tania Priscilla; Martinez Licetti, Martha; Nyman, Sara. 2016. South Africa economic update: promoting faster growth and poverty alleviation through competition. South Africa economic update; issue no. 8. Washington, D.C.: World Bank Group.
[122] See Miller (2009). Klein (2011) based on data from 23 OECD countries shows that leniency policies were associated with a decrease in the industry-level price-cost margin by 3 to 5 percent.
[123] Statistics based on the worldwide most comprehensive database of cartel overcharges (See Connor, J. 2014. *Price-Fixing Overcharges: Revised 3rd Edition* (February 24, 2014).
[124] Ybrayev, Z (2022). Distributional Consequences of Monetary Policy in Emerging Economies: Dollarization, Domestic Inflation, and Income Divergence. Comp Econ Stud 64, 186–210. https://doi.org/10.1057/s41294-021-00163-2

volatility and support private sector development, fostering economic growth and labor markets.

Prior Action 9: *To provide risk mitigation and expand financing for rural and agricultural family businesses led by women, the Borrower, through National Development Agency (ANDE) and National Financial Corporation Administrator of Investment Funds SA (CONAFIN AFISA), has operationalized the Guarantee Fund for the Implementation of Rural Development Policies (FOGADER), by executing two agreements with financial entities, as evidenced by the agreement executed between CONAFIN AFISA and Uruguayan Foundation for Solidarity Cooperation and Development (FUNDASOL), dated March 10, 2022, and the agreement executed between CONAFIN AFISA and República Microfinanzas S.A, dated March 8, 2022.*

28. **The policy is expected to reduce existing gender gaps and positively impact poverty and vulnerability reduction.** Increased access to credit is expected to improve household income for rural family producers, through increased productivity, diversification of economic activities, and employment creation. In addition, gender gaps in ownership and decision-making are expected to be reduced in the medium term as more women engage in entrepreneurial activities and become empowered as subjects to credit.

29. **Barriers that hamper women's access to the services and products of the formal financial system remain in Uruguay, particularly in the rural sector.** In Uruguay, according to the latest Agriculture Census, only 23 percent of all registered agricultural producers are women, and they represent 21 percent of the total farmland ownership. The land under women's ownership diminished by 32 percent from the previous Census in 2020.[44] Florit and others[45] found important gender gaps within the registered owners of family farms applying for subsidies, as 87 percent of male owners were also the main decision-makers, compared to only 34 percent of female owners. Bernheim[46] surveyed women working in dairy farms, horticulture and cattle raising and found that 44 percent participate "little or nothing" in decision-making, and that 28 percent wished they could participate more. Female rural workers routinely contribute to social security under the "helping spouse" modality (*cónyuge colaborador*)[47]. This implies a link between social protection and family relationships, and subdues women's role to men's, as well as making it harder to legally own a business, even though it does allow for increased social protection in some cases[48][49]. This prior action directly responds to an existing specific gender equality gap. Although in Uruguay there already exist instruments for credit guarantees for women-owned micro and small businesses, often rural and more vulnerable households don't have access to this credit because of previous barriers for women to legally constitute and register as owners. The guarantee fund for rural development policies implemented directly targets small family producers making women eligible even when the family business is not registered under their ownership.

30. **An increase in loans for women in family farms will help foster productivity and economic diversification increasing resiliency to shocks.** The evidence across regions and countries shows that credit constraints on households negatively impact agricultural productivity, household income and vulnerability.[50] There is consensus on the relevance of family production for food security, agricultural job creation, poverty mitigation, preservation of biodiversity and cultural heritage. Family production in Uruguay represents up to 30 percent of the agricultural gross value of production, including 80 percent of horticultural products. Nevertheless, there are people in rural areas still living in isolation and vulnerability. In fact, 47 percent of people in these areas show at least one unsatisfied basic need. Main barriers for family production include traditional production systems with low productivity and limited access to credit. [51] In addition, women continue to face exclusion from the formal financial system and the strategies directed towards them have been mainly focused on microcredit programs. In middle-income countries, microcredit interventions tend to be too small to impact income diversification and non-financial asset accumulation.[52] The instrument of credit guarantees provides support to cover the financing needs of productive activities and medium and long-term investments of women in family farmers. In European countries, evidence shows that women can be at the forefront of innovation and diversification in rural areas by developing new activities, products, and services. Therefore, the implementation of credit guarantees could help tackle the barriers, providing access to credit that could foster investment for increased productivity as traditional productive systems are updated.

