Document of
The World Bank

Report No: ICR0000489

IMPLEMENTATION COMPLETION AND RESULTS REPORT
(IBRD-71640)
(Loan/Credit No. P078726)

ON A

STRUCTURAL ADJUSTMENT LOAN

IN THE AMOUNT OF US$151.52 MILLION

TO

THE ORIENTAL REPUBLIC OF URUGUAY

FOR A

PUBLIC SERVICES AND SOCIAL SECTORS STRUCTURAL ADJUSTMENT LOAN

December 19, 2007

Sustainable Development Department
Argentina, Chile, Paraguay, Uruguay Country Management Unit
Latin America and the Caribbean Region

CURRENCY EQUIVALENTS

(Exchange Rate Effective September 30, 2007)

Currency Unit = Peso Uruguayo
US$ 1.0 = 23.12

FISCAL YEAR
January 1 – December 31

ABBREVIATIONS AND ACRONYMS

ADME	Electric Market Administration *(Administración del Mercado Eléctrico)*
AFE	National Railway Administration *(Administración de Ferrocarriles del Estado)*
ANC	National Post Office Administration *(Administración Nacional de Correos)*
ANCAP	Fuel, Alcohol, and Portland Administration *(Administración Nacional de Combustibles, Alcohol y Portland)*
ANCEL	ANTEL's subsidiary for cellular telephones
ANTEL	National Telecommunication Administration *(Administración Nacional de Telecomunicaciones)*
ANP	National Ports Administration *(Administración Nacional de Puertos)*
BROU	Bank of the Oriental Republic of Uruguay *(Banco República Oriental del Uruguay)*
CAS	Country Assistance Strategy
CCC	Grants Control Commission *(Comisión de Control de la Concesión)*
CPI	Consumer Price Index
CREMA	Contract for Rehabilitation and Maintenance
GDP	Gross Domestic Product
GOU	Government of Uruguay
IADB	Inter-American Development Bank
ILD	International Long Distance
IMF	International Monetary Fund
INE	National Statistic Institute *(Instituto Nacional de Estadística*
IPC	Consumer Price Index *(Índice de Precios al Consumidor)*
IVA	Sales Tax *(Impuesto al Valor Agregado)*
LPG	Liquid Propane Gas
MDGs	Millennium Development Goals
MEF	Ministry of Economy and Finance *(Ministerio de Economía y Finanzas)*
MIEM	Ministry of Industry, Energy and Mines *(Ministerio de Industria, Energía y Minas)*
MTOP	Ministry of Transport and Public Works *(Ministerio de Transporte y Obras Públicas)*
MVOTMA	Ministry of Housing, Territorial Development, and Environment *(Ministerio de Vivienda, Ordenamiento Territorial y Medio Ambiente)*
NLD	National Long Distance

OECD	Organization for Economic Cooperation and Development
OPP	Budget and Planning Office *(Oficina Planeamiento y Presupuesto)*
OSE	Estate Sanitary Works *(Obras Sanitarias del Estado)*
PSP	Private Sector Participation
SAL	Structural Adjustment Loan
SSAL	Special Structural Adjustment Loan
TAL	Technical Assistance Loan
TEU	Twenty-foot Equivalent Unit
UFW	Unaccounted-for-water
URAGUA	Private Water Concessionaire in the Department of Maldonado
UREE	Electric Energy Regulatory Unit *(Unidad Reguladora de Energía Eléctrica)*
URSEA	Energy and Water Regulatory Unit *(Unidad Reguladora de los Servicios de Energía y Agua)*
URSEC	Communication Services Regulatory Unit *(Unidad Reguladora de los Servicios de Comunicaciones)*
USO	Universal Service Obligation
UTE	Electric Transmission Factories National Administration *(Administración Nacional de Usinas y Transmisiones Eléctricas)*
VAT	Value Added Tax

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URUGUAY
Public Services and Social Sectors Structural Adjustment Loan

CONTENTS

A. Basic Information

Country:	Uruguay	Program Name:	Uruguay Public Services & Social Sectors SAL
Program ID:	P078726	L/C/TF Number(s):	IBRD-71640
ICR Date:	12/19/2007	ICR Type:	Core ICR
Lending Instrument:	SAL	Borrower:	THE GOVERNMENT OF URUGUAY
Original Total Commitment:	USD 151.5M	Disbursed Amount:	USD 91.5M

Implementing Agencies:
Office of Planning and Budget (OPP)
Ministry of Economy and Finances (MEF)

Cofinanciers and Other External Partners:

B. Key Dates

Process	Date	Process	Original Date	Revised / Actual Date(s)
Concept Review:	09/12/2002	Effectiveness:	04/22/2003	04/22/2003
Appraisal:	11/07/2002	Restructuring(s):		12/28/2006
Approval:	04/08/2003	Mid-term Review:		
		Closing:	12/31/2004	01/31/2007

C. Ratings Summary

C.1 Performance Rating by ICR

Outcomes:	Moderately Unsatisfactory
Risk to Development Outcome:	Moderate
Bank Performance:	Moderately Satisfactory
Borrower Performance:	Moderately Satisfactory

C.2 Detailed Ratings of Bank and Borrower Performance (by ICR)

Bank	Ratings	Borrower	Ratings
Quality at Entry:	Moderately Unsatisfactory	Government:	Moderately Satisfactory
Quality of Supervision:	Satisfactory	Implementing Agency/Agencies:	Satisfactory
Overall Bank Performance:	Moderately Satisfactory	**Overall Borrower Performance:**	Moderately Satisfactory

C.3 Quality at Entry and Implementation Performance Indicators			
Implementation Performance	**Indicators**	**QAG Assessments (if any)**	**Rating:**
Potential Problem Program at any time (Yes/No):	No	Quality at Entry (QEA):	None
Problem Program at any time (Yes/No):	No	Quality of Supervision (QSA):	None
DO rating before Closing/Inactive status:	Satisfactory		

D. Sector and Theme Codes		
	Original	**Actual**
Sector Code (as % of total Bank financing)		
General energy sector	25	25
General information and communications sector	25	25
General transportation sector	25	25
General water, sanitation and flood protection sector	25	25
Theme Code (Primary/Secondary)		
Infrastructure services for private sector development	Primary	Primary
Legal institutions for a market economy	Primary	Primary
Regulation and competition policy	Primary	Primary

E. Bank Staff		
Positions	**At ICR**	**At Approval**
Vice President:	Pamela Cox	David de Ferranti
Country Director:	Pedro Alba	Axel van Trotsenburg
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F. Results Framework Analysis

Program Development Objectives (from Project Appraisal Document)

The loan (along with loan 7165-UR) supports reforms to boost economic growth, improve the competitiveness of the Uruguayan economy, and improve the general welfare of the population through better provision of public and social services and infrastructure.

Specifically, this loan aims to reduce prices, increase quality and coverage, and improve efficiency of investment, production and distribution of services, and infrastructure through: (i) upgrading regulation by strengthening regulatory frameworks in all sectors; (ii) increasing competition by liberalization in the wholesale power market and mobile phone services and sector restructuring of the petroleum, water and sanitation and transport sectors; (iii) improve the efficiency of public expenditure by increasing transparency and accountability and by reducing tax distortions; and (iv) strengthening institutions to carry out functions of regulation, market oversight, sector planning and management.

Revised Program Development Objectives (if any, as approved by original approving authority)

(a) PDO Indicator(s)

Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
Indicator 1 :	Public services effectively regulated.			
Value (quantitative or Qualitative)	Regulatory agencies were established in 1997 for power; in 2001 for communications; and in 2002 for energy & water.	Energy (power, natural gas & petroleum products) and communications (telecommunications & postal services) effectively regulated.		Met
Date achieved	04/08/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 2 :	Real prices reduced; quality & coverage increased; and the efficiency of investment, production & distribution of services and infrastructure improved.			
Value (quantitative or Qualitative)	December 31, 2002 figures as measured in the utilities databases.	Statistically significant improvement or reduction in prices, quality, coverage and efficiency of public services & infrastructure.		Met (see section 3.2 of this ICR).
Date achieved	04/08/2003	12/31/2005		12/04/2006

Comments (incl. % achievement)				
Indicator 3 :	Explicit and participatory national energy and communications policies established, and regulators with adequate capacity to properly carry out their responsibilities and functions.			
Value (quantitative or Qualitative)	Lack of an explicit and participatory national policy in energy and communications.	Energy and communication sector policies approved and widely disseminated.		Met. Guidelines for an Energy Strategy issued & published by MIEM on 18 Aug. 2006. MIEM made responsible for telecom. URSEA & URSEC consolidated.
Date achieved	04/08/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				

(b) Intermediate Outcome Indicator(s)

Indicator	Baseline Value	Original Target Values (from approval documents)	Formally Revised Target Values	Actual Value Achieved at Completion or Target Years
Indicator 1 :	URSEA organization structure defined and staff appointed.			
Value (quantitative or Qualitative)	URSEA recently established and poorly staffed, lacks definitive organization & structure and financial autonomy.	A fully operational URSEA regulating all energy (power, natural gas & petroleum products) and WSS sectors.		Met.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 2 :	Regulatory accounting guidelines issued and approved.			
Value (quantitative or Qualitative)	Lack of regulatory accounting in all public services.	Measure implemented.		Partially met. Study on power ready, on WSS being updated and underway on gas.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				

Indicator 3 :	Performance indicators for energy & communication sectors set, defined, and protocols for their estimation and publication agreed.			
Value (quantitative or Qualitative)	Absence of periodic public information on utilities' performance and service quality.	Measure implemented.		URSEA & URSEC publishing selected information in their websites.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 4 :	First round of quality of service inspections by URSEA completed.			
Value (quantitative or Qualitative)	None	Measure implemented.		Met.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 5 :	Performance review of regulatory framework completed and adjustment proposal made considering the new National Energy Policy.			
Value (quantitative or Qualitative)	N/A	Measure implemented.		Underway.
Date achieved	04/28/2003	12/31/2005		12/16/2005
Comments (incl. % achievement)				
Indicator 6 :	New law defining specific regulatory framework for downstream petroleum products approved by Congress.			
Value (quantitative or Qualitative)	Most regulations and norms included in the ANCAP law.	Measure implemented.		Met. On 2003 GoU issued the Decree 556 establishing a distribution policy for petroleum products. On 2004, URSEA regulated LPG provision and security of facilities & equipments.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 7 :	Definition of an import parity pricing formula for petroleum products and removal of ANCAP regulatory and licensing responsibilities approved.			
Value (quantitative or Qualitative)	None	Measure implemented.		Met. The formula was published in Dec. 2004 by URSEA.

Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 8 :	System for monitoring postal sector performance including quality of service, mail volumes and delivery coverage implemented.			
Value (quantitative or Qualitative)	None	Measure implemented.		Met. Parameters & monitoring indicators defined in study supporting a proposed regulatory framework.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 9 :	Legal and regulatory framework approved for the transport sector.			
Value (quantitative or Qualitative)	Partial subsector regulation of different quality level, not fully consistent.	Measure implemented.		Partially met.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 10 :	ANCAP port and warehouse facilities effectively open to third parties.			
Value (quantitative or Qualitative)	Restricted access.	Measure implemented.		None. Action stop after the ANCAP Law was repealed.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 11 :	New signaling scheme, customer data base administrator, and numbering plan approved.			
Value (quantitative or Qualitative)	None	Measure implemented.		Met. Signaling scheme and numbering plan approved and implemented; and database administrator approved.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				

Indicator 12 :	Commercial cadastre updated and initial package of goods and works for UFW reduction under a risk-based contract under implementation.			
Value (quantitative or Qualitative)	Outdated commercial cadastre and absence of risk-based practices in operations.	Measure implemented.		Commercial cadastre to be updated in 2007 and risk-based contract made unconstitutional by 2004 referenda.
Date achieved	04/28/2003	12/31/2005		12/16/2005
Comments (incl. % achievement)				
Indicator 13 :	Compliance with maintenance and rehabilitation plan and transport sectoral allocation of budget.			
Value (quantitative or Qualitative)	Best practice maintenance & rehabilitation.	Measure implemented.		Met.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 14 :	ADME's managers & staff for dispatch & financial transactions appointed, assets & equipment transferred, and manual of procedures completed & published.			
Value (quantitative or Qualitative)	ADME recently created & still non-operational.	Measure implemented.		Partially met. Managers & staff appointed, organizational structure implemented and operational manual approved, but operational concept under revision.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 15 :	URSEA to have established a Petroleum products unit, defined its functions and hired its staff.			
Value (quantitative or Qualitative)	Petroleum products unit does not exist.	Measure implemented.		Pending.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 16 :	Sector policy and updating of legal and regulatory framework approved in the			

	telecommunications sector.			
Value (quantitative or Qualitative)	Absence of clear functions & responsibilities and cabinet representation, and a relatively new regulator.	Measure implemented.		Met.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 17 :	URSEC's administrative and labor structure, and autonomous financing mechanism approved.			
Value (quantitative or Qualitative)	URSEC lacking administrative & labor structure and autonomous financing.	Measure implemented		Met.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 18 :	Satisfactory implementation of financing mechanism for URSEC.			
Value (quantitative or Qualitative)	Absence of appropriate financing for URSEC.	Measure implemented.		Met. Appropriate mechanism (regulation fee) approved.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 19 :	Institutional reorganization for AFE, MTOP, and ANP implemented.			
Value (quantitative or Qualitative)	Status quo.	Measure implemented.		Underway.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				
Indicator 20 :	Enactment of specific legislation to facilitate comprehensive insurance for multimodal transport chains.			
Value (quantitative or Qualitative)	None	Measure implemented.		Pending.
Date achieved	04/28/2003	12/31/2005		12/04/2006
Comments (incl. % achievement)				

G. Ratings of Program Performance in ISRs

No.	Date ISR Archived	DO	IP	Actual Disbursements (USD millions)
1	05/28/2003	Highly Satisfactory	Satisfactory	51.52
2	12/02/2003	Satisfactory	Satisfactory	51.52
3	06/03/2004	Satisfactory	Satisfactory	51.52
4	12/01/2004	Satisfactory	Satisfactory	51.52
5	05/03/2005	Satisfactory	Satisfactory	51.52
6	01/26/2006	Satisfactory	Satisfactory	51.52
7	12/14/2006	Satisfactory	Satisfactory	51.52

H. Restructuring (if any)

Restructuring Date(s)	Board Approved PDO Change	ISR Ratings at Restructuring		Amount Disbursed at Restructuring in USD millions	Reason for Restructuring & Key Changes Made
		DO	IP		
12/28/2006	N	S	S	51.52	Significant external and domestic developments and a change of government priorities after the new administration was sworn in early 2005 (see section 1.6 of the ICR). Key changes made are summarized in tables included in section 2.1 of the ICR.

1. Program Context, Development Objectives and Design

1.1 Context at Appraisal

When this operation was appraised in November 2002, Uruguay was still in the throws of a deep economic crisis that was precipitated when neighboring Argentina defaulted on its public debt and devalued its currency to one third of its previous value.

The crisis revealed that, although Uruguay had made considerable progress towards macroeconomic stability during the 1990's, the pace of structural and policy reform had not provided a sufficient cushion to absorb external shocks, nor did it insulate the financial system and the economy at large from regional contagion. The crisis also revealed underlying weaknesses in the economy, including an erosion of competitiveness due to the high cost of public services and infrastructure, inadequate supervision of the banking system, a financial sector made vulnerable by a high proportion of volatile non-resident deposits, a highly dollarized economic system in which many private sector liabilities were denominated in foreign exchange and in which a large part of the public sector debt was also denominated in foreign currency with short- to medium-term repayment peaks.

As a result of the crisis, GDP declined by 11 percent in real terms in 2002 and unemployment rose to some 20 percent. Fiscal revenues were deeply affected by the contraction in GDP. In addition, Uruguay was confronted with widening sovereign debt spreads and with a country risk premium that reached more than 2000 basis points. There was a close to 50 percent reduction in the dollar value of the peso following the adoption of a currency float in June 2002 and bank deposits fell by 50 percent in the course of the year. Liquidity support provided to banks contributed to a sharp fall in international reserves and raised concerns regarding Uruguay's ability to service its external debt and withstand additional pressures on the financial system.

In that context, the international financial community provided an unprecedented US$3.9 billion package of financial support to Uruguay with the aim of stabilizing the situation and providing a basis for sustained economic recovery. As part of the package, the Bank's Board first approved a structural adjustment loan and a special structural adjustment loan for a total of US$300 million in August 2002 that focused on fiscal, financial and social protection reforms. The Public Services and Social Sectors Structural Adjustment Loan (SAL) for an amount of US$151.52 million (covered in the present ICR) and the accompanying Special Structural Adjustment Loan (SSAL) in an amount of US$101.02 million (covered in the SSAL's ICR No. 34536) were approved as follow-up operations to these earlier ones.

The economic crisis in Uruguay and the concerted response from the international community spurred the Bank to prepare this operation within a short time-frame spanning just a few months. It also encouraged the Bank to cooperate closely with the authorities to expedite program implementation and, in the course of project execution, to be flexible and accommodating in seeking a way forward when unforeseen developments threatened to obstruct progress.

1.2 Original Program Development Objectives (PDO) and Key Indicators (as approved)

The Program Document covered the Public Services and Social Sectors SAL as well as the accompanying Special SAL. They were presented to the Board jointly as supportive of a single common program set out in the Government's letter of development policy. The proposed loans shared the common objectives of restoring economic growth, improving the competitiveness of the Uruguayan economy, and improving the general welfare of the population: the SAL through greater efficiency in the provision of public services and infrastructure, and the Special SAL through increasing the impact of public expenditures in the education and health sectors. As described earlier, the SAL and the Special SAL follow up on two earlier World Bank loans approved in August of 2002. The four operations were approved as a part of a concerted effort by multilateral institutions to help Uruguay withstand the impact of strong external shocks and set the stage for recovery of sustained economic growth.

The Public Services and Social Sectors SAL covered in this ICR supported measures in the energy, telecommunications, postal services, water and sanitation and transport sectors aimed to reduce prices, increase quality and coverage, and improve the efficiency of investment, production and distribution of services and infrastructure through: (i) increasing competition by liberalizing the wholesale power market and mobile phone services and restructuring the petroleum, water and sanitation and transport sectors; (ii) upgrading regulation and strengthening regulatory frameworks in all of the above named sectors; and (iii) improving the efficiency of public expenditure by increasing transparency and accountability and by reducing tax distortions.

The specific objectives of the SAL (the loan covered in this ICR) were restoring economic growth, improving the competitiveness of the Uruguayan economy, and improving the general welfare of the population through greater efficiency in the provision of public services and infrastructure. The Program Document also states that the outcomes supported by the SAL were to reduce prices; increase quality and coverage; and improve the efficiency of investment, production and distribution of services and infrastructure in the energy, telecommunications, postal services, water supply and sanitation and transport sectors.

