

**PROGRAM INFORMATION DOCUMENT (PID)
APPRAISAL STAGE**

August 10, 2015
Report No.: 99164

Operation Name	Social Inclusion For Shared Prosperity Development Policy Loan
Region	Latin America And Caribbean
Country	Chile
Sector	Central Government Administration (43%), Public Administration – Other social services (36%), Tertiary education (21%)
Operation ID	P154213
Lending Instrument	Development Policy Lending
Borrower(s)	Republic Of Chile
Implementing Agency	Ministry of Finance Ministerio de Hacienda Teatinos 120 Santiago Chile Tel: +56 2 2828 2000
Date PID Prepared	August 10, 2015
Estimated Date of Appraisal	August 31, 2015
Estimated Date of Board Approval	November 6, 2015
Corporate Review Decision	Following the corporate review, the decision was taken to proceed with the preparation of the operation.

I. Country and Sector Background

Chile’s strong economic performance supplemented with high social spending has contributed to significant poverty reduction and shared prosperity over the past two decades. Since 1990s, Chile has sustained high economic growth rates and increased social spending primarily on those at the bottom of the income distribution. Chile also continues to consolidate its position as one of LAC’s strongest performers, with stable economic growth, low inflation, and decreasing unemployment.

Even though Chile performed exceptionally well in reducing poverty and increasing the size of the middle class, income inequality has seen only modest declines. The country’s high level of inequality is one of the Government’s main concerns. Low inter-generational mobility and limited opportunities for vulnerable groups to participate in productive activities are seen as important constraints to reducing inequality. Parents’ education and occupation are the circumstances that explain most of the inequality in access to quality education.

The Government of Chile has defined a comprehensive program of reforms in education, fiscal policy and social protection that aim to enhance equity and social inclusion. The 2014-

2018 Government Program “*Chile de Todos*” emphasizes the importance of reducing inequality and implementing reforms to support a more integrated society with equal opportunities for all. To fulfill the objectives of equity and social inclusion, the Government is introducing wide ranging policy reforms, which include a broad educational reform to expand opportunities for poor, vulnerable and middle class youth in all levels of education, a determined fiscal reform to increase tax collection and improve progressiveness of the system, and social protection reforms to ensure that vulnerable populations do not fall back into poverty and to strengthen poverty measurement to better track the inclusiveness of growth.

II. Operation Objective(s)

In line with priorities set by the Government, this Social Inclusion for Shared Prosperity Development Policy Loan would support the implementation of reforms under three main pillars, as follows: Pillar 1. Promoting Equal Opportunities in Education; Pillar 2. Improving the Conditions to Enhance the Quality of Tertiary Education, and, Pillar 3. Strengthening Institutions for Poverty Measurement and Enhancing Targeting Mechanisms of Social Programs. The Program Development Objective of the DPL is to: (i) promote equal opportunities in education; (ii) improve the conditions to enhance the quality of tertiary education; and (iii) strengthen institutions for poverty measurement and enhancing targeting mechanisms of social programs.

Despite Chile’s substantial upward income mobility and progress in poverty reduction, challenges remain in terms of persistently high inequality, low inter-generational mobility and limited opportunities for vulnerable groups to participate in productive activities. Chile’s Gini Index is much higher than that of the now developed economies when their GDP per capita was at the level of Chile’s today. Persistently high levels of income inequality are a matter for concern, given that they limit the effects of economic growth on poverty reduction. Although Chile registers excellent coverage in primary and secondary education, enrollment rates are considerably lower in tertiary education, particularly for young adults that belong to the lower socioeconomic groups. Also, Chile’s share of unattached youth – those who are neither working nor in school (*ninis*) – remain a sizeable group of the population, contributing to the inter-generational persistence of inequality.