31. **On the supply side, the implementation of credit guarantees is expected to incentivize financial institutions to expand their supply in the medium term and help reduce gender gaps in access to productive resources.** Although the number of direct beneficiaries of credits supported through this policy is relatively small, high repayment rates in microfinance projects to women suggest that, in the medium term, the guaranteed instruments can efficiently remove the barrier to access to credit for women and help establish a relationship with the financial institution for a developed demand over time.

32. **The policy is expected to contribute to women's economic autonomy and improve household income in rural areas.** Dual-earner households are more resilient, as they are generally better-off, and having two distinct sources of income provides more flexibility in case of shocks. [53][54] 46 percent of rural households in 2017 did not include a female earner, compared with 33 percent of non-rural households[55].

ANNEX 5: PARIS ALIGNMENT ASSESSMENT

Program Development Objective(s): The Program Development Objective is to promote i) greening of the economy, and ii) stronger and more resilient growth.	
Step 1: Taking into account our climate analysis (e.g., Country Climate and Development Reports or CCDRs), is the operation consistent with the country climate commitments, including for instance, the NDC, NAP, LTS, and other relevant strategies?	**Answer:** Yes **Explanation**: The approval of Uruguay's second NDC in late 2022 informed by a technical assistance from the WB, is included in the policy actions and constitutes a critical long-term commitment towards achievement of global GHG emission reduction goals, and climate resilience and adaptation targets. Furthermore, on adaptation, the actions are also consistent with the strategies included in the National Adaptation Plan, particularly the Agriculture Adaptation Plan, supported directly through prior actions 4 and 9. Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs, and Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.
Mitigation goals: assessing and reducing the risks	
Prior Action 1. *To formalize Uruguay's climate commitments under the Paris Agreement, the Borrower has approved the second Nationally Determined Contributions (NDC) under the Paris Agreement framework, as evidenced by the UNCCS letter dated January 30, 2023, acknowledging submission of Uruguay's second NDC Submission*.	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** No. **Explanation**: The action is supporting the formalization of the country's climate commitments, specifically the Nationally Determined Contribution (NDC).
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** N/A
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 1: Aligned on mitigation	
Prior Action 2. *To enhance carbon sequestration, promote climate resilience, and protect biodiversity through the conservation of native forests, the Borrower has excluded native forests from the total property area that is used to calculate exceptions to various taxes, as evidenced by Articles 477, 478, and 491 of Law No. 20.075, dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** No. **Explanation**: the action supports fiscal incentives to encourage the registration of native forests and promote their

	conservation by avoiding deforestation and degradation, thus, preventing emissions and maintaining carbon sinks.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** N/A
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 2: Aligned on mitigation	
Prior Action 3. *To conserve marine ecosystems and preserve blue carbon sinks, the Borrower, through Ministry of Environment (MA), has identified new Marine Protected Areas covering at least 10 percent of Uruguay's Exclusive Economic Zones ("EEZs"), established a strategy for the protection of 30 percent of Uruguay's EEZs by 2030, and identified new areas considered "relevant for conservation" covering an estimated 30 percent of Uruguay's EEZ, as evidenced by Ministerial Resolution No. 1152/022, dated December 12, 2022.*	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** No. **Explanation**: the action supports the establishment of new MPA, with interventions that will support the conservation of marine ecosystems, and the carbon removal and sequestrations through the protection of blue carbon sinks.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** N/A
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 3: Aligned on mitigation	
Prior Action 4. *To advance environmental and social sustainability and climate goals and expand trade opportunities for low-carbon organic agricultural products, the Borrower, through Ministry of Livestock, Agriculture and Fisheries (MGAP), has systematized the certification of organic and integrated agricultural and aquaculture production, as evidenced by Decree No. 175/022, dated May 24, 2022 and published in the Official Gazette on May 31, 2022.*	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** No. **Explanation**: the action is expected to reduce emissions from agricultural production by establishing a certification scheme for organic agriculture which involves avoiding synthetic fertilizers and chemicals and being less energy intensive, thus, reducing the carbon footprint while promoting practices that increase farm biodiversity and soil carbon. Furthermore, long-term impacts due to land/aquaculture