The second loan approved as part of the Program, the Public Services and Social Sectors Special Adjustment Loan (not covered in this ICR) focused on the health and education sectors, and its specific objectives were restoring economic growth by increasing the impact of public expenditures in those two sectors, while maintaining or improving services in key priority areas through: (i) restructuring national health funding instruments; (ii) reducing cross subsidies in the public hospital network; (iii) protecting priority education programs: and (iv) improving the management of the education sector.

The loan agreements for both loans incorporated cross-linkages so that disbursement of the second and third tranches of either loan was contingent upon satisfactory progress with the other. However, as detailed in Section 1.6 below, that cross-linkage fell into abeyance when, in May 2005, the Special SAL was closed and the undisbursed balance was cancelled at the request of the Government. The ICR for the Special SAL loan was completed in February 2006. The achievement of all objectives was satisfactory or highly satisfactory.

According to the latest ICR preparation guidelines dated August 2006, for evaluation purposes, a project's objectives encompass both the PDOs stated in project documents and key associated outcome targets. The guidelines state that whenever the PDOs stated in project documents are broad and/or vaguely worded that they can preclude a meaningful evaluation, intended project objectives are inferred by the evaluator from key associated outcome targets (and/or project design features as relevant).

In the case of the SAL, although its overall and specific objectives and expected outcomes are clearly stated in the Program Document, consistent with Bank practice at the time of preparing the Program, no specific indicators (outcome targets) related to the achievement of PDO were stated in the PD. Instead, key monitoring indicators closely related to the loan covenants and conditionalities were included in the Policy Matrix, and as most of the loan covenants, the monitoring indicators specified explicit outputs. Consequently, success in achieving the PDO is assessed in this ICR through the accomplishments made towards the specific original and revised Loan conditions as stated in the Program Document and the amended Loan Agreement.

More details about the assessment of PDO achievement and evaluation of Program outcomes are provided in sections 3.2 and 3.3.

1.3 Revised PDO (as approved by original approving authority) and Key Indicators, and Reasons/Justification

PDOs were not revised. However, given the change in the reform environment caused by the number of external and domestic developments described in section 1.6 below and in other sections throughout this document, the Loan was restructured in 2006 and the conditionality amended to reflect the new policies and approaches of the Borrower at the time. As discussed in section 3.3, achievement of both original and amended conditions has been considered in this ICR for the purposes of the outcome rating (see section 3.3). The justification for the revised conditionalities can be found in section 1.6 and 2.2 below.

1.4 Original Policy Areas Supported by the Program (as approved)

The loan supported sector reforms in energy (power, natural gas and petroleum products), telecommunications, postal services, water supply and sanitation, and transport (roads, railways, ports and airports) with the objectives of reducing prices, increasing quality and coverage, and improving the efficiency of investment, production and distribution of public services and infrastructure. The reforms aimed to achieve this by: (i) strengthening and consolidating regulation; (ii) improving efficiency and increasing competition; and (iii) upgrading and strengthening the institutional development capacity of Ministries, the OPP and sector agencies.

Specific measures within each of the policy areas were as follows:

Regulatory reform focused on establishing, strengthening and consolidating two multisector regulatory agencies: *Unidad Reguladora de Servicios de Energía y Agua* (URSEA) and *Unidad Reguladora de Servicios de Comunicaciones* (URSEC). The operational transparency of both agencies was to be enhanced with the introduction of regulatory accounting. Accountability was to be enhanced by consolidating and upgrading an information system of utility performance that would be accessible to the public. Appropriate legal and regulatory frameworks were to be established or consolidated for downstream petroleum products, natural gas, water supply and sanitation, and postal services.

Efficiency and Competition focused on rationalizing public sector operations and strengthening the framework for private sector participation (PSP). The accounting framework for public utilities was to be made more transparent by establishing a competitive wholesale market and a spot market in the power sector, by moving toward import parity prices for petroleum products and by increasing competition in the retail distribution of petroleum products, by making the market for mobile telephone services more open to private providers to the market and by fostering competition in international long distance services, by granting a management contract for the Montevideo water supply system, and by awarding the management of Montevideo's international airport, the multipurpose terminal port, and the operation of rail networks to private operators.

Institutional Development focused on bringing coherence to reforms in the energy sector through the development of a national energy policy. High international oil prices and region-wide shortages in energy were a serious setback for Uruguay which is heavily dependent upon imported energy supplies. Hence, the development of a national energy policy that would evaluate options and identify possible new sources of energy had become a priority at the time of appraisal.

1.5 Revised Policy Areas (if applicable)

Not applicable. However, although the three policy areas described above remained the same after the 2006 restructuring, some of the premises on which the priorities and tools were based did change and were consequently acknowledged in the new conditionalities.

1.6 Other significant changes

(in design, scope and scale, implementation arrangements and schedule, and funding allocations)

During the period of 2002-2007 and after the loan became effective on April 22, 2003 and the first tranche of US$51.52 million was released, there were a number of external and domestic developments that changed the environment for reform in the country and resulted in a shift in focus in some policy areas, as well as the relevance of some of the measures envisaged under the SAL.

On the external events side, region-wide constraints in the supply of natural gas and electric power affected the possibility of establishing a regional energy market. On the domestic front, significant changes in the legislation governing the hydrocarbon and water supply and sanitation (WSS) sectors and a change in government in the general election of 2004 modified the environment for private sector participation and increased support for public sector management of public services and infrastructure sectors. While the new Government’s policy focus remained committed to unbundling policy-making, regulation and service provision roles, private sector participation was no longer considered an appropriate tool for achieving greater efficiency in both the WSS and the petroleum products sectors. The change in policy and the massive approval of two referenda restricting private sector participation in those two sectors reflected public opinion’s preference for greater involvement of the public sector. However, private sector participation still remained an option (albeit under modified arrangements) in ports, airports, telecoms and railways.

As a result of these changes, the implementation progress was slower than envisaged and a second tranche could not be released in November 2003 as contemplated in the program document. A third tranche, envisaged for disbursement in June 2004 was likewise delayed. The Bank extended the closing date in order to give the Government time to resolve outstanding issues and move the program forward.

By late 2006 it became clear that, while there had been good progress with many of the public sector-specific reforms supported by the SAL, in a few critical areas the targeted reforms had been forestalled as the environment for reform had significantly changed and affected the relevance and viability of some of these reforms. Section 2.2 provides more details about the major factors affecting implementation. Once it became apparent that the obstacles were unlikely to be overcome in the near term, the government and the Bank reassessed progress with the SAL and took action to adapt and reconcile the program to a changed environment. To reflect the new realities while, at the same time, acknowledging the substantial progress achieved in many areas supported by the SAL, the loan was restructured in December 2006 at the request of the Government.

The restructuring of the SAL acknowledged the significant changes that were made to the legislative framework in key sectors over the course of the 2002-2006 loan period, as well as in the focus of Government’s policies after the 2004 general elections. The loan amount was also reduced from the original US$151.52 million to US$91.52 million. A second tranche in the amount of US$40 million was disbursed on January 25, 2007 at which time the outstanding US$60 million balance of the original loan was cancelled and the loan was closed.

The original conditions for tranche release and the revised second tranche conditions are set out in the policy matrix presented in section 2 below. The state of compliance with each of the tranche release conditions was detailed in a project paper that was attached to a memorandum and recommendation of the president (MOP) and circulated to the Executive Directors on December 15, 2006.[1]

The Special SAL, which had cross-linkages with the SAL, was brought to closure in May 2005. At that time, the government requested that the second and third tranches of the Special SAL be cancelled because Uruguay no longer required financial support on special terms. As stated above, the ICR for the Special SAL concluded that the achievements of all objectives were satisfactory or highly satisfactory. All second and third tranche loan conditions of the Special SAL had been met, except for cross-linkages with the SAL. In June 2005, the Board approved a DPL to continue support for Uruguay's social sector reform program on regular IBRD terms. In view of the early closure of the Special SAL and the cancellation of the second and third tranches, the cross-linkage of the SAL with the Special SAL was superseded and was no longer applicable.

The amendments to the SAL did not change the PDO with respect to sound macroeconomic management, a more competitive economy, fostering price reductions, improvements in quality and coverage, and increasing the efficiency in the provision of public infrastructure and services.

The amendments however recognized that the full achievement of some of the proposed outcomes would take longer to achieve than was originally envisaged. It was also acknowledged that a longer time horizon and new operational modalities may, in turn, increase program risks. The Government and the Bank opted to manage those risks by shifting Bank financial support for the development of public infrastructure and services from policy-based to investment lending instruments and AAA. This change in strategy was consistent with the CAS for FY05-10 which was discussed by the Board on June 9, 2005.

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[1] *"Uruguay Public Services and Social Sectors Structural Adjustment Loan No.71640-UR. Proposed Amendment to the Loan Agreement Concerning Release of the Second Tranche and Cancellation of the Third Tranche"* R2006-0229 dated December 15, 2006.

2. Key Factors Affecting Implementation and Outcomes

2.1 Program Performance

Tranche	Amount	Expected Release Date	Actual Release Date	Release
First Tranche	US$51,520,000	April 2003	April 22, 2003	Regular
Second Tranche	US$50 million reduced to US$40 million after amendment	November 2003	January 25, 2007	US$40 million: Regular US$10 million: Cancelled
Third Tranche	US$50 million	June 2004	NA	Cancelled

The table above shows originally agreed and actually released amounts and expected and actual release dates of each tranche. The tables below are derived from the policy matrix for the different tranches and summarize the performance of the Program. The table is drawn from the Program Document and the Loan Agreement as they were originally presented to the Board, and also includes changes that were introduced when the loan was amended in December 2006.

Status of Compliance with Tranche Release Conditions

Note that maintenance of a satisfactory macroeconomic framework was a general condition applicable to all tranches and is not separately listed below. The condition was met uninterrupted during the entire implementation period.

First Tranche	
A First Tranche in an amount of US$51.52 million was released at effectiveness supporting measures taken prior to Board Presentation	**Status**
Regulatory Reforms	
1. Law creating URSEA, a regulatory agency for water and sanitation, power, gas and petroleum products approved. URSEA Board of Directors appointment and the water private concessions in the Department of Maldonado put under its jurisdiction.	Met
2. Technical norms and regulations for transmission and distribution approved and issued.	Met
3. Law eliminating ANCAP's monopoly and allowing free import of oil and derivatives starting in 2006 approved.	Met
4. Law establishing new natural gas legal and regulatory framework submitted to Congress[2].	Met
5. Water sector law presented to Congress[3].	Met
Efficiency and Competition	
6. Service quality and performance indicators for 2003 and 2002 results for OSE agreed and published in daily newspapers.	Met
7. Decision to undertake a tax reform, including the review of taxes applied to the energy products.	Met
8. Specific norms and regulations for generation and transmission issued in June 2002 and for the wholesale market in August 2002.	Met
9. Government granted ILD licenses to 18 operators and approved interconnection regulation.	Met
10. Government awarded new mobile license.	Met
11. OSE created a special unit to manage unaccounted for water activities.	Met
12. Laws approved in 2002 (i) created "Mega-concession" and allowed further concession in ports and airport management, and selling of stake in former state carrier (Pluna), and (ii) separated AFE rail infrastructure from operations and transferred AFE rail infrastructure to MTOP.	Met
13. Law approved in June 2000 providing open access of private operators to public rail infrastructure.	Met

[2] A draft law was presented to Parliament in 2001 by the former administration but withdrawn by the current government which was concerned that that the draft law did not address the needs of the gas sector and did not reflect its sector policy.

[3] A draft law was presented to Parliament in early 2003 by the former administration. However, the October 2004 referendum rendered unconstitutional a number of key articles invalidating the overall concept of the proposed law.

Second Tranche (Original Conditions)	
A Second Tranche in an amount of US$50 million was originally scheduled for release in November 2003, after full compliance with the conditions included in this table.	**Status**
Regulatory Reforms	
1. MIEM has issued a decree announcing the target tariff for electricity distribution and establishing a convergence path towards the target tariff (consistent with URSEA's recommendation and the benchmarking studies carried out by URSEA).	Not met
2. MIEM has issued a decree establishing the regulatory framework for the importation, production and commercialization of petroleum products.	Met as amended in action 3 of revised tranche 2
3. The Executive has issued a decree establishing the regulatory framework for the Borrower's postal services sub-sector.	Met as amended in action 4 of revised tranche 2
4. The Executive has issued a decree approving two divisions within ANCAP with separate accounts, management and finances for its petroleum business and its port and logistic facilities.	Met as amended in action 5 of revised tranche 2
5. The Borrower has complied with a new natural gas law, which includes provisions to: (a) eliminate legal ambiguities, including with respect to the attributions of the public and private sector; (b) establish a tariff regime; and (c) define right of way issues.	Not met
Efficiency and Competition	
6. The Borrower's Congress has approved and the Executive has promulgated a law establishing the legal and regulatory framework for the water supply and sanitation sector, which includes, inter alia, provisions to shift the authority to carry out feasibility studies and grant concessions from OSE to the Executive.	Not met
7. ADME has approved a first set of PPAs and has requested proposals for three ongoing energy contracts to be replaced by PPAs.	Not met
8. The Executive has approved unit tariffs and URSEA has approved conditions for open access to ANCAP's port, wholesale oil import, and storage facilities.	Not met
9. OSE has offered to award a performance-based contract to a private operator for the management of the UFW reduction program in Montevideo, as evidenced by the public offer issued for the award of the contract.	Not met
10. The Borrower has brought to the point of concession the management of the Carrasco International Airport, as evidenced by the issuance of invitations to bid for the award of the concession.	Met
Institutional Development	
11. The Borrower, through MIEM, has published and complied with a national energy policy which addresses issues relating to: (a) the relative price of fuels; (b) the economics of gas and electricity importation from Argentina and Brazil; (c) the economics and politics of a strategic national reserve of generating capacity; (d) the environmental impact of changes in the country's energy portfolio; (e) the consistency of the new electricity, gas and petroleum regulations with the national energy policy; and (f) the institutional capacity required to implement and monitor a national energy policy.	Met as amended in action 11 of revised tranche 2
12. The Borrower has fulfilled all of the conditions set forth in Schedule 3 to the Special Structural Adjustment Loan Agreement (Loan 7165-UR).	Superseded

Second Tranche (Revised as Amended)	
A revised as amended Second Tranche in an amount of US$40 million was released on January 25, 2007 and US$10 million cancelled. The conditions in this tranche comprise the conditions of the original Second and Third Tranches that were either fully met or met as revised.	**Status**
Regulatory Reform	
1. (a) URSEA has completed the technical work needed for the implementation of regulatory accounting in the power sector; (b) URSEC has begun executing the technical work needed for the implementation of regulatory accounting in the telecommunications sector; and (c) URSEA has begun: (i) updating the technical work needed for implementation of regulatory accounting in the WSS sector; and (ii) executing the technical work needed for implementation of regulatory accounting in the natural gas sector.	Met Met Met
2. (a) URSEA and URSEC have selected the sets of performance indicators that will be reported to them by operators of electricity, WSS (in the case of URSEA) and telecommunication services (in the case of URSEC); and (b) Parliament has approved and the Executive has promulgated laws authorizing URSEA and URSEC to request information from the public and private operators of electricity, natural gas, WSS (in the case of URSEA), and telecommunication services (in the case of URSEC).	Met Met
3. MIEM has issued a decree establishing the regulatory framework for the commercialization of petroleum products.	Met
4. Parliament has approved and the Executive has promulgated a law that includes: (a) the definition of universal postage coverage; and (b) establishment of a postal services fee and a fund that will administer such resources.	Met
Efficiency and Competition	
5. ANCAP has issued a resolution establishing a logistic unit with separate accounts and management and with responsibility for the importation, storage, transport and delivery functions of its petroleum products.	Met
6. The Borrower has brought to the point of concession the management of Carrasco International Airport, as evidenced by the issuance of invitations to bid for the award of the concession.	Met
7. The Borrower has closed the gap between the ex-refinery and the estimated import parity prices of gasoline, gasoil and fuel oil within a range of plus or minus 25 percent, calculated based on a quarterly moving basis.	Met
8. The Borrower has reduced relative distortions in fuel pricing to the extent necessary to be within a range of + or - 20 percent of Brazil and Chile.	Met
9. URSEC has (a) set up an independent telephone numbering management system; (b) adopted a customer database administrator; and (c) defined precise rules for signaling (i.e. identifying the origin and destination of a telephone call).	Met
10.(a) The Borrower has brought to the point of concession the management of the Montevideo Multipurpose terminal (*puerto polivalente*), as evidenced by the issuance of invitations to bid for the award of concession. (b) Parliament has approved and the Executive has promulgated a law authorizing the formation of a public limited company jointly owned by AFE and the Borrower's National Corporation for Development (*Corporación Nacional para el Desarrollo*), a corporation established by the Borrower's Law No. 15785 of December 4, 1985, for the operation of railways in Uruguay.	Met Met
Institutional Development	
11. The Borrower, trough MIEM, has published guidelines for the definition of a national energy strategy to improve energy security in Uruguay at an affordable cost.	Met

Third Tranche (Original Conditions)	
A Third Tranche in an amount of US$50 million was initially scheduled for release in June 2004 and cancelled on January 25, 2007.	**Status**
Regulatory Reform	
1. (a) Private and public utilities under URSEA's and URSEC's jurisdiction have implemented regulatory accounting, as certified by independent auditors.	Met as amended in actions 1 (a), (b) and (c) of revised tranche 2
(b) Private and public utilities under URSEA's and URSEC's jurisdiction have published performance indicators for the fourth quarter of 2003.	Met as amended in actions 2 (a) and (b) of revised tranche 2
2. The Borrower has fully closed the gap between the ex-refinery and the estimated import parity prices of petroleum derivatives.	Met as amended in action 7 of revised tranche 2
Efficiency and Competition	
3. The Borrower has reduced relative price distortions in the structure of fuel taxation, through the enactment of any necessary amendments to existing tax laws, to the extent necessary to reach equilibrium with the major neighboring countries.	Met as amended in action 8 of revised tranche 2
4. First spot transactions for electricity have been completed under the framework of the ADME	Not met
5. URSEC has: (a) set up an independent telephone numbering management system; (b) adopted a customer database administrator; and (c) defined precise rules for signaling (i.e., identifying the origin and destination of a telephone call).	 Met Met Met
6. (a) The Borrower has brought to the point of concession the management of the Montevideo port multipurpose terminal (*puerto polivalente*), as evidenced by the issuance of invitations to bid for the award of the concession. (b) The Borrower has offered to award contracts to private companies to operate in former AFE rail network, as evidenced by the public offer issued for the award of the contracts.	Met Met as amended in action 10 (b) of revised tranche 2
7. The Borrower has fulfilled all of the conditions set forth in Schedule 4 to the Special Structural Adjustment Loan Agreement (Loan 7165-UR)	Superseded

The remaining paragraphs of this section present a summary of the main outputs and measures implemented within the three specific policy areas (see section 1.4) under the agreed revised loan conditions for tranche 2, including the measures imported from the original conditionalities for tranche 3. More detail about the relevance of these outputs as well as progress made against all original conditions and revised for tranches 2 and 3 can be found in Annex 7.