The program of reforms supported by the proposed DPL addresses these challenges:

Pillar 1. Promoting Equal Opportunities in Education

The Government of Chile aims to improve access and quality of education to improve social integration in the education system. As a first step, the Government has passed the Inclusion Law that will gradually regulate the admission process to public schools, eliminate shared funding and prohibit profits in educational institutions that receive state contributions. The Government has also created the Program for Effective Access to Higher Education to support low income students transition from high school to college and thus provide them greater opportunities and possibilities for their future development. For tertiary education, the Government has expanded scholarships for students from the seven lowest income deciles who attend tertiary education.

Pillar 2. Improving the Conditions to Enhance the Quality of Tertiary Education

The Government aims to improve the conditions to enhance the quality tertiary education. As part of a comprehensive reform for tertiary education, the Government has increased resources to state universities, particularly for institutional strengthening, research and innovation, teacher development and strengthening links with the labor market. By doing so it aims to improve the quality of public education and thus increase the availability of a skilled workforce.

Pillar 3. Strengthening Institutions for Poverty Measurement and Enhancing Targeting Mechanisms of Social Programs

The Government, in line with international best practices, has released and implemented a revised official methodology for measuring monetary poverty and has introduced a new multidimensional poverty index to enhance the monitoring of poverty and inequality and thus inform the design of social policy. The design and introduction of this new methodology and index is the result of an important effort of many academic and international organizations including the Foundation for Poverty Alleviation (*Fundación para la Superación de la Pobreza*), the Economic Commission for Latin America and the Caribbean, and the Oxford Poverty and Human Development Initiative, among others. The Government also aims to improve targeting for social programs through the design of a new allocation model for benefits and social services; the Social Protection Card Sheet System (*Ficha de Protección Social*) will be replaced with the System for Support of Social Selection (*Sistema de Apoyo a la Selección Social*).

Equity-driven policies, such as the ones supported by this DPL, are expected to enhance the country's capacity to grow in a sustained and inclusive manner. It is fundamental to expand educational opportunities to increase productive participation, particularly of those in the bottom of the income distribution and other typically excluded groups, to unlock their inherent economic potential by means of higher productivity, thus spurring on growth. Similarly, by improving the monetary poverty measurement methodology, introducing a multidimensional poverty measure and improving the quality of information and the methods used for targeting social policies the Government will be in a much better position to identify potential beneficiaries and help them improve their productive opportunities through an adequate set of programs tailored to their specific needs.

III. Rationale for Bank Involvement

This DPL supports and recognizes specific reforms to promote equity and social inclusion in Chile. The proposed single-tranche operation supports an initial round of policy actions mostly related to the ongoing education reform and to a lesser extent to policies related to strengthening institutions for poverty measurement and targeting of social programs. The considerable focus on education is due mainly to the current timing and sequencing of reforms in Chile. In addition, most of the actions included in the operation have close links with past and current World Bank-supported knowledge services and technical assistance.

The proposed operation has been requested by the Government of Chile and underscores the Government's interest in consolidating and expanding World Bank Group collaboration to strengthen equity and eradicate extreme poverty. The supported program is

consistent with the FY11-FY16 Chile Country Partnership Strategy (CPS) Report No. 57989-CL, which was discussed by the Board of Executive Directors on February 15, 2011, in particular with the pillar of job creation and improving equity. The proposed operation is also consistent with the Government's development strategy, specifically with the education reform.

IV. Tentative financing

Source:		(\$m.)
Borrower		
International Bank for Reconstruction and Development		\$100m
Borrower/Recipient		
IBRD		
Others (specify)		
	Total	\$100m

V. Institutional and Implementation Arrangements

The preparation of this operation is being led by the Budget Office (DIPRES), with participation from the Ministry of Education and the Ministry of Social Development. These agencies will be responsible for the operation's overall implementation, and for reporting on its progress. In addition, the World Bank is designing a Joint Study Program with the Ministry of Education and with the support of international academics, to perform a detailed four-year evaluation of the Inclusion Law. This plan will include laying out the different studies that can help develop and improve its implementation as well as to leverage the gradual implementation to learn from each step of the reform. The World Bank will monitor the selected actions of the Government's program through semiannual implementation status and results reports.