	expansion are not expected as productivity is not expected to decline as a result of this measure.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** N/A
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 4: Aligned on mitigation	
Prior Action 5. *To foster the production and use of green hydrogen as a clean fuel to decarbonize freight heavy industry and agriculture, the Borrower, through Ministry of Industry, Energy and Mining (MIEM), has created the program "Fondo Hidrógeno Verde" to promote innovation and research in Green Hydrogen and its derivatives, as evidenced by the agreement between the MIEM, Uruguay Technological Laboratory (LATU), and National Agency of Research and Innovation (ANII), dated March 30, 2022..*	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** No. **Explanation**: 97 percent of Uruguay's electricity matrix is provided by renewable energy sources. To further reduce emissions from sectors such as transport and industries, the policy established a fund to promote research, innovation, and development of renewable-based Green Hydrogen.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** N/A
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 5: Aligned on mitigation	
Prior Action 6. *To promote food and essential goods price resilience against climate and global shocks and foster a competitive tradable sector, the Borrower, through MEF, has: (i) reduced its common external tariff on average by 10 percent in agreement with its Mercosur partners, as evidenced by Decree Nº 369/022, dated November 11, 2022, and published in the Official Gazette on November 24, 2022, that adopted Mercosur's Common Market Council Decision No. 8/22; and (ii) reduced the import charges for assessing regulatory conformity for imported food items from 1.5 percent to 0.5 percent, as evidenced by Decree No. 194/022, dated June 14, 2022, and published in the Official Gazette on June 20, 2022.*	
Pillar Objective: Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer: Yes**. **Explanation**: Stimulating international trade by making imported goods more affordable can lead to an increase

	in the volume of goods being transported across long distances, potentially resulting in higher GHG emissions from transportation.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** No. While trade might lead to increased emissions, these are not expected to be significant in the Uruguayan context. Nevertheless, the country has a framework in place for decarbonizing the transport sector (maritime and river-based) which reduce transition risks.
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 6: Aligned on mitigation	
Prior Action 7. *To strengthen its competition policy framework, increase market contestability and foster legal certainty, the Borrower, through MEF, has: (i) created and operationalized a network of regulators with competition enforcement powers, to reinforce interinstitutional cooperation and promote information sharing as evidenced by a Framework Collaboration Agreement signed on November 22, 2022; and (ii) strengthened merger control rules by enabling more thorough analysis in problematic cases and approving technical norms clarifying key elements of the regulatory framework, as evidenced by Article 147 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022, and Resolution No. 175/022 dated August 23, 2022.*	
Pillar Objective: Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** No. **Explanation**: This action aims to strengthen the institutional framework to strengthen competition, and as such, it is expected to have neutral impacts on GHG emissions.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** N/A
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 7: Aligned on mitigation	
Prior Action 8. *To promote investment and credit in domestic currency and longer-term financial instruments, the Borrower has issued measures to: (i) homogenize rates for returns in indexed and nominal Uruguayan Pesos; (ii) reduce tax rates for returns in local currency and longer-term investments; and (iii) homogenize tax rates and terms for returns on investments in bank deposits and market instruments, as evidenced by Articles 485 and 487 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*	
Pillar Objective: Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.	

Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** No. **Explanation**: The action is expected to have neutral impacts on GHG emissions.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** N/A
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 8: Aligned on mitigation	
Prior Action 9. *To provide risk mitigation and expand financing for rural and agricultural family businesses led by women, the Borrower, through National Development Agency (ANDE) and National Financial Corporation Administrator of Investment Funds SA (CONAFIN AFISA), has operationalized the Guarantee Fund for the Implementation of Rural Development Policies (FOGADER), by executing two agreements with financial entities, as evidenced by the agreement executed between CONAFIN AFISA and Uruguayan Foundation for Solidarity Cooperation and Development (FUNDASOL), dated March 10, 2022, and the agreement executed between CONAFIN AFISA and República Microfinanzas S.A, dated March 8, 2022.*	
Pillar Objective: Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.	
Step M2.1: Is the prior action likely to cause a significant increase in GHG emissions?	**Answer:** No. **Explanation**: While increased access to credit would increase production and corresponding GHG emissions, the universe targeted with this program is small in absolute numbers. As the aim is to close financial and gender gaps for this relegated group it is not expected that it will lead to a significant increase in emissions.
Step M2.2: Is the prior action likely to introduce or reinforce significant and persistent barriers to transition to the country's low-GHG emissions development pathways?	**Answer:** N/A
Step M3: Is the risk of the prior action introducing or reinforcing significant and persistent barriers being reduced to low after mitigation measures have been implemented?	**Answer:** N/A
Conclusion for PA 9: Aligned on mitigation	
Mitigation goals: Conclusion of the Paris Alignment Assessment for the Program	
Adaptation and resilience goals: assessing and managing the risks	
Prior Action 1: *To formalize Uruguay's climate commitments under the Paris Agreement, the Borrower has approved the second Nationally Determined Contributions (NDC) under the Paris Agreement framework, as evidenced by the UNCCS letter dated January 30, 2023, acknowledging submission of Uruguay's second NDC Submission.*	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	

Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** No. **Explanation**: The NDC includes the climate plans which are meant to guide adaptation efforts at national level.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** N/A
Conclusion for Prior Action 1: Aligned on adaptation	
Prior Action 2: *To enhance carbon sequestration, promote climate resilience, and protect biodiversity through the conservation of native forests, the Borrower has excluded native forests from the total property area that is used to calculate exceptions to various taxes, as evidenced by Articles 477, 478, and 491 of Law No. 20.075, dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** No. **Explanation**: the action aims at incentivizing native forest registration, which is expected to lead to their conservation, as such, it is not expected to be impacted by climate hazards.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** N/A
Conclusion for Prior Action 2: Aligned on adaptation	
Prior Action 3: *To conserve marine ecosystems and preserve blue carbon sinks, the Borrower, through Ministry of Environment (MA), has identified new Marine Protected Areas covering at least 10 percent of Uruguay's Exclusive Economic Zones ("EEZs"), established a strategy for the protection of 30 percent of Uruguay's EEZs by 2030, and identified new areas considered "relevant for conservation" covering an estimated 30 percent of Uruguay's EEZ, as evidenced by Ministerial Resolution No. 1152/022, dated December 12, 2022.*	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** Yes. **Explanation**: Marine ecosystems are vulnerable to risks from climate hazards, such as rising ocean temperatures, which could considerably reduce marine food provisioning, fisheries distribution, revenue values, and provision of ecosystem services through reduced functioning.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** Yes. **Explanation** The PA considers a network of connected MPA, including protection of the water column and its associated fauna to strengthen ecosystem resilience in the face of increased pressure on fishery stocks, and alterations in their composition and productivity due to climate change.
Conclusion for Prior Action 3: Aligned on adaptation	
Prior Action 4: *To advance environmental and social sustainability and climate goals and expand trade opportunities for low-carbon organic agricultural products, the Borrower, through Ministry of Livestock, Agriculture and Fisheries (MGAP),*	

has systematized the certification of organic and integrated agricultural and aquaculture production, as evidenced by Decree No. 175/022, dated May 24, 2022 and published in the Official Gazette on May 31, 2022.	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** No. **Explanation**: The PA harmonizes organic certification across the agricultural sector, establishes a national registry of certifiers, and increases transparency in the procedures required to obtain certification. In fact, organic agriculture promotes practices that preserve natural resources, increase farm biodiversity and soil carbon, without use of synthetic chemical inputs or genetically modified organisms or their derivatives, thus, it increases resilience against climate impacts.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** N/A
Conclusion for Prior Action 4: Aligned on adaptation	
Prior Action 5: *To foster the production and use of green hydrogen as a clean fuel to decarbonize freight heavy industry and agriculture, the Borrower, through Ministry of Industry, Energy and Mining (MIEM), has created the program "Fondo Hidrógeno Verde" to promote innovation and research in Green Hydrogen and its derivatives, as evidenced by the agreement between the MIEM, Uruguay Technological Laboratory (LATU), and National Agency of Research and Innovation (ANII), dated March 30, 2022.*	
Pillar Objective: Pillar 1 seeks to promote greening of the economy through policy actions that generate GPGs.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** No. **Explanation**: Climate risks are not expected to adversely impact this reform.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** N/A
Conclusion for Prior Action 5: Aligned on adaptation	
Prior Action 6: *To promote food and essential goods price resilience against climate and global shocks and foster a competitive tradable sector, the Borrower, through MEF, has: (i) reduced its common external tariff on average by 10 percent in agreement with its Mercosur partners, as evidenced by Decree No. 369/022, dated November 11, 2022, and published in the Official Gazette on November 24, 2022, that adopted Mercosur's Common Market Council Decision No. 8/22; and (ii) reduced the import charges for assessing regulatory conformity for imported food items from 1.5 percent to 0.5 percent, as evidenced by Decree No. 194/022, dated June 14, 2022, and published in the Official Gazette on June 20, 2022.*	
Pillar Objective: Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.	

Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** No. **Explanation**: Given Uruguay's dependence on the agriculture sector, which is itself climate-vulnerable, and its limited integration into global value chains, the PA aims at increasing the country's ability to deal with climate impacts by reducing trade barriers that hinder the country's ability to smooth shocks such as those linked to climate change.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** N/A
Conclusion for Prior Action 6: Aligned on adaptation	
Prior Action 7: *To strengthen its competition policy framework, increase market contestability and foster legal certainty, the Borrower, through MEF, has: (i) created and operationalized a network of regulators with competition enforcement powers, to reinforce interinstitutional cooperation and promote information sharing as evidenced by a Framework Collaboration Agreement signed on November 22, 2022; and (ii) strengthened merger control rules by enabling more thorough analysis in problematic cases and approving technical norms clarifying key elements of the regulatory framework, as evidenced by Article 147 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022, and Resolution No. 175/022 dated August 23, 2022.*	
Pillar Objective: Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** No. **Explanation**: Climate risks are not expected to adversely impact this reform.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** N/A
Conclusion for Prior Action 7: Aligned on adaptation	
Prior Action 8: *To promote investment and credit in domestic currency and longer-term financial instruments, the Borrower has issued measures to: (i) homogenize rates for returns in indexed and nominal Uruguayan Pesos; (ii) reduce tax rates for returns in local currency and longer-term investments; and (iii) homogenize tax rates and terms for returns on investments in bank deposits and market instruments, as evidenced by Articles 485 and 487 of Law No. 20.075 dated October 20, 2022 and published in the Official Gazette on November 3, 2022.*	
Pillar Objective: Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** No. **Explanation**: Climate risks are not expected to adversely impact this reform.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** N/A

Conclusion for Prior Action 8: Aligned on adaptation	
Prior Action 9: *To provide risk mitigation and expand financing for rural and agricultural family businesses led by women, the Borrower, through National Development Agency (ANDE) and National Financial Corporation Administrator of Investment Funds SA (CONAFIN AFISA), has operationalized the Guarantee Fund for the Implementation of Rural Development Policies (FOGADER), by executing two agreements with financial entities, as evidenced by the agreement executed between CONAFIN AFISA and Uruguayan Foundation for Solidarity Cooperation and Development (FUNDASOL), dated March 10, 2022, and the agreement executed between CONAFIN AFISA and República Microfinanzas S.A, dated March 8, 2022.*	
Pillar Objective: Pillar 2 helps to promote stronger and more resilient growth through actions that enhance competitiveness, economic diversification, and development.	
Step A2: Are risks from climate hazards likely to have an adverse effect on the prior action's contribution to the Development Objective(s)?	**Answer** No. **Explanation**: Facilitating access to credit for women to support their economic activities can actually support them in the face of climate shocks.
Step A3: Does the design of the prior action reduce the risk from climate hazards to an acceptable level, considering climate adaptation good practices applicable to the country context?	**Answer** N/A
Conclusion for Prior Action 9: Aligned on adaptation	
Adaptation and resilience: All PAs are aligned with the adaptation goals of the Paris Agreement	
OVERALL CONCLUSION OF PARIS ALIGNMENT ASSESSEMENT: The DPL is fully aligned with and supporting the mitigation and resilience goals of the Paris Alignment.	