Regulation of public services

As described above, some of the original loan conditions for disbursement of tranches 2 and 3 under this policy area were not fully achieved and had to be revised in 2006. Nonetheless, over the course of the SAL implementation period, regulation was successfully introduced and consolidated in Uruguay, despite the changing political and economic environment within the country and the region. As discussed in section 3, this strengthened regulation seems to have played an important role in helping to achieve the Program Objectives of increased quality and coverage and enhancing the efficiency of services and infrastructure. In some instances, increased regulation has also helped to achieve a reduction in prices. As can be seen in the table above, in addition to the two conditions included in tranche 1, all four amended conditions under this area were met. Specifically:

(i) The unbundling of policy making, regulation and operation functions of public services was completed with the creation URSEC, the regulatory agency for communications and postal services, in February 2001 and URSEA in December 2002 covering both the energy (power, natural gas and petroleum products) and water (water supply and sanitation) sectors. Since then, URSEC and URSEA have become well established entities and started technical work needed for the implementation of regulatory accounting in the telecommunications, power, WSS and natural gas sectors (Action 1 of the revised conditions for release of the second tranche). In the power and WSS sectors, URSEA has completed this work and public utilities are preparing to implement it. In the telecommunication and natural gas sectors, consultant firms completed the technical work and regulators expect to complete the implementation of regulatory accounting in 2007. With the support of the national government, both agencies have continued to improve their performance and their technical and managerial capacities with renewed ownership, interest and dedication. The agencies have been staffed, directors have been appointed, and operational procedures have been defined. Both agencies have begun operations.

(ii) The regulators have selected the sets of performance indicators to be reported to them by operators (Action 2) and publication has progressed significantly in the sectors of electricity, WSS and telecommunications. In the WSS sector, the water utility regularly published data concerning quality of service and complementary performance indicators both in the national press and, since February 21, 2003, on its web page. URSEA has posted water quality indicators on its web page since May 10, 2005. With respect to the power sector, although the selection of indicators had been completed earlier in 2004, the first set to be published was for the period January – June 2006. They relate to the quality of service both in technical and commercial terms. In telecommunications, URSEC has posted on its web page, aggregated performance indicators for fixed and mobile operators since October 2006. The intention is, in the medium term, to publish these indicators operator by operator.

(iii) A regulatory framework for the commercialization of petroleum products was established through a decree (Action 3). A referendum on December 8, 2003 revoked the 2002 law that ended ANCAP's monopoly over the import, export and refining of crude oil as well as the export of petroleum derivatives. The possibility that there may be resistance to privatization had been recognized in the Project Document as a possible risk to the program. Following the referendum, MIEM issued a decree establishing rules for non-discriminatory access to all stages of the commercialization of hydrocarbons, including wholesale and retail distribution, as well as transport and distribution services. The decree introduced limited competition by allowing new distributors and service stations to be independent of ANCAP. Hence, ANCAP no longer has a monopoly on the domestic distribution and sale of petroleum products. Furthermore, in February 2004, URSEA issued two new regulations on LPG. As a result, there was an increase in the number of bids (from 2 to 4) from operators interested in the distribution of 13 Kg LPG cylinders.

(iv) A regulatory framework for the postal sector has not been established by decree, but most of the important sector issues were satisfactorily addressed in Articles 77-79 of the 2005-2009 Budget Law. (Action 4 of the revised conditions for release of the second tranche). Articles 77-79 of the 2005-2009 Budget Law established a framework for URSEC to monitor and regulate the sector. It mandates universal postal coverage, defines the postal services fee and establishes the fund that will administer sector resources. Moreover, a law is a more powerful instrument than a decree and that underscores the importance attached by the government to postal service issues. The Executive has informed the Bank that the approval of the Articles was a first step toward a comprehensive regulatory framework for postal services. Meanwhile, a system has been introduced for monitoring sector performance including the quality of service, the volume of mail and the coverage of delivery services.

Other original loan conditions under the policy area of regulation, such as establishing a target tariff for electricity distribution and a sector law for natural gas were not achieved. Likewise, a sector regulatory framework for WSS has not been established. This is explained by different factors. More significant however is the progress made in these areas through other mechanisms and policies which may have also contributed towards PDO achievement (see Annex 7 for detail).

In the case of the WSS, for example, the Government has begun anew to reorganize the sector (provision of WSS services, urban drainage and water resources management). New institutions have been created, and an extensive dialogue has begun between them. Comprehensive legislation to underpin the legal and regulatory framework for the WSS sector is now under-way. Significant progress has been made in preparing the draft law, which is now expected to be presented to parliament within one to two years.

Efficiency and Competition

One quarter of the original loan conditions under this area were fully met as envisaged in the Program Document. About one half of the conditions were partially achieved and slightly more than one quarter has not been met due to changes in the legal framework and in the regional and national sector contexts. The achieved outputs have contributed to fostering a reduction in prices, an increase in access and consumption, and better quality of services. In particular:

(i) Competition increased considerably in the telecommunications and transport sectors. Eighteen private companies began to provide international long distance services and three new mobile companies began competing with the national company in the mobile phone market. Interconnection regulation, an independent telephone numbering management system, a customer database administrator, and precise rules for identifying the origin and destination of phone calls were approved and implemented (Actions 9a, 9b and 9c of the revised conditions for release of the second tranche). In the transport sector, private operators now manage Montevideo's international airport (Action 6). On July 8, 2003 a contract for the 20-year concession of the Carrasco International Airport was signed between the National Ministry of Defense and the public company "*Puerta del Sur*." Arrangements are under way to improve railway operations by awarding management contracts to private operators and Parliament authorized the creation of the *Corporación Ferroviaria del Uruguay* – CFU (Railway Corporation of Uruguay), as a public company, responsible for the rehabilitation and maintenance of railway infrastructure through a contract with AFE (Action 10b).

(ii) In the energy sector the results are mixed. Despite the limited success in opening access in the petroleum sector and in establishing an effective and competitive wholesale power market, there has been considerable progress in making the accounts of ANCAP more transparent (Action 5), in advancing towards the goal of closing the gap between the ex-refinery prices and the estimated import parity prices of petroleum derivatives (Action 7), and in reducing the discrepancies in the retail price of fuels between Uruguay and neighboring countries. (Action 8). Furthermore, a number of measures have been taken to broaden the sources of energy generation, including aero derivative gas turbines, wind power, biomass and small hydro projects. A transition program will gradually introduce wholesale market regulation and establish standards necessary to facilitate the development of independent generation projects. Recent developments have led the government to reconsider the market structure for power. There is a debate within the public sector as to whether, given the relatively small size of the domestic market, expectations from a broader competition framework may be unrealistic. There is also discussion as to whether the electric power utility should keep a strong vertical structure, in order to compete in a regional market that is dominated by large companies. It has been suggested that, at least for the time being, the function of load dispatching and system operations should not be transferred to ADME because it may weaken UTE. However, the transfer of those functions to ADME is crucial if new players are to be attracted and if competitiveness in the power sector is to be enhanced.

(iii) In the WSS sector, the original condition for OSE to award a performance-based contract to a private operator for the management of unaccounted-for-water (UFW) in Montevideo (Action 9) was not complied with as the Constitutional Amendment of 2005 made it unconstitutional to invite private operators to participate in WSS. However, OSE has made it clear that two of its top priorities are the development and implementation of new strategies for: (i) reducing UFW and increasing water revenues; and (ii) the company's organizational renewal. As described later on this document, the Bank is supporting that endeavor with a recently approved second APL.

Specific obstacles and main achievements in this policy area within each sector and under each of the original and revised loan conditions are discussed in detail in annex 7.

Institutional Development

Over the course of its implementation, the Program significantly impacted economic development through its support in helping to establish and consolidate regulation in all infrastructure sectors; separate sector functions; define sector policy; and restructure the sectors and their entities. The Program's assistance to regulatory reform was discussed above. The unbundling of sector functions has been notable and welcome in the WSS and energy sectors, including the establishment of new policy making institutions. Particular efforts have been made to strengthen DINASA, the new Directorate for Water and Sanitation, and the DNETN, the National Directorate for Energy and Nuclear Technology, notably through the World Bank's Public Services Modernization Technical Assistance Project (TAL).

The SAL directly contributed to the achievement of these results by encouraging and supporting the development and publication of the government's Guidelines for an Energy Strategy, as described below. In addition, the SAL contributed more broadly to these results by raising national awareness of the existing shortcomings and providing momentum for institutional strengthening.

The SAL also made significant contributions to the strengthening of institutions in the transport and communications sectors. In the transport sector, the SAL encouraged the reorganization of the sectors, particularly the railways sector, and supported the launching of new schemes and companies as the Mega-concession and the CREMA in the roads sector, and the CFU and the CCFU in the railways sector. In the communications sector, the SAL encouraged transferring the responsibility for the sector from the Minister of Defense to the MIEM.

Specific achievements under the agreed revised loan condition (Action 11) to help strengthen infrastructure institutions can be summarized as follows:

The Guidelines for the definition of a National Energy Policy have been issued and published by the MIEM (Action 11 of the revised conditions for release of the second tranche). On August 18, 2006 the MIEM issued and posted in its web-page the government's "Guidelines for an Energy Strategy – Uruguay 2006," which provides the basic building blocks of a policy. The strategy took account of inputs from the previous ESMAP-financed work. The key objectives visualized by the Government for the energy sector are to (i) ensure cost-effective supply to satisfy domestic demand, with a good quality of service under the aegis of the State, by maximizing the use of local, regional and renewable energy resources; (ii) promote energy efficiency, diversify the sources of supply and promote clean energy, and (iii) expand the sector with public and private participation, by adapting the legal and regulatory frameworks as necessary. The guidelines address issues relating to: (a) a robust and cost effective electric energy supply system; (b) improved access to fossil fuel resources; (c) inclusion of natural gas in the energy matrix; (d) a greater use of renewable (particularly biofuels, windpower, and biomass-based power generation); (e) policies for energy efficiency; (f) updating and improving the regulatory framework; (g) making energy more accessible to the poor; and (h) encouraging coordination between institutions and participants in the energy sector to better formulate policies and plans and to build capacity within MIEM, particularly the National Directorate of Energy and Nuclear Technology (*Dirección Nacional de Energía y Tecnología Nuclear*, DNETN).

Cross-Linkage of Tranche Release Conditionality

When the second and third tranches of the Special SAL were cancelled at the request of the government and the loan was closed in April 2005, the link became redundant.

Additional Considerations

The impact of the Program went beyond compliance with the specific loan conditionalities. Although some of the original conditions were not fully met as stated in the Program Document and the Loan Agreement, the Government has widely acknowledged that the SAL created a critical momentum during the crisis and its aftermath to achieve necessary sector reforms. The explicitly stated outcomes were largely met in most sectors, as described in section 3.2 and Annex 8, though in several instances through different instruments than originally envisaged in the SAL. The fact that the Government's strategy remained closely aligned with the overall direction proposed by the SAL, though using different means, and sought to achieve the original outcomes partially explains this positive result.

The above focus on sector outcomes was the approach followed during the supervision of Program implementation. The Project team focused on assessing the likelihood of achieving the PDO based on the positive evolution of outcome indicators, as well as progress in the overall dialogue with the authorities on key sector issues, rather than focus on specific outputs/conditions. This difference in approach partially explains the inconsistency between the historic ratings given to the Project in the ISR reports, which rated progress towards achieving the DO as satisfactory, and in this ICR, where outcome assessment is based on compliance with original and revised conditionalities.

2.2 Major Factors Affecting Implementation:

As indicated above, while many of the public sector-specific reforms supported by the SAL were implemented satisfactorily, some of the targeted reforms in a few critical areas were forestalled by external events beyond the control of the Government and by domestic developments that changed the environment for reform in the country. With respect to external events, region-wide constraints emerged in the supply of natural gas and electric power such that the establishment of a regional energy market envisaged by the SAL was no longer a practical proposition, at least in the near term. On the domestic front there were two constitutionally sanctioned referenda that changed the public policy framework on public service reform: the repeal in December 2003 of earlier legislation that had opened the market for petroleum products to private enterprises and the October 2004 constitutional amendment that effectively prohibited private participation in the provision of water supply and sanitation services. At the same time, in the general election of 2004, a new coalition government was elected to office with increased support for public sector management of public services and infrastructure sectors.

Those developments prompted the Government and the Bank to rethink the strategy for achieving the development objectives of the SAL in some important areas. In water supply and sanitation, private participation could no longer be pursued as an instrument for increased efficiency. Instead, increased efficiency would depend more upon institutional, policy and regulatory reform within the public sector. Similar constraints applied to the import, export and refining of petroleum products. Region-wide problems with the supply of electricity and natural gas necessitated a change in sector strategies and ruled out, for example the development of a spot market for electric power, at least in the short- to medium term.

The improved overall financial position of the government by 2005 made it unnecessary for Uruguay to draw down the Special SAL beyond the first tranche. The Special SAL was closed in May 2005 and the undisbursed balance cancelled.

2.3 Monitoring and Evaluation (M&E) Design, Implementation and Utilization

SAL performance was monitored and evaluated using monitoring indicators closely related to the output indicators that were included in the Policy Matrix for the loan. As noted in section 1.2, however, no specific indicators were related to the PDO in the Program Document (as was common practice at the time). This presented significant challenges during the preparation of this ICR, both in terms of finding appropriate data sources and in assessing success at achieving the proposed outcomes (see section 3.2).

The continuity and effectiveness of supervision was not affected by the economic crisis or by the changes in administration. The Policy Matrix and the associated monitoring indicators were the main M&E tools for supervising project implementation, including the regular preparation of Project Status Reports (PSRs). Particularly noteworthy was the close cooperation between Bank staff and government officials in monitoring project implementation, which ensured a continuous dialogue with the government’s economic team, including OPP, and sector ministries of both the former and the current administrations. The new administration which took office in 2005 made good use of the M&E framework in determining approaches and instruments to further advance the Project objectives.

Additional support in monitoring and implementing the Program was provided through the Public Services Modernization Technical Assistance Project (Loan 4598-UR). That operation was founded upon detailed analytical work, and it incorporated lessons from the Bank's ongoing lending experience and policy dialogue. Drawing upon the operational experience from sector projects in power, transport and WSS, the dialogue on public service reform was expanded in 1996 and 1997 and additional analytical and advisory work was undertaken. The Technical Assistance Loan added yet another important dimension to the dialogue by providing the necessary inputs and capacity building to implement the reforms, in particular the strengthening of the regulatory agencies, the new Directorate for Water and Sanitation (DINASA), the National Directorate for Energy and Nuclear Technology (DNETN) and other infrastructure Ministries.

2.4 Expected Next Phase/Follow-up Operation (if any):

Not applicable.

3. Assessment of Outcomes

3.1 Relevance of Objectives, Design and Implementation

(to current country and global priorities, and Bank assistance strategy)

The SAL Program objectives and conditionality were well defined. They constituted a well structured program of reform that would enable Uruguay to resolve the economic crisis and advance its long-term development goals with respect to sustained growth with equity. Program objectives reflected the priorities identified both by the Government and by the Bank in the Country Assistance Strategy (CAS) discussed by the Board on April 19-21, 2005. They were also in line with the issues and recommendations identified in the 2007 Bank paper entitled "Strengthening Energy Security in Uruguay."[4]

The objectives of consolidating regulation and accountability, rationalizing public sector operations, bringing coherence to reforms in the electricity, petroleum and natural gas sectors through the development of a national energy policy, and strengthening the framework for private sector participation were sufficiently flexible to accommodate changing circumstances. These objectives target key areas of public services and infrastructure where, partially triggered by the implementation of the SAL, there is an active public debate on issues such as the development of a national energy policy and the operationalization of the regulatory framework for electric power.

The program design was sound and properly based on a subset of the broad reform program the Government was taking or planning to take in each sector, as outlined in the Letter of Development Policy dated March 7, 2003. The design remains relevant today as demonstrated by the revised Letter of Development Policy dated November 29, 2006 (and the May 4, 2005 letter sent by the Minister of Economy and Finance in relation to the 2005 CAS).

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[4] *"Strengthening Energy Security in Uruguay"* ESMAP Technical Paper 116/07 dated May 2007.

Bank staff properly recognized the importance of infrastructure investment for economic growth and poverty reduction, and made an accurate diagnosis of the infrastructure weaknesses in Uruguay, particularly in terms of policy gaps, relative inefficiencies in the provision of services and limited private sector participation. It reflects well upon the due diligence of Bank staff that they foresaw how vulnerable Uruguay would be to regional and global shortages in energy and to fluctuations in the cost of natural gas and other fuels because of the limited generation capacity installed in the country at the time. Based on that diagnosis, Bank staff properly selected public services and infrastructure as high-priority sectors and, within those sectors, identified the areas of competition and regulation, efficiency and competition, and institutional development as a focus for the reform efforts of the SAL Program. Sectors and themes continue to be high-priorities as they were at the time of Program appraisal.

The PD explicitly acknowledged the risk that the consensus for reform in Uruguay might weaken. When that risk materialized, the Government was confronted with legal and constitutional impediments which obstructed private sector participation in the provision of WSS services and in the refining and international commerce of petroleum products. The Government was, therefore, unable to achieve some of the originally agreed conditions in those areas. A new administration assumed office in March 2005 with a strong commitment to the public management of key economic and social sectors. In addition, region-wide constraints emerged in the supply of natural gas and electric power which made it impossible to establish a regional energy market as envisaged in the SAL-supported program. As a result of those factors, the reform program fell short of accomplishing its agreed outputs in important respects**.**

The operation focused on the right issues, but policy conditionality gave too much weight to specific means (e.g. PSP) as opposed to intended outcomes. At appraisal, Bank staff properly identified the impact of infrastructure investment on economic growth and poverty reduction, and made an accurate diagnosis of Uruguay's weaknesses in the infrastructure sectors, particularly in terms of policy shortcomings, inefficiencies in the provision of services, close and restricted markets, and limited private sector participation. The regulatory framework, efficiency and competition, and institutional development were rightly identified as the areas on which the SAL-supported program should focus. In hindsight however, the Program could have better recognized the likelihood of the risk of shifts in public opinion and how this may have led to different choices of instruments to achieve the Program objectives.