VI. Risks and Risk Mitigation

This DPL is subject to risks related to political and governance, sector strategies, policies and stakeholders, and implementation risks. There is some degree of political opposition to the overall Education Reform. Even though, the gradual implementation of the Inclusion Law has mitigated initial concerns from the opposition, political risk to achieve the objectives of this operation is considered Moderate. With respect to the Inclusion Law, the potential closing of subsidized private schools due to the elimination of profits in the provision of primary and secondary education may have negative impacts on students currently attending those schools, as they may have to migrate to other available schooling opportunities. According to experts, this risk may be mitigated by the absorption of these students by public schools which are currently under-capacity. Moreover, supply side interventions also supported by the education reform that aim to improve the quality of public education and are expected to raise the student performance in public schools, such as better teaching careers, will function as another potential mitigation mechanism. The effective implementation of the Inclusion Law, especially with regard to the new admission process, is another potential risk. Gradual implementation of this reform and an adequate monitoring and evaluation framework will mitigate some of these risks.

The Ministry of Social Development (MDS) has in-house capacity to design and implement the new system for selecting beneficiaries of social programs. However, MDS may face challenges in the implementation of the system, which requires it to play a large coordination role to ensure the appropriate institutions provide timely information to the system and that institutions utilize the new system to allocate benefits of social programs.

Taking into account the risks presented and discussed above, along with the associated mitigation measures, the overall risk of this operation is low. On balance, the potential risks of the operation are offset by the expected benefits.

VII. Poverty and Social Impacts and Environment Aspects

The Government policies supported in this DPL are expected to have a positive poverty and social impact. Previous evidence and prospective analysis show that there are reasons to expect a positive impact from most of the reforms supported with regard to the operation's key objective: to promote equity and social inclusion in Chile. The reforms included in the Inclusion Law are expected to increase equity in the distribution of educational quality across socioeconomic groups. Specifically, policies for primary and secondary education that support a regulated admission system, gradually eliminate copayments and prohibit profits in educational institutions that receive public contributions are expected to have a positive poverty and social impact by increasing the share of students with the expected years of schooling for their corresponding age and expanding the opportunities to access quality education for students in the bottom 40 percent of the income distribution. The main unknown in the process of implementation of the Inclusion Law is whether the reform will significantly increase the demand for non-subsidized private education. There is a gap in the literature as many studies have focused on the voucher reform *per se* and do not consider in depth the potential differences between for-profit, non-profit and municipal schools. Existing evidence shows that for-profit schools in Chile tend to reduce costs on staff by shortening the school day, hiring less experienced and younger teachers and in middle schools hiring teachers without a specialty.¹ However, further research is needed to establish the impacts of such behaviors on quality.

It is also expected that increasing the coverage of the Preferential School Subsidy (targeted vouchers) will diminish schools' local market power and raise competition in poor neighborhoods inducing increases in quality. Similarly, the expansion of scholarships in tertiary education and the implementation of policies that support the Effective Access to Higher Education Program are expected to increase completion of tertiary education which is associated with higher returns. Prior Actions regarding the strengthening of institutions for poverty measurement are expected to help identify vulnerable populations and to feed back into the redesign and evaluation of social policies. Finally, through the new System for Support of Social Selection the Government aims to move away from a system that only targets the poor, to a more inclusive one that aims at broader eligibility, excluding only the highest income deciles.

None of the policies supported by the proposed DPL are expected to have adverse effects on the environment. The DPL does not support actions linked to the construction or rehabilitation

¹ Levin (2001); Elacqua, Martinez and Santos (2011).

of schools, or other civil works that would likely impact the environment. No effect is expected on forests and other natural resources.

VIII. Contact point

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