ANNEX 6: IBRD INTEREST BUYDOWN: – KEY PERFORMANCE INDICATORS, TARGETS AND LENDING RATE REDUCTION

Objective

1. **The objective of the proposed mechanism is to reinforce positive incentives for the Government of Uruguay to achieve ambitious environmental goals during the IBRD loan repayment period, through a step-down in the interest rate paid when overperforming against Uruguay's unconditional NDC targets for reducing the intensity of GHG emissions, as set by the country under the Paris Agreement.**

2. **Building on the model of the US$1.5 billion SSLB issued by Uruguay in October 2022, the mechanism responds to the commitment set out in the WBG Evolution Roadmap[125] to develop approaches for providing concessionality to incentivize countries to address GPGs through the introduction of long-term performance-based incentive mechanisms, including interest buydowns.** The mechanism introduces two innovative features to WBG financing modalities by: a) incorporating an interest buydown provision in the standard WB financing agreement; and b) extending WB capacity to incentivize GPGs outcomes beyond project closing.

3. **Through its leadership of the Development Committee, the Government of Uruguay has made substantial efforts to advance innovative instruments to encourage the provision of GPGs through positive financial incentives and has been a strong supporter of the GPG Fund objectives.** The proposed mechanism introduces several further innovative features in line with the Evolution Roadmap that will: (a) provide financial incentives for overperformance of sequentially ambitious targets, based on commitments set by Uruguay in its NDC under the Paris Agreement; (b) reinforce partnerships between multilateral institutions in supporting the achievement of national environmental goals through robust reporting and credible external verification of climate-related indicators; and (c) focus on providing positive incentives to countries for their provision of GPGs through a step-down only approach.

Approach

4. **This proposed mechanism embeds a KPI related to the reduction in methane intensity of beef production, which is core, relevant and aligned with the country`s sustainability strategies.** It also provides additionality to the SSLB KPIs, which focus on the reduction of aggregate carbon emissions intensity and conservation of native forests at a whole-of-economy level.

5. **The proposed financial mechanism has the following distinct features:**

- it will not include an interest rate increase if KPI targets are not met (which would be the case for the SSLB); instead, interest payments would remain at (or revert to) standard IBRD terms;
- the rate of the interest reduction will be determined such that achievement of the respective KPI targets in each of the ten years of the performance period would lead to a maximum US$12.5 million reduction in the

[125] Evolving the World Bank Group's Mission, Operations, and Resources: A Roadmap. WBG, December 2022

total interest paid over the maturity of the US$350 million loan.[126] As a result, the proposed interest buy-down is expected to exceed the SSLB coupon step-down in bps terms.
- Determination of the interest buy-down will be made annually during the performance period (rather than only once at the mid-point maturity of the SSLB), to incentivize continuous achievement of the KPI targets throughout the maturity of the loan.

Proposed Indicator and Targets

6. **The use of the methane intensity of beef indicator will: (i) highlight the breadth of Uruguay's commitments to climate action by employing a macroeconomically significant KPI beyond the ones used for the SSLB; and (ii) strengthen the case for use of concessional resources from the GPG Fund, by providing additionality beyond the expected impact of the SSLB.** Taken together, the KPIs embedded in both sustainable finance instruments demonstrate Uruguay's determination to pursue a sustainable development path that combines higher growth and productivity in the beef sector with its commitment to zero deforestation. Uruguay's ongoing Livestock and Climate pilot project ("*Ganadería y Clima"*)[127] has worked with farmers to generate innovative proof-of-concept solutions for improved livestock management practices that reduce the methane emission intensity per unit of live weight of beef produced and increase productivity, supporting achievement of the ambitious targets of the proposed interest buy-down. It also builds on the WB's engagement in the livestock sector over the years through lending operations such as the ongoing Uruguay Agro-Ecological and Climate Resilient Systems project (P176232).

7. **The KPI is established as a measure for action on climate mitigation in Uruguay's NDC 1 (2017) and NDC 2 (2022), with increasing levels of ambition.** The targets for this KPI will reflect Uruguay's NDC commitments as follows:

- **KPI**: reduce the intensity of emissions of methane per unit of product (live weight beef) with respect to the reference value for the observation year 1990.[128]
- **Achievement of targets during the 2028-2032 performance period**: interest buydown would apply if the target of 33 percent or more reduction in the intensity of methane emissions per unit of product (live weight beef) with respect to the reference period is met. This is a more ambitious reduction effort than the unconditional target of the NDC 1 (32 percent, to be met by 2025), which has become even more challenging given the headwinds in meeting this target as a result of the recent drought (the most severe in one hundred years). Given the lags associated with the calculation, estimation and verification of this indicator, years 1-5 of the performance period will span from 2028 to 2032, referring to observation years 2025-2029.
- **Achievement of targets during the 2033-2037 performance period**: a higher level of interest rate buydown will apply in these years if the reduction is 36 percent or more, reflecting the higher level of ambition established under NDC 2, which sets an unconditional target of 35 percent to be met by 2030. The lower level