The amended program was also well structured, albeit more limited in scope than the original program. It took into account the significant achievements made with many of the policy and institutional reforms supported by the original program, while acknowledging the impediments to fully implementing the original program. The shortfall between the original program and the amended program was reflected in a reduced loan amount from US$151.52 million under the original loan to US$91.52 million under the amended loan.

Implementation was well organized and properly structured. Bank staff and Government officials had a clear understanding of the macroeconomic and fiscal constraints confronting a population with limited resources. Joint monitoring of Program implementation by Bank staff and government officials helped ensure a continuous dialogue with the government economic team, including OPP, and the sector ministries of both the former and the current administrations. The ease of the dialogue helped to build a bridge to the new administration. The parallel implementation of the ongoing Public Services Modernization Technical Assistance Project (Loan 4598-UR) offered valuable additional support by securing the necessary technical and financial support to establish and strengthen capacity at the regulatory agencies (URSEA and URSEC), the new Directorate for Water and Sanitation (DINASA), the National Directorate for Energy and Nuclear Technology (DNETN), ADME and the Ministry of Transport and Public Works.

3.2 Achievement of Program Development Objectives (PDO)

This section summarizes whether the Program objectives of boosting economic growth by improving the competitiveness of the Uruguayan economy and better serving the public with infrastructure and public and social services have been achieved, as measured by the achievement of the loan's anticipated development outcomes: macro-economic stability, reduced prices, increased quality and coverage, and improved efficiency of public services and infrastructure. Annex 8 reviews in more detail the evolution of these outcomes and other progress at the sector level.

The overall conclusion is that Uruguay has largely met the broad development objectives set out by the program, although some of the original conditions were not fully met and some of the means prescribed by the SAL for achieving sectoral objectives (e.g. more PSP in the water sector) were rejected by both Uruguay's population and its elected government during the latter half of the program.

Macroeconomic Stability

The SAL Program has largely met its broad development objectives and from a macroeconomic perspective has exceeded all expectations. The Uruguayan economy has performed well, as it continued to recover from the 2002 financial crisis and deep economic recession. However, in a few critical areas, targeted reforms were forestalled by external events beyond the control of the government and by domestic political developments that changed the environment for reform.

The SAL Program was part of a US$3.9 billion package pledged by multilateral institutions in 2002 to help Uruguay to stabilize its economy following the 2002 crisis. This exceptional package was successful in supporting Uruguay in overcoming the crisis, without resorting to a debt default or actions that would have led to loss of confidence in the banking sector. The recovery since 2002 has exceeded all expectations. After a contraction of 11 percent in 2002, real GDP had recovered to 116 percent of its pre-crisis level by end-2006. Unemployment has fallen, and inflation has been brought under control, falling from 26 percent in 2002 to 6.4 percent in 2006. Public debt declined from 104 percent of GDP at the end of 2003 to an estimated 64 percent of GDP at the end of 2006. Financial indicators have improved. The high liquidity of the banking sector has reduced vulnerabilities: the liquidity of the banking sector and central bank reserves, cover almost 80 percent of short-term debt and foreign currency deposits. Banking deposits of residents have recovered to about 85 percent of the pre-crisis level.

Table 1: Uruguay Medium Term Macroeconomic Framework
(Percentage of GDP, unless otherwise indicated)

	2003	2004	2005	2006 Est.	Projections 2007	2008
Real GDP (percentage change)	2.2	11.8	6.6	7.0	5.2	3.8
CPI (eop, percentage of change)	10.2	7.6	4.9	6.4	6.5	6.0
Primary Balance	2.7	3.8	3.9	3.9	4.0	4.0
Overall fiscal balance	-3.2	-2.2	-0.7	0.5	-0.3	-0.1
Public sector debt	104	92	69	64	57	55
External current account balance	-0.5	0.3	0.0	-2.4	-3.6	-2.6
excluding: pulp mill projects 2/	-0.5	0.3	0.0	-1.1	-1.3	-1.6
Official reserves (millions of U.S. dollars)	2,087	2,512	3,438	2,777	3,580	3,957
as a % of ST debt + FX deposits	20.0	27.7	32.9	30.7	35.7	38.8

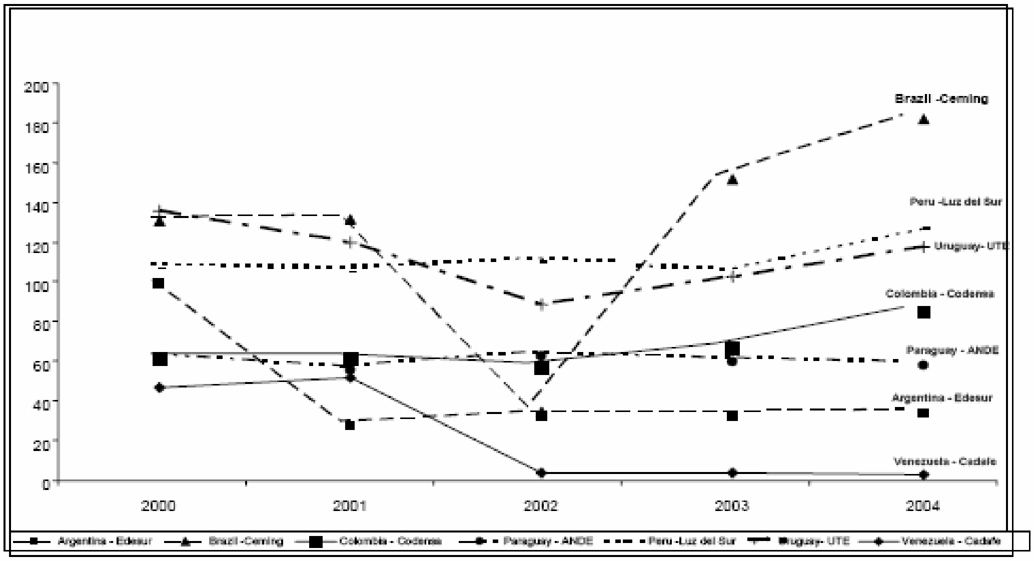
Sources: Uruguayan authorities; and IMF staff estimates

The highly satisfactory 2002-2007 fiscal impact of the SAL positively contributed to the excellent macroeconomic result. Originally estimated at US$168.6 million in the PD, the actual net fiscal impact of the Program will exceed this figure. The sale of concessions to private operators in telecommunications, airports and ports alone has reported at least US$101.1 million to date (US$54.1 million from cellular bands, US$2.9 million from radio links, US$7.5 million from the Montevideo airport, and US$36.6 million from the logistical terminal of the port of M'Bopicuá). The US$101.1 million far exceeds the US$81.7 million estimated for 2002-2006 in the PD. In addition to the revenues obtained from private operators, total benefits to the government include a reduction of over US$40.7 million in operating subsidies to AFE and DNV. Other benefits include the transfers made by ANCAP, ANTEL and UTE to the Treasury and the taxes paid by private and public utilities and ANCAP from 2002 to 2005. These fiscal benefits are over and above the benefits to the public resulting from wider and better access to public services and infrastructure.

Part of the explanation for these impressive results lays in the careful management of fuel prices and public services tariffs, whereby periodic increases were made so that tariffs could recover to their pre-crisis levels. As shown in Figures 1 and 2, both average power and water tariffs recovered quickly from the 2002 economic crisis. An impressive result considering that it was done without social conflict or protest, and without diminishing the high regard that Uruguayans have for their utilities as illustrated in surveys of public satisfaction.[5]

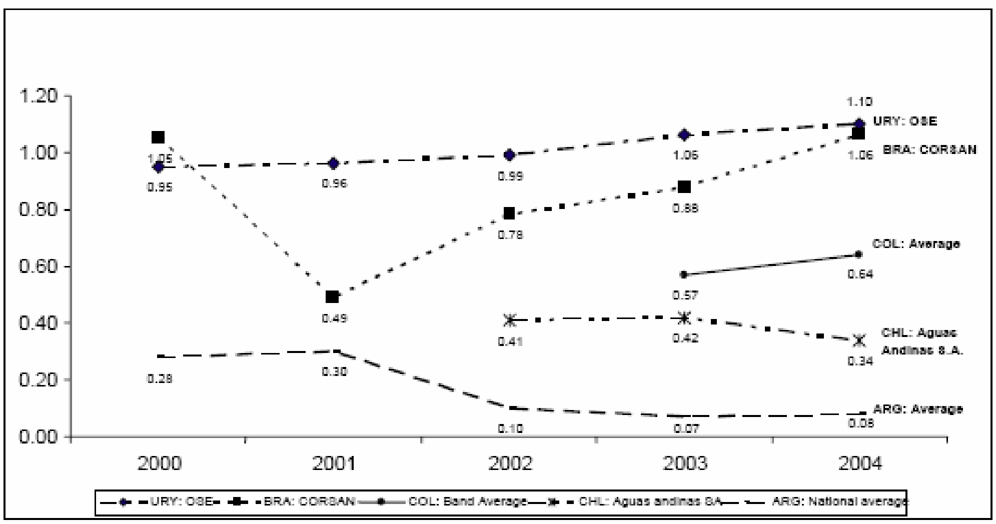
[5] In 2006, for example, the Regional Electrical Integration Commission (CIER) awarded UTE its 2006 Quality Prize – Customer Satisfaction in the bronze category.

Figure 1: Electricity Price (US$/MWh)



Source: UTE.

Figure 2: Average Revenue – Water only (US$/m^3 water sold)



Source: OSE.

As discussed in section 2.1, the SAL Program led to important policy reforms and other measures that successfully contributed to establishing, strengthening and consolidating regulation, promoting competition and improving efficiency; and boosting institutional development. All this has been done within the framework of fiscally sound policies and free of the social upheaval that usually surrounds most reform programs. The fact that the Government maintained and strengthened social protection programs, despite the economic, political and social upheaval that ensued after the 2002 crisis, certainly helped to achieve these results.

Reduced Prices

In most sectors, prices have declined during the loan period (see figures 3 to 8 in annex 8). The SAL contributed indirectly to the price declines through strengthened regulation in the communications, water and energy sectors; increased competitiveness, and greater utility efficiency.

Increased Quality and Coverage

High coverage rates of access to public services and infrastructure have been maintained and the overall perceived quality of public services and infrastructure in Uruguay remains good. The SAL program design widely recognized that Uruguay already enjoyed very high coverage levels of public services and infrastructure in comparison with other Latin American countries. Hence, the program objective was to ensure that the coverage rates would be maintained, in spite of the crisis. No SAL conditions explicitly focused on increasing coverage.

The overall perceived quality of public services and infrastructure in Uruguay remains high, as noted in the World Bank's (2007) Investment Climate Survey and the World Bank's (2007) *Eficiencia en Infraestructura Productiva y Provisión de Servicios en Uruguay*.

Improved Efficiency

Overall, efficiency has improved, as demonstrated in the related indicators, mainly through progress in management and performance, increased participation of the private sector, more competition, and strengthened regulation to varying degrees in the different sectors.

The significant progress that has been made in regulation has helped to improve operators' efficiency and to strengthen sectors' institutions. The process of strengthening and consolidating URSEA, the regulatory agency for energy and water and URSEC, the regulatory agency for communications, is attested by the following results:

- Both agencies are now well established entities that have continuously improved their technical and managerial capacities.
- The presence, roles and responsibilities of both URSEA and URSEC are now acknowledged and recognized, and their reputation and standing with the companies they regulate and with the public at large are sound.
- Both agencies show a relatively high and increasing degree of compliance with existing legislation in the markets they regulate, regularly publish performance indicators, develop strategies to foster growth and competition, and help focus public scrutiny on both private and public utilities.
- Both URSEA and URSEC enjoy a large degree of autonomy. Both agencies have their own autonomous budgets; have defined and approved their own organizational structures; most of the staff who were previously working as short-term consultants

has been fully incorporated as public employees through a competitive process; and have put in place and are implementing ambitious training programs.

Increased private sector participation has also helped to improve efficiency and competition in some sectors, particularly in telecommunications were 18 new private companies began to provide international long distance services during the SAL implementation period and three new mobile companies began competing with ANCEL in the mobile phone market. Uruguay's economic growth and competitiveness have also been boosted by extensive private participation in the ports sector. As shown in table 7, 76 percent of the US$48.4 million invested in ports between 2003 and 2005 and 78 percent of the US$500 million expected to be invested in 2006-2009 represents private capital. Particularly important are those initiatives linked to the transport of forest related products, as for example the ports of Nueva Palmira and M'Bopicuá which are now strong contributors to the export of forest products.

Table 7. Public and Private Investment in Ports (2003-2009)

Investment (US$ million)	Public	Private	Total
Completed	11.8	36.6	48.4
Executed	16.0	20.0	36.0
Under procurement	101.3	387.0	488.3
Equipment	3.0	9.3	12.3
Total	132.1	452.9	585.0

Source: ANP (2006)

As discussed earlier and in annex 7, private sector participation has also played a significant role boosting efficiency and competition in airports and energy. In the energy sector, new private operators have joined the distribution market of LPG in the last four years, following URSEA's approval and implementation of regulation related to this fuel. Additionally, eight new private power generators have joined the market as co-generators, with a total generation capacity of 157.7 MW based in renewable sources (solid waste, wind power and biomass).

The main achievements in each of the sectors per outcome can be found in annex 8.

3.3 Justification of Overall Outcome Rating

(combining relevance, achievement of PDOs)

Rating: **Moderately Unsatisfactory**

The Program Document clearly stated that the operation's main objective was to restore growth in Uruguay at the very delicate[6] juncture of the 2002 regional economic crisis, as part of a concerted effort by multilateral institutions to help the country withstand the impact of strong external shocks and set the stage for recovery. Expected outcomes

[6] Program Document approved by the Board of March 24, 2003

included (i) macroeconomic stability, (ii) increased efficiency and competition, (iii) reduced prices, and (iv) increased quality and coverage of public services and infrastructure. Significant progress was made in all of the above, as described in the previous section and in annex 8.

In the case of the SAL, although its objectives and expected outcomes are clearly stated in the Program document, consistent with Bank practice at the time of preparing the Program, no specific indicators related to the achievement of PDO were stated in the Program Document. Instead, key monitoring indicators closely related to the loan covenants and conditions were included in the Policy Matrix, and as most of the loan covenants, the monitoring indicators specified explicit outputs rather than outcomes. Consequently, success at achieving the PDO is assessed in this ICR through the accomplishments made towards the specific original and revised Loan conditions as stated in the Program Document and the amended Loan Agreement.

According to the *harmonized evaluation criteria* for ICR evaluations and the ICR guidelines issued in August 2006, the overall rating should be assessed against both the original and the amended loan conditions. Following this criterion and **with respect to the originally programmed conditionality the operation is rated as unsatisfactory.** Few conditions were fully met before restructuring the Program and amending the loan. This was particularly the case in the energy and WSS sectors. In the energy sector, programmed reforms were forestalled by external events in the region-wide market beyond the control of the government and agreed outputs could not be met as originally envisaged. In the WSS sector, the 2004 Constitutional Amendment invalidated the overall concept of the draft law that had been sent to Parliament and the agreed approach of pursuing efficiency in controlling unaccounted for water through risk-based contracts with private firms. There was also widespread public resistance to private participation in these two sectors.

With respect to the amended program the operation is rated as satisfactory. As amended, the revised program was made responsive to the development needs of Uruguay at the present juncture. The role of the private sector is less than envisaged under the original program but nevertheless substantial in some areas of infrastructure and public services. Moreover, in the energy sector, the revised program corresponds more closely to the present needs of Uruguay because it takes into account recent region-wide constraints that were not present at the time of appraisal.

As shown in the following table that summarizes this exercise, the overall rating for the operation would be Moderately Unsatisfactory.

		Against Original PDOs	Against Revised PDOs	Overall Disbursements and Rating	Comments
1.	Rating	Unsatisfactory	Satisfactory		
2.	Rating value	2	5		
3.	Weight : % disbursements before and after amendment	56%	44%	100%	1st tranche US$51.52 m. 2nd tranche US$40.00 m.
4.	Weighted value (rows 2x3)	1.1	2.2	3.3	
5.	Final rating (rounded)			Moderately Unsatisfactory	

Note: The weights corresponding to each rating are as follows:

Highly Satisfactory	= 6	Moderately Unsatisfactory	= 3
Satisfactory	= 5	Unsatisfactory	= 2
Moderately Satisfactory	= 4	Highly Unsatisfactory	= 1

While this program is rated as moderately unsatisfactory, the Government of Uruguay has largely achieved the overall development objectives to which the program aspired. As described in annex 8, there has been significant progress in moving towards attaining the stated outcomes in most sectors. Prior to Board presentation, the government responded to the crisis situation by introducing substantial structural reforms. These reforms laid the basis for sustained economic recovery which continues today. Overall, efficiency indicators have generally improved. Significant progress has been made in the policy area of regulation and increased private sector participation (in some sectors) has also helped improve efficiency and competition. In other sectors (water in particular), improved management of a public utility without PSP explains many of the gains. In most sectors, prices have declined during the loan implementation period. High coverage rates of access to public services and infrastructure have been maintained, consumption of public services has increased, and their overall perceived quality remains very good.[7] Public services and infrastructure have been strengthened through improved management and efficiency while, at the same time, protecting the access of the poor to public services.

During implementation, the performance of the loan was judged as satisfactory based on progress toward the PDOs, and the flexibility of and strong partnership between the Government and Bank in adapting to new context in order to sustain progress toward the PDOs. As shown in the following table, the sector by sector results for each outcome are mixed and the overall result is moderately satisfactory.

[7] Since at the time of project design no specific PDO indicators, targets and monitoring mechanisms were provided (see section 2.3), outcomes are assessed in terms of trends observed during the loan period and/or comparisons with country performance across Latin America, depending on data available.

Outcomes	WSS	Transport	Telecom	Postal Services	Power	Natural Gas	Petroleum Products	Overall
Macroeconomic stability								HS
Improved efficiency & competition	MS	S	HS	S	MS	S	MS	MS
Reduced prices	S	S	HS	S	S	S	S	S
Increased quality & coverage	S	S	HS	MS	S	MS	MS	MS
Overall rating	MS	S	HS	MS	MS	MS	MS	MS

However, despite the achievement of the PDOs in Uruguay, this Program is rated as marginally unsatisfactory in this ICR due to the following reasons. First, it is very difficult to demonstrate that the achievements were accomplished through the instruments laid out in the SAL conditions, since the SAL program failed to provide a results framework that adequately linked the loan conditions and program outcomes. Second, many SAL conditions were not actually met as specified in the original Program Document and the Uruguayan government clearly achieved some results (such as better results in the WSS sector) largely through improved management of a public utility, rather than the full set of policy prescriptions (including PSP) contained in the PD.

3.4 Overarching Themes, Other Outcomes and Impacts

(if any, where not previously covered or to amplify discussion above)

(a) Poverty Impacts, Gender Aspects, and Social Development

Under the original program, the operation was cross-linked to a Special SAL which sought to protect social programs from the effects of the economic crisis. Although the cross-linkage was abandoned when the SAL was amended, the developmental objectives of the Special SAL were fully achieved and documented in the ICR for that operation.