[126] Noting that the WB and the Government of Uruguay have agreed to consider the possibility of applying for additional financing for the buydown as an incentive for early achievement of the KPI targets if new financing becomes available from one or more countries from Annex I of the United Nations Framework Convention on Climate Change.
127 "*Ganadería y Clima"* is a pilot project with funding of US$1.2 million from a partnership between the UNEP-convened Climate and Clean Air Coalition (CCAC), GEF, FAO, and Ministry of Livestock, Agriculture and Fisheries.
[128] The reference value is calculated as the average of the intensity of emissions of methane per unit of product (live weight beef) over the period 1987 to 1991, excluding the maximum and minimum intensity values (i.e., the truncated average of three annual values).

of interest buydown corresponding to the first performance period will apply in these years if the reduction is below 36 percent, but at or above 33 percent. Given the lags associated with the calculation, estimation and verification of this indicator, years 6-10 of the performance period will span from 2033 to 2037, referring to observation years 2030-2034.

- **Buffer year 2038**: If a target is missed in an earlier year, the foregone nominal amount in terms of interest payment reduction may be applied if the same target is achieved in this buffer year, subject to (i) the interest payment in any given year cannot become negative, and (ii) the total amount of the buydown may not exceed US$12.5 million.[129] This flexibility will only apply for a single year of the overall performance period in which a target is missed.
- **Latest official value**: 28 percent reduction (corresponding to 2018). The next official values (corresponding to 2019 and 2020) are expected to become available by May 2024.
- **Calculation of the indicator and frequency**: annual, with truncated five-year rolling average data, reported and externally verified two and a half years after the corresponding observation date. For the calculation of the KPI value, and its assessment compared to the respective targets, the result of the formula is rounded up or down to the nearest integer, consistent with the way the numerical goals were set under Uruguay's NDC 1 and NDC 2, as well as the SSLB Framework.

KPI Methodology

8. **The methodology used to calculate the performance against the KPI will be the same as that employed by Uruguay to report NDC progress data to the United Nations and will be consistent with the SSLB Framework.** The KPI calculates the intensity of methane emissions from the non-dairy livestock sector per unit of live weight beef product (as set out in the 2017 NDC). The estimate of emissions will apply the IPCC 2006 Guidelines[130], or subsequent versions or refinements as agreed by the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement (CMA), and nationally appropriate methods consistent with that guidance.

Reporting, Verification and Application of Interest Reduction

9. **The reporting process will be enhanced to go beyond Uruguay's requirements under the Paris Agreement.** Reporting of methane emissions from the non-dairy livestock sector will move from biennial to annual frequency with a one-year lag, in line with the standards of most developed economies. Retention by the Bank of an independent agency for verification of the proposed mechanism will build on the reporting procedures established for the SSLB, for which the United Nations Development Programme has been contracted to provide verification services, with the first verification report issued in May 2023.

10. **The proposed mechanism will utilize the sectoral cattle methane emissions data verified annually as part of the GHG emissions intensity KPI of the SSLB, combined with verified data on annual beef production data to calculate the methane emissions intensity per unit of live weight beef.** The methane emissions data is calculated as a truncated five-year rolling average to smooth inter-annual (primarily weather-based) variation, with the average for the observation year incorporating data from the three preceding years and the following

[129] Noting that the WB and the Government of Uruguay have agreed to consider the possibility of applying for additional financing for the buydown as an incentive for early achievement of the KPI targets if new financing becomes available from one or more countries from Annex I of the United Nations Framework Convention on Climate Change.
[130] 2006 IPCC Guidelines for National GHG Inventories.

year, with the maximum and minimum values excluded, and the result of the formula rounded up or down to the nearest integer.[131] Allowing for an additional year and five months to report and verify the data, the statistic at the start of the performance period in 2028 will relate to 2025, while the statistic at the end of the performance period in 2037 will relate to 2034. In the buffer year, the statistic for the KPI verified in 2038 will relate to 2035.