(b) Institutional Change/Strengthening

(particularly with reference to impacts on longer-term capacity and institutional development)

The SAL Program has had a major institutional development impact in the areas of public services and infrastructure. Substantial progress was made with administrative reforms in URSEA and ANCAP that enhanced efficiency and set the foundations for further institutional transformation in the future, including the establishment of new policy making institutions. As stated above, particular efforts have been made to consolidate the unbundling of sector functions and strengthen DINASA, the new Directorate for Water and Sanitation, and the DNETN, the National Directorate for Energy and Nuclear Technology, notably through the World Bank's Public Services Modernization Technical Assistance Project (TAL). In the transport sector, the SAL encouraged the reorganization of the sectors, particularly the railways sector, and supported the launching of new schemes and companies as the Mega-concession and the CREMA in the roads sector, and the CFU and the CCFU in the railways sector. In the communications sector, the SAL encouraged transferring the responsibility for telecommunications to the MIEM from the Minister of Defense.

In the energy sector, small-scale power generation has been encouraged and this action represents an important advance in terms of increasing competitiveness pressure in the sector. In addition, the publication of guidelines for a national energy strategy was an important step forward, although it falls short of the original objective which was to introduce a full national energy policy. The reasons for this outcome are threefold. First, external developments in the regional energy market necessitated a reassessment of national energy policies. Second, there was a change of government that brought new ideas to bear on national energy strategies and third, there was a need for additional time to build a new national consensus on how the country should adapt to the changing regional environment.

(c) Other Unintended Outcomes and Impacts (positive or negative, if any)

In retrospect, the SAL-supported program may have been too ambitious in scope and content to rally the widespread support needed for successful implementation. In particular, the proposed initiatives to encourage Private Sector Participation (PSP) in WSS and in the international trade and refining of petroleum products mobilized a number of important constituencies that wanted those sectors to remain firmly in the public domain. As a result, legislative and constitutional initiatives were invoked to block the way. The SAL may have played a role in provoking opposition by elevating the profile of PSP and possibly conveying the impression that the authorities were taking advantage of a crisis situation to push through reforms that did not have broad public support. In Uruguay, where there is a long tradition that calls for consensus, a more measured and longer-term approach to PSP in WSS and petroleum trade may have allowed more time to prepare public opinion. However, both the Bank and the borrower were operating in a crisis environment where an accelerated reform appeared justified.

3.5 Summary of Findings of Beneficiary Survey and/or Stakeholder Workshops
(optional for Core ICR, required for ILI, details in annexes)

Not applicable.

4. Assessment of Risk to Development Outcome

Rating: **Moderate**

For the first time in the last seventy years, the elections of 2005 brought to power a political force other than the two traditional parties, the leftist movement, *Frente Amplio*. The *Frente Amplio* has placed renewed emphasis on the public sector as a leading force in the development process and on improving the efficiency of state-owned public service providers, while maintaining the objective of private sector participation in the majority of sectors. This new approach is still in its early stages. The public sector-oriented approach to the provision of infrastructure and public services may lead to a more gradual and more limited improvement in efficiency than the approach that had been envisaged originally under the Program. Although public utilities in Uruguay are not loss-making, the longer-term financing requirements of the public investment program under the new approach could also impose an added fiscal burden.

The gradualist, consensus approach that has traditionally characterized the Uruguayan model continues to operate under the new administration. Maintaining the pace of the reform process will be challenging given the need for social consensus, including the labor unions and the business community, to carry out wide-ranging reforms aimed at improving the investment climate. Delays in the passage of the tax reform illustrate the challenge of developing the required consensus. On the other hand, the search for consensus that characterizes Uruguay has historically helped to ensure that reforms, once implemented, are generally sustained.

The domestic risks noted above are mitigated by the clear mandate the current administration has received from the Uruguayan electorate and the alignment of the overall objectives of the SAL Program with the government's program. A continued focus on enhancing social protection will mitigate still further the risks arising from social exclusion.

A source of external vulnerability to the program arises from possible restrictions in electric power and natural gas supply that could beset the region. The government is actively exploring improved electricity interconnection with Brazil to complement an existing one with Argentina. Regional energy supply constraints mean that some international cooperation agreements entered into before the crisis are not being honored and will require modification. Those same problems may also be a deterrent to private sector participation. On the other hand, the perspective of unmet energy demand in the future strengthens incentives for investment and innovative market-driven solutions.

5. Assessment of Bank and Borrower Performance

(relating to design, implementation and outcome issues)

5.1 Bank Performance

(a) Bank Performance in Ensuring Quality at Entry *(i.e., performance through lending phase)*

Rating: **Moderately Unsatisfactory**

The Bank collaborated effectively with the borrower in devising an effective strategy for regulatory reform and for increasing efficiency and competition. Possible risks to program implementation were clearly flagged in the Program Document. However, the Bank's performance in identifying, preparing and appraising the operation is rated as moderately unsatisfactory. This is due to the fact that despite the appraisal team's awareness of Project risks, particularly in terms of public opposition to PSP in the WSS and hydrocarbon sectors, the push for structural reform went ahead without explicit alternative strategies in the event that the risks materialized. More generally, the design of the SAL raises a more fundamental question about whether far-reaching structural reforms can best be achieved at a time of deep crisis when conditionality can easily be perceived as an attempt to use external financing as a way to force through policy reforms without popular support.

Finally, the M&E arrangements were not very strong as the PDO were very broadly framed, making difficult to assess their accomplishment.

Loan identification and design were consistent with the CAS. It built directly on previous adjustment operations (SAL and Special SAL), and was consistent with the government's development strategy. The Bank worked closely with the IMF, the IDB and other donors on the design of the loan. Policy actions supported by the SAL program in the areas of public services and infrastructure were well designed. They were designed to have a positive impact on the quality of the public services while preserving access by the poor to those services. The focus on policies that would protect electricity, oil and gas, WSS, transport, telecommunications, and postal services was appropriate considering the social and economic emergency in the country at the time.

(b) Quality of Supervision
(including M&E arrangements)

Rating: **Satisfactory**

The Bank team kept a pro-active relation with government authorities during supervision and was able to engage the new Government in a continued dialogue. The team constantly adjusted, persuaded and engaged former and current authorities and brought about a good result overall. The SAL was monitored through three full supervision missions that included both infrastructure and human development specialists in November 2003, May 2004 and April 2005, and supplementary supervision missions carried out periodically by public services and infrastructure specialists in conjunction with their other supervision responsibilities. The supplementary supervision missions followed up progress on implementing agreed monitoring indicators and discussed results with MEF, OPP, sector ministries and staff, and regulators. It is noteworthy that supervision was not confined to technical Bank staff or to sector specialists. The country Director and program managers took an active interest in program implementation and were constantly available to provide assistance and additional resources when needed.

In addition to regular supervision missions there were ancillary activities that strengthened the supervision function. The Bank funded an ESMAP technical paper that provided support to the government for addressing strategic issues in the energy sector. A Technical Assistance Loan provided an additional avenue of support for supervision of the SAL.

Lastly, the continuity in task management that the Bank maintained both during project preparation and supervision helped to keep a far-reaching multi-sectoral program on track against a background of huge changes both in Uruguay and in the region.

(c) Justification of Rating for Overall Bank Performance

Rating: **Moderately Satisfactory**

The overall assessment of the Bank performance is rated as moderately satisfactory. Project identification and appraisal were moderately unsatisfactory in that a significant amendment to the loan became necessary in the course of its implementation**.** The Bank strove to minimize project delays resulting from political changes in the country, new management teams, and new policy emphases. As it became clear that the project's contingency funds would not be needed and there would be large savings, the Bank urged the government to modify the Loan. Supervision was satisfactory at all stages of implementation and it was intensified during the most severe stages of the economic crisis.

5.2 Borrower Performance

(a) Government Performance

Rating: **Moderately Satisfactory**

The borrower’s role in loan preparation and implementation was rated as moderately satisfactory. The borrower participated actively in the preparation and implementation of the SAL. This included the preparation of interviews, information, research, surveys, contacts, meetings and discussions. The borrower acted quickly, establishing the conditions that made it possible to protect the most vulnerable sections of the population from the effects of the crisis.

The change of administration in March 2005, although unprecedented in the history of Uruguay, did not disrupt the program. The new government showed a high commitment to the development objectives of the program. The communication between the MEF, OPP, and sector authorities was fluent. OPP, with the support of the Ministry of Economy and Finances, worked efficiently to implement the program and no setbacks on the infrastructure sector were in evidence. However, the desire of the government to evaluate anew some program actions (such as the articulation of a national energy plan) has caused the time horizon for program implementation to be extended.

(b) Implementing Agency or Agencies Performance

Rating: **Satisfactory**

The principal agencies responsible for overall loan implementation were OPP and the MEF and their performance is ranked satisfactory. The active involvement of high ranked officials and their commitment to the implementation of the program is especially noteworthy. The role of the sector agencies is likewise ranked **satisfactory**. The agents participating in the Program had widely different responsibilities, and therefore performed different roles. The involvement and active participation of the MIEM after the change in government is also noteworthy.

(c) Justification of Rating for Overall Borrower Performance

Rating: **Moderately Satisfactory**

The borrower's commitment to the adjustment program, and the arrangements made for monitoring program implementation were good. Implementation was not easy because it involved many different government agencies and ministries. Nevertheless, OPP and MEF (and later on by MIEM) did a very good job in keeping track of the situation and making sure that other agencies were aware of their respective obligations. Were it not for the performance of OPP and MEF, continuity may have been lost as a result of many changes in ministers. Where program implementation fell short of the original targets (conditions), the Borrower cooperated with the Bank to find alternative strategies that would satisfy the original development objectives.

6. Lessons Learned
(both operation-specific and of wide general application)

The experience preparing and implementing the SAL Program provides important lessons for future operations.

(i) The design of the SAL raises a fundamental question about whether far-reaching structural reforms can best be achieved at a time of deep crisis when conditionality can easily be perceived as an attempt to use external financing as a way to force through policy reforms without popular support. This may be particularly true in consensus-driven countries like Uruguay.

(ii) Sector reforms should be based on a realistic assessment of the political and economic context and the willingness of the people and the government to accept the reform. Discussions with officials of the current and previous administrations during program implementation showed that a program involving policy changes with many different objectives (increased competitiveness, improved performance, reduced costs, increased competition, greater private participation in many sectors, reduced vulnerability to external changes, etc) involves regulatory rules and an institutional framework that can only work with popular support.

(iii) Regional economic and political issues present opportunities and risks that have to be taken into account in Bank operations. Many infrastructure projects and some services such as telecommunications and energy need a market size that is not to be found in a small country such as Uruguay. The Bank should be mindful that reforms may be affected by changes and have consequences beyond the national frontier and their likelihood of happening should be carefully assessed.

(iv) When cross-linking conditions for tranche release between development policy loans, the financial leverage needs to be weighed together with the potential problems that might arise if reforms move at different speeds. While cross-conditionality provides a good incentive to fulfill commitments, it may also slow down or impede implementation. The experience with the SAL and the Special SAL shows that in some cases, linking two or more operations that have no direct policy connections may have a negative effect when a program that is progressing well does not receive the expected support because of delays elsewhere.

(v) A solid prior understanding of sector issues will facilitate the preparation and implementation of the Program**.** Continuous dialogue with government counterparts and independent analysts simplified the team's work during preparation, because the issues could be clearly identified.

(vi) Close and careful supervision can secure the sustainability of programs even in a time of crisis or change in government. Despite the difficult economic and social situation in Uruguay and the frequent changes of ministers and staff, proactive supervision and a sustained dialogue with MEF, OPP and sector authorities engendered support of the program from all counterparts, and ensured implementation even after March 2005 when there was an unprecedented change of government. An active dialogue enabled bridges to be built with the new administration.

(vii) Other instruments such as a TA loan can help secure the successful implementation of structural and institutional reforms. The Technical Assistance Loan was instrumental in helping to implement the SAL. In particular, by securing the necessary technical and financial inputs to establish and strengthen capacity at the regulatory agencies (URSEA and URSEC), the new Directorate for Water and Sanitation (DINASA), the National Directorate for Energy and Nuclear Technology (DNETN), ADME and the Ministry of Transport and Public Works.

(viii) When a program is vulnerable to serious risks and those risks are identified at appraisal, the operation should include contingency plans that can be mobilized in the event that the risks materialize.

(ix) Strong M&E arrangements should be clearly specified, including appropriate indicators and targets to assess achievement of programmed outcomes.

(x) PDO should be tightly defined to facilitate an objective basis for assessing success.

(xi) Tariff increases and other reforms are possible without social upheaval if properly identified and smoothly conducted. The Bank should understand and acknowledge cultural realities and, if needed, accept slowing down some reforms and relaxing some measures and controls.

7. Comments on Issues Raised by Borrower/Implementing Agencies/Partners

(a) Borrower/Implementing agencies

Annex 4 presents the Government's comments to the draft ICR prepared by the Bank. In general terms, these comments are consistent with the conclusions of the World Bank's ICR. However, the Government left on record its discrepancy with the overall rating ("Moderately Satisfactory" in the draft submitted for their consideration), arguing that the ICR provides enough information to justify a "Satisfactory" rating based on the achievement of the PDOs and how the Government and Bank worked effectively to continue to move toward the PDOs through changes in administration and regional context.

(b) Cofinanciers

Not applicable.

(c) Other partners and stakeholders
(e.g. NGOs/private sector/civil society)

Not applicable.

Annex 1. Bank Lending and Implementation Support/Supervision Processes

(a) Task Team members

Names	Title	Unit	Responsibility/ Specialty
Lending			
Carlos E. Velez	Lead Economist & TTL	LCSUW	
Anna Wellenstein	Infrastructure Policy Advisor	LCSUW	
Vivien Foster	Lead Economist	AFTSN	
Juan Gaviria	Sector Leader	AFTTR	
Ariel Fiszbein	Adviser	DECVP	
Luis Guasch	Senior Adviser	LCSSD	
Eleodoro Mayorga	Hydrocarbons Specialist	COCPO	
Paulo Correa	Senior Economist	ECSPF	
Nelson de Franco	Lead Energy Specialist	LCSFP	
Franz Drees-Gross	Sector Leader	LCSSD	
Juan Ianni	Postal Services Specialist	CITPO	
Juan Pablo Uribe	Senior Health Specialist	LCSHH	
Suhas Parandekar	Senior Education Economist	LCSHE	
Jorge Rebelo	Lead Transport Specialist	LCSTR	
Pilar González	Lawyer	LEGLA	
Daniel Oks	Senior Economist	LCSPE	
Marcelo Celani	Telecommunications Consultant		
Luis Vaca-Soto	Energy Consultant		
Luis Perez	Health Consultant		
Jorge Kogan	Transport Consultant		
Juan Pablo Martinez	Transport Consultant		
Supervision			
Carlos E. Velez	Lead Economist & TTL	LCSUW	
Anna Wellenstein	Sector Leader	LCSSD	
Franz Drees-Gross	Sector Leader	LCSSD	
David E. Yuravlivker	Representative	LCCUY	
Philippe J-P. Durand	Lead Energy Specialist	LCSEG	
Lucia Spinelli	E T Consultant	LCSEG	
Manuel Dussan	Energy Consultant	LCSEG	
Juan Gaviria	Sector Leader	LCSSD	
Pilar Gonzalez	Sr Counsel	LEGLA	
Eleodoro O. Mayorga Alba	Lead Economist	COCPO	
Daniel Fernando Oks	Consultant/Economist	LCSPE	
James Parks	Lead Economist & Sector Leader	LCSPR	
Rolande Simone Pryce	E T Consultant	LEGLA	
Jorge M. Rebelo	Lead Transport Specialist	LCSTR	
Frank J. Earwaker	Consultant	LCC7C	
Vickram Cuttaree	Infrastructure Economist	LCSTR	

Catherine Tovey	Water and Sanitation Specialist	LCSUW	
Andres Pizarro	Senior Transport Specialist	LCSTR	
Luis Vaca-Soto	Energy Specialist, Consultant	LCSEG	
Patricia Lopez	Senior Financial Analyst	LCSUW	

(b) Staff Time and Cost

Stage	Staff Time and Cost (Bank Budget Only)	
	No. of staff weeks	USD Thousands (including travel and consultant costs)
Lending		
FY03	59	356.94
FY04		0.00
FY05		0.00
FY06		0.00
FY07		0.00
Total:	59	356.94
Supervision/ICR		
FY03		6.00
FY04	7	49.44
FY05	6	46.78
FY06	10	78.09
FY07	26	145.61
FY08	3	12.75
Total:	52	338.67

Annex 2. Beneficiary Survey Results
(if any)

Not applicable.

Annex 3. Stakeholder Workshop Report and Results
(if any)

Not applicable.

Annex 4. Borrower's Comments on Draft ICR

This loan was negotiated and approved in the framework of the international financial institutions' aid package for our country, in response to the serious financial crisis weathered in 2002.

In addition to its purpose as a loan operation, it called for a series of reforms intended to promote economic growth, enhance the economy's competitiveness, and improve the people's social well-being.

At the conclusion of the operation it is possible to note substantial progress in attainment of its objectives in terms of economic growth and social well-being, as well as implementation of the reforms agreed upon in each sector.

In the course of the operation there were changes in the contextual setting, which entailed a significant change in the implicit assumptions that justified a number of the actions (established as conditionalities in the initial operating plan). Firstly, there was the crisis in the regional electric and natural gas markets, which precluded broad integration of markets as a mechanism of achieving greater competitiveness in the energy sector. Secondly, there were two referendums (in matters concerning the petroleum sector, the potable water sector, and sanitation) that resulted in changes in the legal framework, so there was no legal basis for some of the proposed reforms. Thirdly, the government elected by the voters in 2004, which supports the operation's objectives, placed greater emphasis on the strategy of improving the management of public sector actors as a means of attaining more effective and efficient provision of public services (in water and power).

Achievement of most of the objectives (economic growth with macroeconomic stability, increased competitiveness, and improvement in the people's well-being), and the successful completion of the operation, lead us to conclude that the latter was satisfactory.

Consequently, the government considers necessary to leave on record its discrepancy with the overall rating … which was given to the operation in Section 3.3 ("Justification of Overall Outcome Rating"). Beyond this rating, the content of the document prepared by Bank staff provides adequate information that will give the operation a rating that is one category higher ("Satisfactory"). For example, with regard to the "Outcomes" table of Section 3.2 ("Achievement of Program Development Objectives"), if the appropriate point is awarded to each cell of the matrix and the average was calculated (by row or column), an overall rating of "satisfactory" (5 points) instead of "moderately satisfactory" (4 points) will be the result.