11. **An Annual Verification Report will be provided annually no later than May 31st of the subsequent year to the one following the relevant reporting year for the KPI.** It will provide the KPI levels at the observation year against the KPI target, with updated information on the performance of the selected KPI, including baselines. It will also contain additional quantitative and/or qualitative information to facilitate monitoring of progress towards targets. For purposes of verifying achievement of the KPI targets, the Borrower shall provide to the Bank and the Independent Verification Agency the information, data, and other evidence supporting the achievement of the KPI Targets at least five months prior to each KPI Target Verification Date.

12. **The biannual loan repayment dates will be selected by the Borrower such that the first is at least 120 days after the annual deadline for receipt of the Annual Verification Report, and the second is six months later.** The annual deadline for WB operational review of the Annual Verification Report will be 90 days before the first biannual loan repayment date, and the annual deadline for review by WB Finance and Accounting staff will be 60 days before the first biannual loan repayment date. Over the ten-year performance period of the IBRD loan repayment, adequate provision will be made for operational and WB Finance and Accounting staff to review the Annual Verification Report and issue repayment invoices.

Performance Period and Lending Rate Reduction

13. **The proposed mechanism will provide for annually determined performance-based interest buydowns over ten years from 2028-2037.** Over this period, data for the KPI will relate to the years 2025-2034.

14. **The buydown will be implemented through two levels of lending rate reduction corresponding to the lower and higher KPI targets.** Reductions will be applied to the two semesters following annual achievement of the KPI targets. The levels of lending rate reduction will be determined such that achievement of the lower KPI target in years 1 to 5 of the performance period (with a lower level of lending rate reduction), followed by achievement of the higher target in years 6 to 10 (with a higher level of lending rate reduction), will lead to a maximum US$12.5 million reduction in the total interest paid over the life of the US$350 million IBRD loan.[132] If over the period 2033-37 the higher target for a KPI is not achieved but the lower target is reached, the lower rate of buydown will be applied. It should be noted that the amount of the buy-down in any given period cannot exceed the amount of the interest payment (i.e., a negative interest rate will not be possible), there will be no reduction of the loan principal, and the total value of the interest buydown cannot exceed a maximum of US$12.5 million.[133]

Built-in Incentives for Early Achievement and One-off Flexibility for Missed Target

[131] For example, the observation corresponding to year 2025 (NDC 1 target year), is calculated as the truncated (i.e., excluding min and max) average of years 2022, 2023, 2024, 2025 and 2026. Thus, this observation will be calculated in 2027 (when the 2026 data is reported with a one-year lag) and verified by May 2028 (that is, five months after the observation is officially calculated).
[132] Noting that the WB and the Government of Uruguay have agreed to consider the possibility of applying for additional financing for the buydown as an incentive for early achievement of the KPI targets if new financing becomes available from one or more countries from Annex I of the United Nations Framework Convention on Climate Change.
[133] Ibid.

15. **To incentivize early achievement of the higher target, the higher level of buydown will be made available a year ahead of the NDC 2 target date (i.e., in 2032, corresponding to data for 2029), with corresponding reductions in the buydown amount available for the final two years of the performance period.** Certain flexibility will be provided such that if a KPI target is missed during the performance period, at the request of the Government of Uruguay the nominal value of the foregone interest buydown amount for a single year in which a KPI target is missed may be applied as a reduction of interest in year 11 of the repayment period, provided the missed KPI target is achieved in that year. If no target is missed in previous years, the interest payment in year 11 will revert to standard IBRD terms (see Table A5).

Table A5: KPI Targets, Observation, Reporting and Verification Years

Perf. Year	Verifn. Year	Rpt. Year	Obs. Year	Higher Target (%)	Lower Target (%)
1	2028	2027	2025	-	33
2	2029	2028	2026	-	33
3	2030	2029	2027	-	33
4	2031	2030	2028	-	33
5	2032	2031	2029	-	33
6	2033	2032	2030	36	33
7	2034	2033	2031	36	33
8	2035	2034	2032	36	33
9	2036	2035	2033	36	33
10	2037	2036	2034	36	33
Buffer:					
11	2038	2037	2035	36	33