The manner in which this operation was designed, the changes in the regional and local context following signing, and the negotiation process to modify a number of conditionalities that were no longer feasible or appropriate, leave us with some lessons for the design of future operations:

- It is important to have the destination of the loan proceeds closely linked to the operation's objective and the conditions set for disbursements.
- Mechanisms must be designed to permit flexible terms when there are major changes in the premises and hypotheses, without necessarily altering the operation's basic objectives.
- Carefully evaluate the political, social, and cultural viability of those conditions that call for actions that may not enjoy support by a broad sector of society, either because they are not fully understood or because there is no agreement on the means chosen to accomplish the objective.
- When there is more than one way of achieving the same objective, choose the most effective one but do not reject the rest.
- Distinguish clearly between the indispensable and accessory conditions for attaining given objectives.

In conclusion, despite significant changes in the contextual setting, we can assert that the operation's objectives were achieved for the most part. It is also important to note that the Bank staff and the government representatives both put forth considerable effort during the negotiations at which both parties demonstrated flexibility in prioritizing the initial objectives of the program, without retaining the conditionalities that were no longer applicable.

Finally, as noted in the Charter on Development Policies of November 27, 2006, successful economic development strategy requires alternatives that successfully blend productive growth and social inclusiveness, setting aside the false dichotomy between the two concepts. Taking this premise into account, and considering the lessons and experience gained by all parties in the various stages of this operation, we shall certainly improve the design and execution of future joint cooperation activities.

Annex 5. Comments of Cofinanciers and Other Partners/Stakeholders

Not applicable.

Annex 6. List of Supporting Documents

1. Uruguay – Policy Notes, March 31, 2005, Report No. 31338-UY.
2. Uruguay – Sources of Growth, Policy for Human Capital Development, Integration, Competition and Innovation. November 9, 2004.
3. Uruguay – Improving the Efficacy of Public Expenditures, June 15, 2005, Report No. 305943-UY.
4. Uruguay – Client Survey Fiscal Year 2004, EXT-CD.
5. Uruguay – *Modelo de Equilibrio General Computable para Analizar los Impactos Macroeconómicos del Proceso de Reforma de los Servicios Públicos en Uruguay*, Departamento de Economía, FCS-UDELAR.
6. World Bank Program Document for a Social Program Development Policy Loan, May 10, 2005, Report No. 32289-UY.
7. World Bank Uruguay Country Assistance Strategy 2005-2010.
8. World Bank Implementation Completion Report (FSLT-71650) for the Public Services and Social Sectors Special Structural Adjustment Loan, February 23, 2006, Report No. 32536.
9. World Bank Implementation Completion Report (FSLT-71380) for a Special Structural Adjustment Loan, June 30, 2005, Report No. 32618.
10. Uruguay Poverty Update 2003, June 2004, Report No. 26223-UR.
11. World Bank Program Document for the Public Services and Social Sectors Structural Adjustment and Special Structural Adjustment Loans to Uruguay. March 25, 2003, Report No. 25012-UR.
12. ANCAP (1974-2007) *Histórico de Precios*, Montevideo, Uruguay.
13. Uruguay (2007) – *Documentos del Poder Ejecutivo, Diario Oficial* No. 26.164, March
14. International Monetary Fund (2007), *URUGUAY IMF Country Report No. 07/146*, April 2007.
15. MIEM (2006) Enfoque Metodológico - Taller sobre Elaboración de Propuestas de Lineamientos de Estrategia Energética, Montevideo, Uruguay.
16. URSEA (2007) *Marco Normativo, Leyes, Decretos y Reglamantos del Poder Ejecutivo, Resoluciones de URSEA*, Montevideo, Uruguay.
17. UTE (2007) *Pliegos Tarifarios, Gerencia de Sector Análisis Tarifario,* Enero-Junio, 2007, Montevideo, Uruguay.
18. World Bank (2003) *Uruguay: Structural Adjustment Loan Project*. Report 25012. Washington. D.C.
19. World Bank (2006) Uruguay: ICR Public Services and Social Sectors Special Structural Adjustment Loan, Report 34536. Washington. D.C.
20. World Bank (2002) *Uruguay Country Assistance Strategy (CAS)*, August 8, Report No. R2002-0147. Washington. D.C.
21. World Bank (2005) *Country Assistance Strategy (CAS) for the Oriental Republic of Uruguay for the period FY05-FY10*, Report No. 31804-UY, May 10, Washington. D.C.
22. Uruguay, 2005 *Letter from Minister Astori*, May 4, Montevideo.
23. Uruguay, 2006 *Revised Letter of Development Policy,* November 29, Montevideo
24. World Bank (2003) *Uruguay Poverty Update Report,* Report No. 26223-UR, Washington D.C.
25. World Bank (2007) *Strengthening Energy Security in Uruguay*, ESMAP Technical Paper 116/07, Washington. D.C.
26. World Bank (2005) *Uruguay: Corporate Governance Country Assessment (ROSC),* Washington. D.C.

Annex 7. Compliance with Original and Revised Conditions for Tranches 2 and 3

Regulation of public services

Over the course of the SAL implementation period, regulation was successfully consolidated in Uruguay, despite the changing political and economic environment within the country and the region. Following on from the establishment of URSEC, the regulatory agency for communications, in February 2001, the unbundling of policy making, regulation and operation functions of public services was completed with the creation of URSEA in December 2002 which was charged with rule-making for both the energy (power, natural gas and petroleum products) and water (water supply and sanitation) sectors. Since then URSEA and URSEC have become well established entities. With the support of the national government, both agencies continue to improve their performance and their technical and managerial capacities with renewed ownership, interest and dedication. No specific transport related outputs were part of the loan conditionality.

Specific achievements within each sector and under each of the agreed loan conditions established to help improve regulation can be summarized as follows:

The government successfully established two multi-sector regulatory agencies: URSEA for energy & WSS and URSEC for communications & postal services. Hence, action 1 of the amended conditions governing the release of the second tranche has been met. The agencies have been staffed, Directors have been appointed, and operational procedures have been defined. Both agencies have begun operations. The introduction of regulatory accounting has, however, progressed at different paces in power, WSS, telecommunications, and natural gas. In the power and WSS sectors, URSEA completed the technical work needed for the implementation of regulatory accounting, and public utilities are preparing to implement it. In the telecommunication and natural gas sectors, consultant firms completed the technical work. The regulators expect to complete the implementation of regulatory accounting in 2007.

The publication of performance indicators has progressed significantly. Hence, action 2 of the amended conditions for second tranche release has been met. In the WSS sector, the water utility regularly publishes data concerning quality of service and complementary performance indicators both in the national press and, since February 21, 2003, on its web page[8]. URSEA has posted water quality indicators on its web page since May 10, 2005. With respect to the power sector, on December 24, 2003 URSEA specified a list of indicators that would be published and the modalities of publication. The first set of indicators to be published was for the period January – June 2006. They relate to the quality of service both in technical and commercial terms. In telecommunications, URSEC has posted on its web page, aggregated performance

[8] OSE no longer publicly commits to achieving certain performance levels by certain dates.

indicators for fixed and mobile operators since October 2006. The intention is, in the medium term, to publish these indicators operator by operator. In the natural gas sector, URSEA is currently considering which indicators to request from the concession operator.

Energy

The objective of establishing a target tariff for electricity distribution and converging towards that tariff has not been accomplished to date. Hence, action 1 of the original conditions for second tranche release has not been met. Uruguay has faced a tight power supply situation for several years. Its strategy was based on hydropower resources and on medium-term contracts to purchase power from Argentina. In 2003, URSEA completed a value added study on power distribution and submitted it with a recommendation to the government. However, the former administration left the approval of a target tariff for power distribution to the successor government. After consulting with URSEA and UTE and considering the changes that have taken place in the energy market, particularly in the regional power and natural gas markets, the government decided not to issue the decree at this stage. The Ministry of Industry, Energy and Mines (MIEM) considered that there were other policies that have higher priority, particularly the introduction of transmission tolls. Clearly defined tolls are a basic requirement for attracting the interest of private participants in power generation because they facilitate wholesale transactions. In March 2004, Argentina began reducing energy exports to Uruguay because it was experiencing domestic shortages and Uruguay had to make alternative arrangements which raised the marginal cost of the Uruguayan system from US$54/MWh in 2004 to US$209/MWh in 2006. Tolls for transmissions at voltage levels equal or greater than 150 kV and international transmission were finally approved by decree early in 2007.

A regulatory framework for downstream petroleum products was established. Hence, action 3 of the amended conditions for release of the second tranche has been met. A constitutionally sanctioned referendum on December 8, 2003 revoked the 2002 law that ended ANCAP's monopoly over the import, export and refining of crude oil as well as the export of petroleum derivatives, restricting the market for petroleum products to private enterprises and therefore impacting competition. The possibility that there may be resistance to private sector participation had been recognized in the Project Document as a possible risk to the program. Following the referendum, MIEM issued a decree establishing rules for non-discriminatory access to all stages of the commercialization of combustibles, including wholesale and retail distribution, as well as transport and distribution services. The decree introduced limited competition by allowing new distributors and service stations to be independent of ANCAP. Hence, ANCAP no longer has a monopoly on the domestic distribution and sale of petroleum products. Furthermore, in February 2004, URSEA issued two new regulations on LPG. As a result, there was an increase in the number of bids (from 2 to 4) from operators interested in the distribution of 13 Kg LPG cylinders.

A sector law for natural gas has not yet been enacted. Action 5 of the original conditions for release of the second tranche has not been met. A draft law presented to Parliament by the former administration was withdrawn by the current government which was concerned that the draft law did not address the needs of the gas sector and did not reflect its sector policy. The government believes that public and private sector responsibilities, the tariff system and user rights are already well defined in concession contracts and decrees. Furthermore, the law that created URSEA established regulatory principles for all services for which URSEA is accountable, including natural gas. Today URSEA enforces the terms of concession contracts, including tariffs, service quality and security.

Nonetheless, the government wants to improve the existing legal and regulatory framework for the natural gas sector and MIEM is to lead the task. Options under consideration include the consolidation of all natural gas regulations in a single text (*Texto Ordenado*) and the enactment of a sector law. The objective of the original loan condition was to create a stable legal and regulatory framework for the sector to encourage the introduction of natural gas in the domestic and industrial market and to take advantage of the potential for a regional natural gas market when it develops. Issuing the *Texto Ordenado* would be a significant step towards that objective. The government is concerned that new legislation might be perceived by private operators as a change in the rules of the game that may require contracts to be renegotiated – a perception that may be negatively received by the market.

Postal Services

A regulatory framework for the postal sector has not been established by decree, but most of the important sector issues were satisfactorily addressed in Articles 77-79 of the 2005-2009 Budget Law. Hence, Action 4 of the amended conditions for release of the second tranche has been met. Articles 77-79 of the 2005-2009 Budget Law established a framework for URSEC to monitor and regulate the sector. It mandates universal postal coverage, defines the postal services fee and establishes the fund that will administer sector resources. Moreover, a law is a more powerful instrument than a decree, underscoring the importance of postal service issues to the government. The Executive has informed the Bank that the approval of the Articles was a first step toward a comprehensive regulatory framework for postal services. Meanwhile, a system has been introduced for monitoring sector performance including the quality of service, the volume of mail and the coverage of delivery services.

Water Supply and Sanitation (WSS)

A sector regulatory framework for WSS has not been established. Hence, Action 6 of the original conditions for release of the second tranche has not been met. A draft law establishing the regulatory framework was sent to Parliament by the former administration but it was rendered unconstitutional by the October 2004 Constitutional Amendment. Article 47 of the Constitutional Amendment requires WSS services to be provided exclusively by state entities. That provision invalidated the overall concept of the draft law. The government has begun anew to establish a legal and regulatory framework for the entire water sector (provision of WSS services and water resources management). New institutions have been created, and consultations have begun between them. Comprehensive legislation to underpin the legal and regulatory framework for the WSS sector is now under-way. Significant progress has been made in preparing the draft law, which is now expected to be presented to parliament within one to two years.

Article 327 of the Budget Law 2005-2009 makes the National Directorate of Water and Sanitation (DINASA) responsible for national policies concerning the provision of WSS services and Water Resources Management. Article 331 of the same law establishes an Advisory Commission on Water and Sanitation (COASAS) to incorporate and implement sector policies through inter-institutional coordination and public consultations. In January 2006 the Executive appointed a director for DINASA and placed the entity under the Ministry of Housing, Land Management and the Environment (MVOTMA). In parallel, a coordinating structure has been established to align the new institutional design with the Constitutional reform. An Executive decree was promulgated in November 2006, defining the COASAS' tasks and composition, and opening up a consultation process for the development of the WSS regulatory framework. In addition, an agreement has been signed between MVOTMA and the *Universidad de la República* to assess legal, institutional and technical options for a WSS regulatory framework. Finally, with support from the Bank-financed Public Services Modernization Technical Assistance Project (TAL), work has begun on regulatory legislation with respect to Article 47 of the Constitutional Amendment. It is clear, therefore, that the government is methodically searching for new strategies to improve efficiency and the quality of service in WSS.

Efficiency and Competition

In the telecommunications and transport sectors the results are impressive. Five of the six agreed outputs were fully achieved and the sixth was partially achieved. As a result competition was considerably increased. Eighteen private companies began to provide international long distance services and three new mobile companies began competing with the national company in the mobile phone market. Interconnection regulation, an independent telephone numbering management system, a customer database administrator, and precise rules for identifying the origin and destination of phone calls were approved and implemented. In the transport sector, private operators now manage Montevideo's international airport (Action 6). On July 8, 2003 a contract for the 20-year concession of the Carrasco International Airport was signed between the National Ministry of Defense and the public limited company "Puerta del Sur." Arrangements are under way to improve railway operations by awarding management contracts to private operators and Parliament authorized the creation of the Corporación Ferroviaria del Uruguay – CFU (Railway Corporation of Uruguay), as a public limited company, responsible for the rehabilitation and maintenance of railway infrastructure through a contract with AFE. (Action 10. b).

In the energy and WSS sectors the results are mixed. In the energy sector, despite the lack of success in opening access in the petroleum sector and in establishing an effective and competitive wholesale power market, there has been considerable progress in making the accounts of ANCAP more transparent, in eliminating fuel tax distortions and in closing the gap between ex-refinery prices and estimated import parity prices of petroleum products. Furthermore, a number of measures have been taken to broaden the sources of energy generation, including aero derivative gas turbines, wind power, biomass and small hydro projects. A transition program will gradually introduce wholesale market regulation and establish standards necessary to facilitate the development of independent generation projects.

In the WSS sector, OSE established and put in operation a special unit to manage unaccounted for water activities. The 2005 Constitutional amendment precluded the company from hiring private sector operators to manage that type of program.

Specific achievements within each sector and under each of the agreed loan conditions established to help increase efficiency and competition can be summarized as follows:

Energy

Costs and revenues of the *Administración Nacional de Combustibles, Alcohol y Portland* (ANCAP) have been made more transparent. Hence, Action 4 of the amended conditions for release of the second tranche has been met and has produced the desired result. On February 2005, following the 2003 referendum that revoked the law establishing open access to the oil market, ANCAP created a logistics unit to make costs and revenues more transparent and to facilitate collaboration with companies interested in producing refined products. The new logistics unit is responsible for storage, transport and delivery of ANCAP's petroleum products. It operates separately from the commercialization unit, and it has a separate management and accounting system. Except for the establishment of separate finances, the new unit complies with the requirements of the original condition.

Region-wide constraints to the supply of electric power made it impossible for ADME, the power authority, to arrange for power purchase agreements as envisaged under the program. Hence, Action 7 of the original conditions for release of the second tranche was not met. Law 16.832 of 2002 created an Electricity Wholesale Market (ADME) defined as consisting of a market for fixed-term contracts and a spot market. Power purchase agreements were to be an integral part of ADME. However, the supply of energy from Argentina was seriously interrupted at the time of the economic crisis so that new fixed-term contracts with private sector generators could not be secured. There was also a lack of private sector interest in the development of new electricity generation in the competitive market. The dollarization of export contracts and a temporary interruption of gas supplies from Argentina further disrupted earlier agreements between UTE and private agents in Argentina. There were no offers from private operators in the 2002 when bids were invited for a 300 MW natural gas combined cycle power plant.

In 2005, however, measures were taken to broaden the sources of energy generation in Uruguay and in 2006 UTE signed a power purchase agreement for the installation of 1.2MW aero derivative gas turbine at the Maldonado Landfill. The government also arranged for a wind power project within the framework of a debt restructuring agreement with Spain and issued a decree allowing UTE to contract additional generating capacity based on renewable fuels, and UTE has invited bids for 60 MW of power generation projects based on wind, biomass and small-scale hydro power. To encourage small generation projects, the government is focusing on the security of supply, the design of tolls and access to the transmission network.

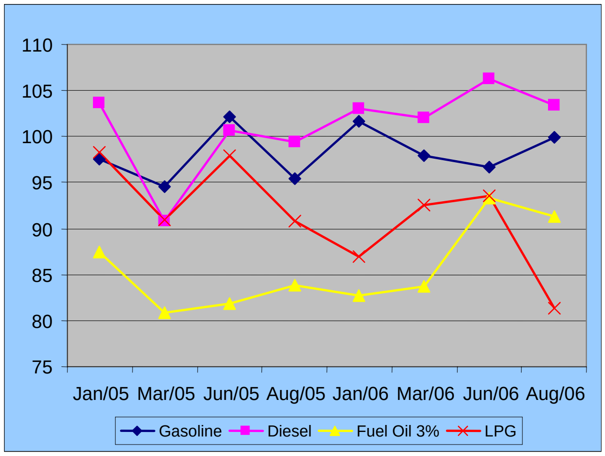
Recent developments have led the government to reconsider the market structure for power. There is a debate within the public sector as to whether, given the relatively small size of the domestic market, expectations from a broader competition framework may be unrealistic. There is also discussion as to whether the electric power utility should keep a strong vertical structure, in order to compete in a regional market that is dominated by large companies. It has been suggested that, at least for the time being, the function of load dispatching and system operations should not be transferred to ADME because it may weaken UTE. However, the transfer of those functions to ADME is crucial if new players are to be attracted and if competitiveness in the power sector is to be enhanced.

Region-wide constraints to the supply of electric power also made it impossible for ADME, the power authority, to establish a spot market for power supply as envisaged under the program. Hence Action 4 of the conditions for third tranche release was not met. A prerequisite for a spot market is the establishment of fixed-term contracts. The government is working to develop a transition program that will gradually introduce wholesale market regulation and establish standards for independent generation projects.

The private sector has not been given open access to the port and warehouse facilities of ANCAP as envisaged under the program. Hence, Action 8 of the original conditions for release of the second tranche has not been met. A referendum led to the repeal of Law 17.448, which would have permitted private operators access to ANCAP facilities. ANCAP retains a monopoly position in this sector apart from the distribution and retailing of petroleum products.

Significant progress has been made towards the goal of closing the gap between the ex-refinery prices and the estimated import parity prices of petroleum derivatives. Hence, Action 7 of the amended conditions for release of the second tranche has been met. From March 2003 to July 2006, the gap for the main derivatives has been reduced significantly, except for LPG (*supergas*) which is used widely by households in Uruguay for heating and cooking. Due to the volatility of international prices it is very difficult to close the price gap for derivatives and keep it closed. Nevertheless, the gap continued to be reduced even when world petroleum prices spiked which indicates that higher prices for derivatives, other than LPG, were fully passed on to the domestic consumer (see Figure 1 below). Key to this achievement has been the methodology established by URSEA in August 2004 for calculating import parity prices for liquid fuels. Those import parity prices are regularly posted on URSEA's web page. In July 2006, the government decreased the consumer price for LPG to encourage substitution away from electricity as part of its broader energy policy.

Figure 1: Relationship between tax free domestic fuel prices and import parity prices (%)



Source: URSEA

Discrepancies in the retail price of fuels between Uruguay and neighboring countries have been significantly reduced. Hence, Action 8 of the amended conditions for release of the second tranche has been met. Relative price distortions have been reduced in two ways: (i) fuel taxes are now fixed instead of proportional as before; and (ii) the absolute prices themselves have been adjusted. In August 2006, for example, tax on a liter of Gasoline Supra 95 (Nafta Super) was 3.4 times higher than tax on a liter of Diesel (Gas Oil). The difference is significantly lower than the 5.3 ratio that prevailed in August 2002. In part as a consequence of harmonizing taxes, a liter of Gasoline Supra at the pump cost 1.5 times more than a liter of Diesel in August 2006. The gap is 30 percent less than in August 2002. Consequently, price differentials between Uruguay and neighboring countries are now smaller (less than 20 percent relative to Brazil and Chile). The price differentials between Uruguay and Argentina are larger because of current Argentine pricing policies.

Water Supply and Sanitation

OSE was not able to offer a performance-based contract to a private operator for the management of a program to reduce Unaccounted-for-Water (UFW) in Montevideo. Hence, Action 9 of the original conditions for release of the second tranche was not met. The Constitutional Amendment of 2005 made it unconstitutional to invite private operators to participate in the WSS. However, OSE has made it clear that two of its top priorities - to be led by OSE are a public sector company - are: (i) reducing UFW and increasing water revenues; and (ii) the company's organizational renewal. The Bank is supporting these efforts with the recently approved second APL for OSE.

Telecommunications

An independent telephone numbering management system has been introduced and it has improved competition in telecommunications. Hence Action 5(a) of the original conditions for release of the third tranche has been met. Besides granting additional licenses in both International Long Distance (ILD) and mobile markets, in 2001 the government made URSEC responsible for planning and managing the telephone numbering system and for assigning numbers. In December 2004, URSEC approved the National Numbering Plan.

The adoption of a customer database administrator has improved competition in telecommunications. Hence, Action 5(b) of the original conditions for release of the third tranche has been met. Decree 442/01 appointed URSEC administrator of the customer database. URSEC held public consultations on how best to access ILD operators and finally adopted a system in September, 2006. The new system is based on dialing and not on pre-subscribing to the data base of a particular administrator, as was the old system.

Precise rules for signaling (i.e., identifying the origin and destination of a telephone call) have been defined and they have improved competition in telecommunications. Hence, Action 5(c) of the original conditions for release of the third tranche has been met. Decree 442/01 made URSEC responsible for the signaling plan. The precise rules for signaling were laid out in the National Signaling Plan and legally established through Resolution 429/04.

Transport

Private operators now manage Montevideo's international airport. Hence, Action 10 of the original conditions for release of the second tranche has been met. On July 8, 2003 a contract for the 20-year concession of the Carrasco International Airport was signed between the National Ministry of Defense and the public limited company *"Puerta del Sur."* The concession covers the administration, operation, maintenance and management of the airport, including commercial activities such as duty free shops. The concession payments consist of a "canon" or fixed charge of US$2.5 million (amortized over the life of the contract) and a fee of US$2.3 per unit of work, which would result in a total contract price of about US$34 million.

Invitations were issued to bid for awarding a management concession of the Montevideo port multipurpose terminal (*puerto polivalente*). Hence, Action 6(a) of the original conditions for release of the third tranche has been met. In December 2002, the National Administration of Ports (ANP) invited bids for the concession of the multipurpose terminal of the port of Montevideo. However, later on the bidding process was halted and the multipurpose terminal concession has not been awarded. Nonetheless and as discussed in section 3.2, the underlying development objective (boosting Uruguay's economic growth and improving the operational efficiency and competitiveness of its ports) was attained in other ways.

Arrangements are under way to improve railway operations by awarding management contracts to private operators. Hence, Action 10(b) of the amended conditions for release of the second tranche has been met. Under the previous government, MTOP invited bids to renovate the railway sections between Montevideo – Rivera – Sagayo – Minas and Toledo – Rio Branco but none of the offers received on March 2004 complied with technical and financial requirements and the bid was cancelled. Subsequently, in January 2006 the current government reversed the separation of infrastructure management and railways operations. Under the new sector policy, a scheme to integrate the railway transport system with the private sector was launched. Under this scheme, Parliament authorized the creation of the *Corporación Ferroviaria del Uruguay* – CFU (Railway Corporation of Uruguay), as a public limited company, responsible for the rehabilitation and maintenance of railway infrastructure through a contract with AFE.

The CFU is expected to be set up in 2007 and will then call for bids from private companies for the rehabilitation of about 900 km of the rail network. The *Comercializadora de Carga Ferroviaria del Uruguay* (CCFU), a parallel mixed (private and public) entity is also to be created and, together with AFE, made responsible for marketing, planning, coordinating and controlling the rail transportation of freight throughout the country and the maintenance of rolling-stock. The objective is to attract the participation of private companies, which would provide rolling-stock and operational expertise. The private sector is expected to invest about US$30 million in infrastructure investment and rehabilitation and US$40 million in capital investment in CCFU.

Institutional Development

Over the course of its implementation, the Program significantly impacted economic development through its support in helping to establish and consolidate regulation in all infrastructure sectors; separate sector functions; define sector policy; and restructure the sectors and their entities. The Program's assistance to regulatory reform was discussed above. The unbundling of sector functions has been notable and welcome in the WSS and energy sectors, including the establishment of new policy making institutions. Particular efforts have been made to strengthen DINASA, the new Directorate for Water and Sanitation, and the DNETN, the National Directorate for Energy and Nuclear Technology, notably through the World Bank's Public Services Modernization Technical Assistance Project (TAL).

The SAL directly contributed to the achievement of these results by promoting and supporting the development and publication of the government's Guidelines for an Energy Strategy, as described below. In addition, the SAL contributed more broadly to these results by raising national awareness of the existing shortcomings and providing momentum for institutional strengthening.

The SAL also made significant contributions to the strengthened of institutions in the transport and communications sectors. In the transport sector, the SAL supported the reorganization of the sectors, particularly the railways sector, and supported the launching of new schemes and companies as the Mega-concession and the CREMA in the roads sector, and the CFU and the CCFU in the railways sector. In the communications sector, the SAL encouraged transferring the responsibility for telecommunications to the MIEM from the Minister of Defense.

Specific achievements under the agreed loan condition established to help strengthen infrastructure institutions can be summarized as follows:

Guidelines for the definition of a National Energy Policy have been issued and published by the MIEM. Hence, Action 11 of the amended conditions for release of the second tranche has been met. On August 18, 2006 the MIEM issued and posted in its web-page the government's "Guidelines for an Energy Strategy - Uruguay 2006," which provides the basic building blocks of a policy. The strategy took account of inputs from the previous ESMAP-financed work. The key objectives visualized by the Government for the energy sector are to (i) ensure cost-effective supply to satisfy domestic demand, with a good quality of service under the aegis of the State, by maximizing the use of local, regional and renewable energy resources; (ii) promote energy efficiency, diversify the sources of supply promote clean energy, and (iii) expand the sector with public and private participation, by adapting the legal and regulatory frameworks as necessary. The guidelines address issues relating to: (a) a robust and cost effective electric energy supply system; (b) improved access to fossil fuel resources; (c) inclusion of natural gas in the energy matrix; (d) a greater use of renewables (particularly biofuels, windpower, and biomass-based power generation); (e) policies for energy efficiency; (f) updating and improving the regulatory framework; (g) making energy more accessible to the poor; and (h) encouraging coordination between institutions and participants in the energy sector to better formulate policies and plans and to build capacity within MIEM, particularly the National Directorate of Energy and Technology (*Dirección Nacional de Energía y Tecnología Nuclear*, DNETN).

Annex 8. Progress on Project Development Objectives

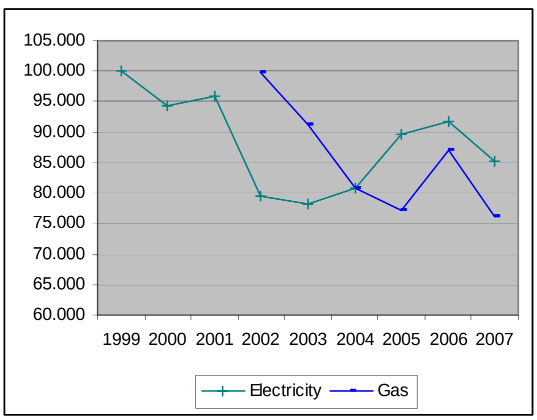
Reduced Prices

In most sectors, prices have declined during the loan period. The SAL contributed mostly indirectly through strengthened regulation in the communications, water and energy sectors (since regulators help set tariff structures); increased competitiveness, and greater utility efficiency. Moreover, specific program conditions were targeted at *increasing* petroleum prices to align them with market prices. This section reviews the evolution of prices at the sector level.

Energy

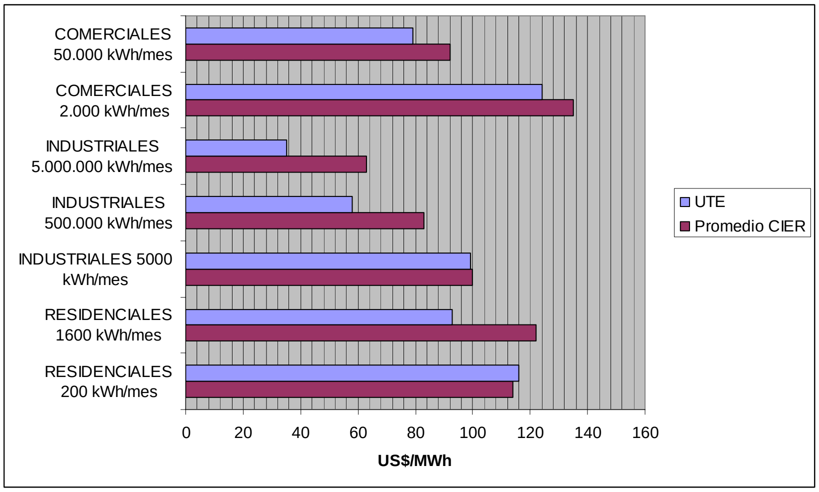
Reforms in the power sector have been modest, yet progress has been made. The cost of gas has decreased by 24% compared with 2003 (see Figure 3). Electricity prices have been reduced by 15% compared with pre-crisis 2000 levels, although they are now 9% higher that in 2003. Nevertheless, most of UTE's tariff blocks remain below the Regional average tariffs in the power sector (see Figure 4).

Figure 3: Evolution of consumer's power and gas price indexes (constant prices and without taxes)



Source: URSEA and DNETN

Figure 4: Comparison of UTE tariffs with regional average for utilities in CIER (Regional Electric Integration Commission)



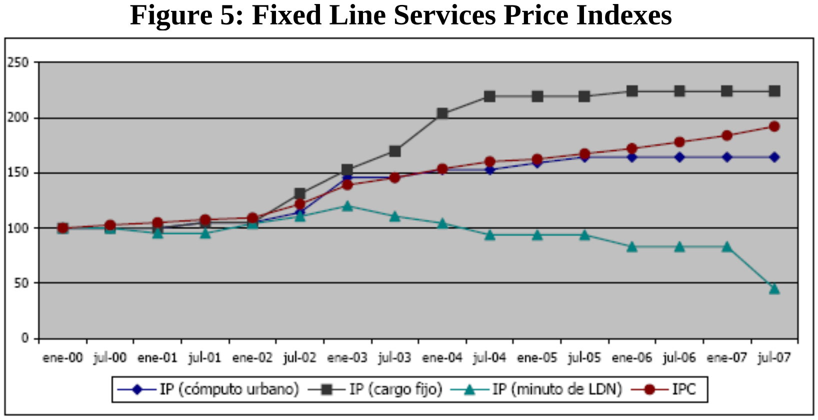
Source*:* CIER

In the petroleum sector, as discussed in section 2.1 and in annex 7, rather than reducing prices, the aim was to close the gap between the ex-refinery prices and the estimated import parity prices of petroleum derivatives. This objective was accomplished and the gap for the main derivatives has been reduced significantly, except for LPG (*supergas*) which is used widely by households in Uruguay for heating and cooking.

Telecommunications

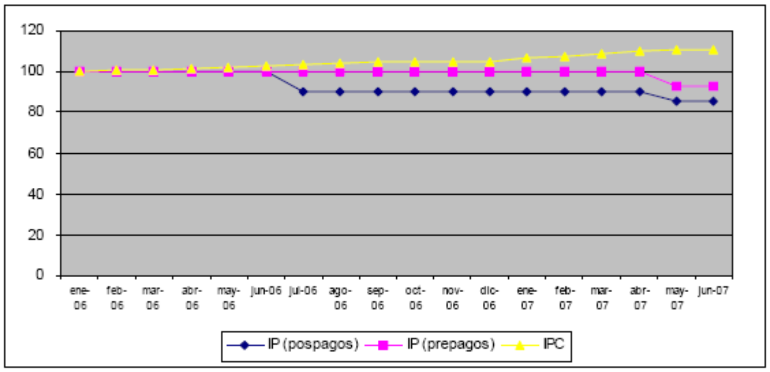
The cost of communications has generally been falling, according to the latest figures provided by URSEC. For example, the average cost of a long distance call fell by 33% (in constant pesos) between January 2002 and January 2005 and appears correlated with the entrance of new players in the communications market in mid-2002 (Figure 5). Figure 6 shows that prices of mobile communications (both pre-paid and post-paid) have been evolving below the overall price index. Figure 7 shows a recent decline in mobile phone prices.

Figure 5: Fixed Line Services Price Indexes



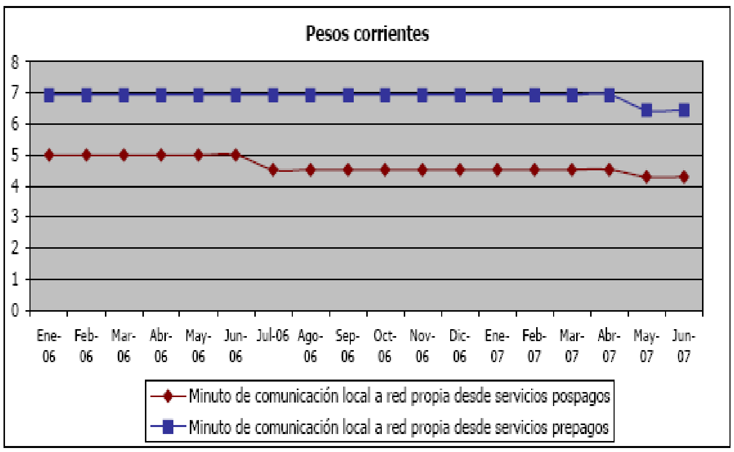
Source: URSEC

Figure 6: Consumer Prices and Mobile Services Prices Indexes



Source: URSEC

Figure 7: Cost of mobile to mobile communication (current pesos)



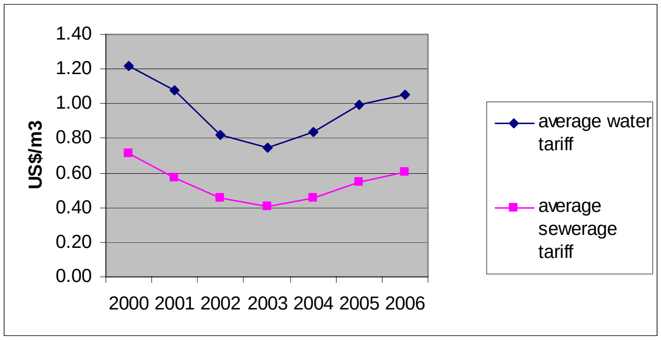
Source: URSEC

Water and Sanitation

In the WSS sector, some modest reductions in tariffs have also been made. Although tariffs have recovered from their post-crisis low in 2003, tariffs do remain almost 15% lower than in 2000 (see Figure 8). Moreover, OSE should be commended for its careful management of tariffs during the crisis and its ability to rapidly recover revenue collection rates following the crisis (shown in Figure 28 below, under the efficiency section), thereby achieving the twin objectives of maintaining affordability and supporting a rapid economic recovery and financial sustainability of the utilities. OSE restructured tariffs in January 2007 in efforts to rationalize and make tariffs more transparent. This restructuring should further reduce average tariffs for 2007.

Figure 8 also illustrates the quick recovery of average water tariffs from the 2002 economic crisis. The effective handling of tariffs ensured that the crisis had only a temporary impact on OSE's revenue. However, relative to other Latin American countries, Uruguay's tariffs continue to be high, indicating there may be room for more efficiency gains in the future

Figure 8: Evolution of OSE tariffs (constant prices)



Source: OSE

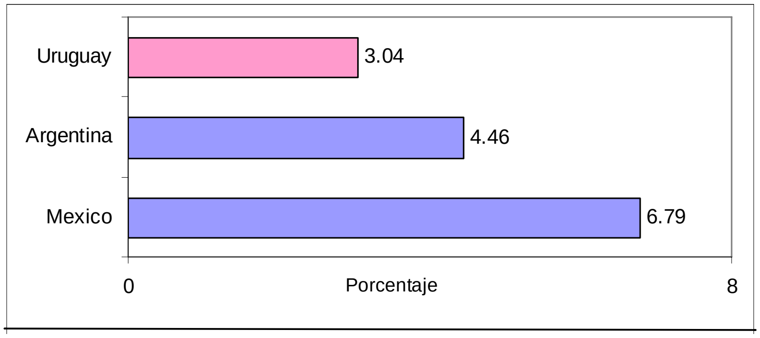
Transport

Uruguay has lower direct transport costs than Argentina or Mexico[9] (Figure 9), although it varies significantly according to the type of product (see Tables 2 and 3). Final destination also affects transport costs (direct costs for export are typically two or three times higher than domestic, when comparing Food and Other Manufactures in Tables 2 and 3).

The surveys conducted for the preparation of the Investment Climate Assessment also indicated that transportation costs and losses from breakage and spoilage as a percentage of shipment value are low in Uruguay compared with countries in the region (Figure 10). This data can be considered as a proxy for indirect costs in the absence of a monetary quantification. The low indirect costs are an indication of the good quality and relative reliability of transport services and infrastructure in the country. As shown in table 4, the average shipment time for exporting firms is 20 days to destination whereas at the local level, the average delivery time is less than one day (this is a good value that indicates no significant interruptions or unnecessary delays in domestic transportation adding to the indirect costs).

[9] Based on answers provided by interviewed firms for the Investment Climate Assessment, World Bank, 2007

Figure 9: Direct Transport Costs as a % of Total Value of Shipping Main Product (manufacturing firms)



Source: Surveys for Investment Climate Assessment, 2007, World Bank

Table 2: Direct Transport Costs as a % of Total Value of Shipping By type of Product (non-exporting firms)

Type of Product	Transport cost over total value of shipping (%)
Food	3,1
Construction, Transport and Storage	2,8
Non metal minerals	10,7
Other manufactures	2,7
Wholesale Product	6,1
Average	3.2

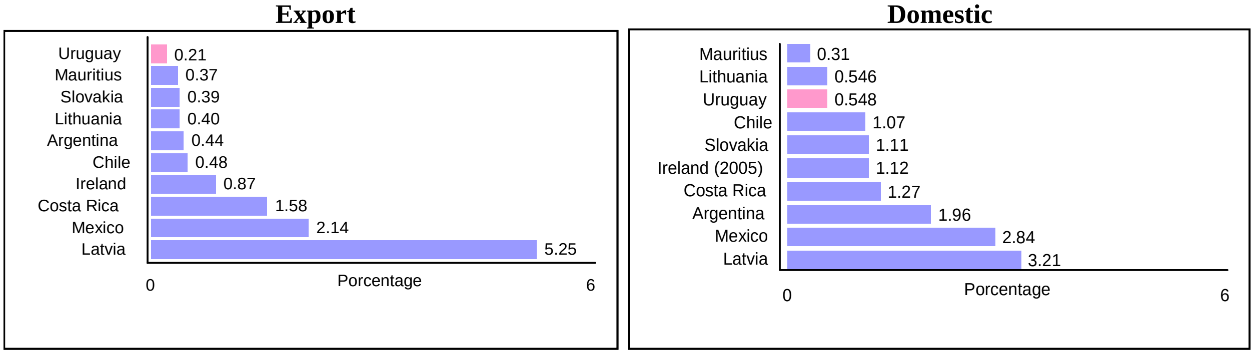
Source: Surveys for Investment Climate Assessment, 2007, World Bank

Table 3: Direct Transport Costs as a % of Total Value of Shipping By type of Product (Exporting firms)

Type of Product	Transport cost over total value of shipping (%)
Food	7,6
Other manufactures	9,1
Chemical Products	21,5
Average	13,0

Source: Surveys for Investment Climate Assessment, 2007, World Bank

Figure 10: Breakage or Spoilage Losses in Shipments (Export and Domestic)–Indirect Costs



Source: Surveys for Investment Climate Assessment, 2007, World Bank

Table 4: Average Arrival Time to Destination

Firms	No. of Responses	Days
All	50	14,5
Exporting firms	36	19,8
Non exporting firms	14	0,9

Source: Surveys for Investment Climate Assessment, 2007, World Bank

Ports operations in Montevideo are competitive and have grown considerably since the 2002 reform. In 2005, the port of Montevideo handled 454,531 TEU (Twenty-foot Equivalent Unit) (See Table 5). Overall, the number of TEUs has increased seven-fold since the 2002 reform, which resulted in intra-port competition, a decline in port tariffs, and significant new investments from the private sector. The average cost of container transfer in Montevideo is substantially lower than non-concessioned ports in Peru, Ecuador, and Central America. The port of Montevideo is fairly competitive relative to other privately operated ports in Latin America. For instance, the cost per TEU in Montevideo is less than in Buenos Aires (Argentina) and Valparaiso (Chile) but slightly more than in Cartagena (Colombia).[10]

Table 5: Container Traffic in Montevideo Port

Year	TEUs	Annual Growth (%)
1990	64,286	
2000	287,298	35
2001	301,641	5
2002	292,962	-3
2003	333,871	14
2004	424,791	27
2005	454,531	7

Source: Montevideo Port webpage; http://www.anp.com.uy/montevideo/default.asp

[10] See Universidad Politécnica de Valencia, 2003.

Increased Quality and Coverage

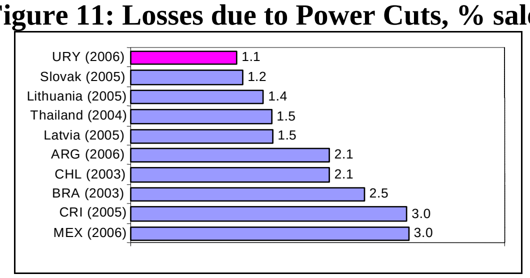
High coverage rates of access to public services and infrastructure have been maintained and the overall perceived quality of public services and infrastructure in Uruguay remains good. The SAL program design widely recognized that Uruguay already enjoyed very high coverage levels of public services and infrastructure in comparison with other Latin American countries. Hence, the program objective was to ensure that the coverage rates would be maintained, in spite of the crisis. No SAL conditions explicitly focused on increasing coverage.

The overall perceived quality of public services and infrastructure in Uruguay remains high, as noted in the World Bank's (2007) Investment Climate Survey and the World Bank's (2007) *Eficiencia en Infra-estructura Productiva y Provisión de Servicios en Uruguay*. The following paragraphs review the main achievements in each of the sectors in terms of improved coverage and quality of the services and infrastructure.

Energy

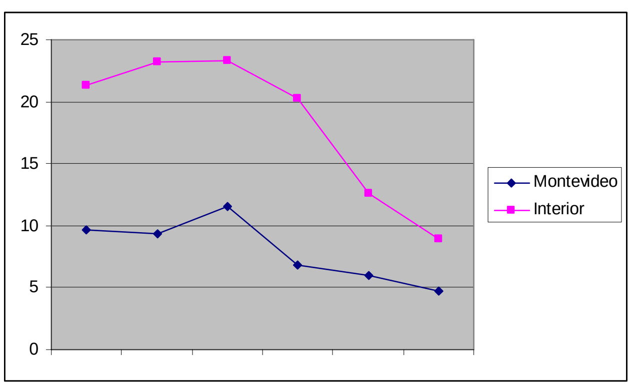
Uruguay compares very well with other regional countries in losses due to power cuts as declared by businesses (Figure 11). There has also been a positive evolution in the reduction of the frequency of interruptions for consumers (Figure 12). Although, coverage rates have remained above 90%, waiting times for access to the service still ranks relatively poorly compared with other countries in the region (Figure 13).

Figure 11: Losses due to Power Cuts, % sales



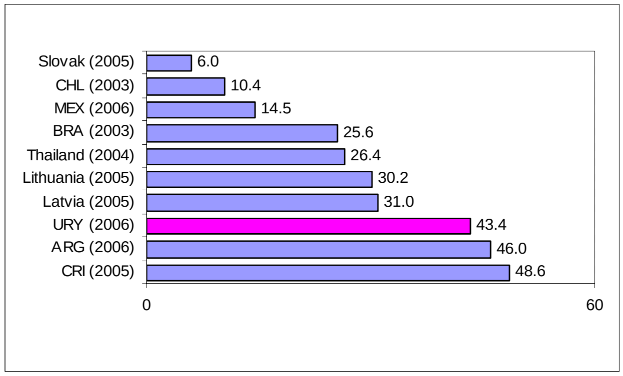
Source: 2007 Investment Climate Survey, World Bank

Figure 12: Evolution of frequency of interruptions for consumers (1999-2005)



Source: UTE

Figure 13: Average days to obtain a new electricity connection

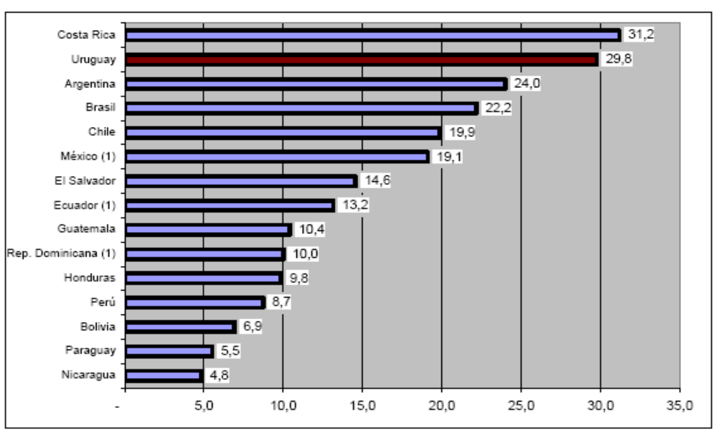


Source: 2007 Investment Climate Survey, World Bank

Telecommunications

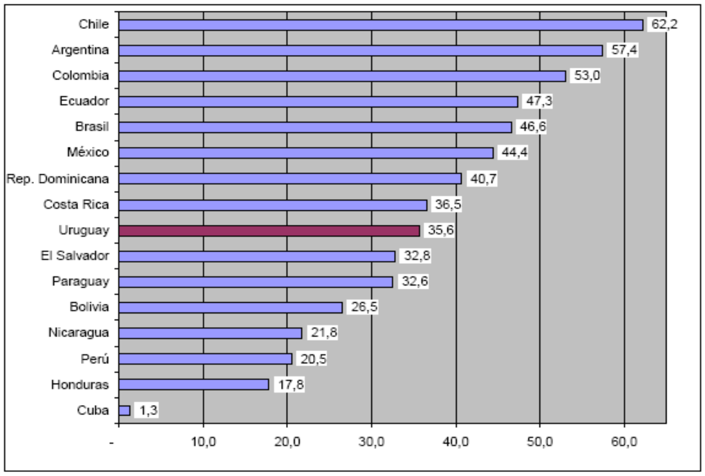
Uruguay has managed to develop the most extensive telecommunications sector in the entire region and it now has the highest penetration rate in Latin America for fixed-line subscribers. The fixed network is 100 percent digitalized and there is no waiting time to acquire a fixed line. Fixed-line coverage and teledensity is very high compared to regional averages (Figure 14) and Uruguay ranks amongst the first 10 in Latin-America in terms of mobile teledensity (Figure 15). As discussed above, Uruguay remains well ranked in the Americas in terms of digital opportunity access.

Figure 14: Regional comparison of land phone teledensity (per 100 people) December 2006



Source: URSEC, 2007

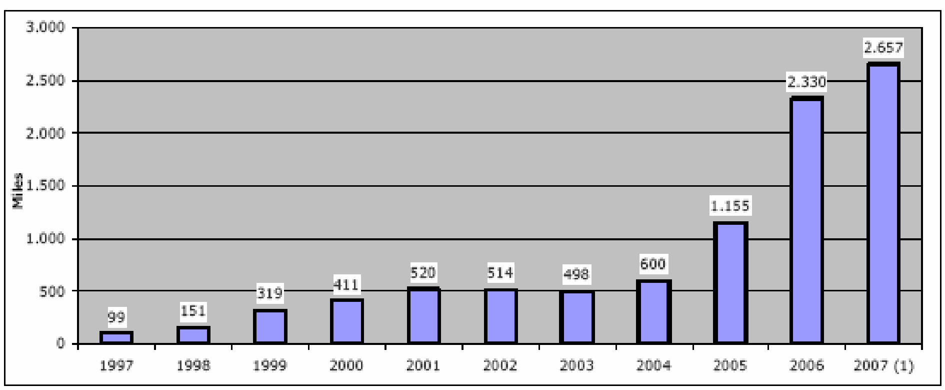
Figure 15: Regional comparison of mobile phone teledensity (per 100 people)



Source: URSEC (2007)

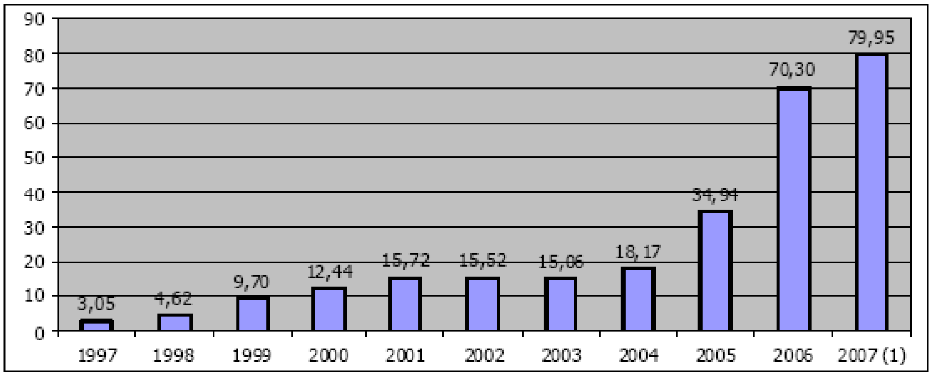
Competition in the mobile telephone industry began in 2004, leading to an explosion in the number of mobile subscribers and teledensity (mobile phone subscribers per 100 inhabitants), especially in the last three years (see figures 16 and 17).

Figure 16: Number of Mobile Subscribers (1000)



Source: URSEC (2007)

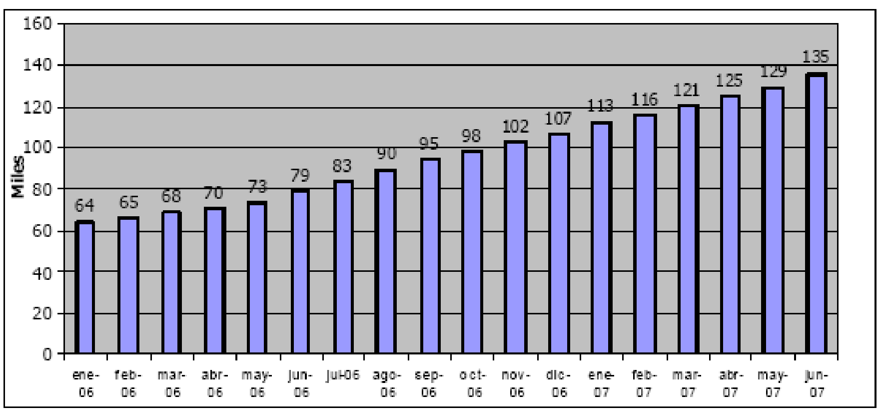
Figure 17: Evolution of Mobile Teledensity (mobile phone subscribers per 100 people (1997-2007)



Source: URSEC (2007)

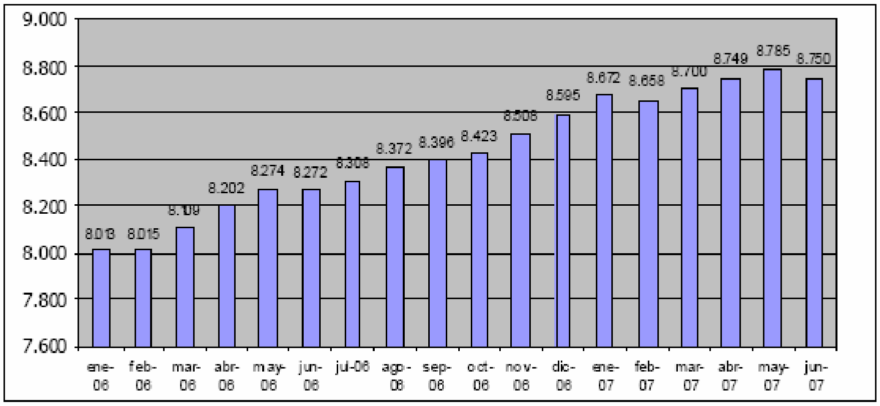
Internet access is also growing at a considerable rate, especially non-commuted services through the different technologies offered by the operators. The current trends shows that non commuted access is gradually substituting commuted services (figure 18). The volume of data transmission services (national and international) is also showing a growth trend in the last 2 years (figure 19).

Figure 18: No. of Non-commuted Access to Internet Services (1000)



Source: URSEC (2007)

Figure 19: Volume of Data Transmission Services (national and international)



Source: URSEC (2007)

Water and Sanitation

OSE's capacity to reduce its operating costs and maintain a sound operating margin (discussed above) also enabled OSE to scale-up investments in WSS service expansion during the crisis and its aftermath. Uruguay continues to enjoy some of the highest water supply coverage levels for middle income countries. Access to safe water is universal and 96% of households are connected to the piped water supply network. As with most of the region, access to sewerage is somewhat lower at around 48% nationally (see figure 20).

Since 2002, OSE has successfully provided an additional 81,000 new water supply connections, including 5,400 individual household connections in informal settlements in Montevideo which sprung up after the crisis. However, given already excellent water coverage rates, and in the absence of detailed up-to-date data, these incremental improvements in coverage have not been reflected in the national coverage data available[11]. OSE gains in terms of improving sewerage coverage have been easier to measure. Access to OSE sewerage services[12] in the interior of Uruguay (excluding the capital Montevideo) has increased from 26% in 2002 to 32% in 2006. OSE's capacity to

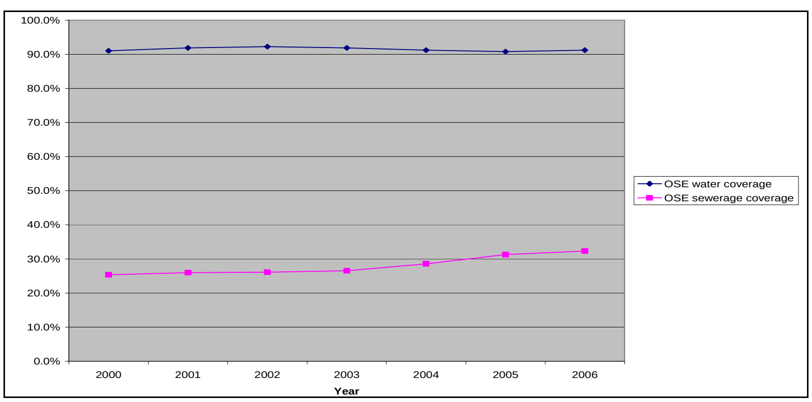
[11] According to the WHO-UNICEF JMP, household connection rates to the piped water network remained constant between 2000 and 2004 (latest available data) at 96%. According to OSE own data, the proportion of households in Uruguay with an OSE water connection has decreased very slightly from 92.3% in 2002 to 91.2% in 2006. However OSE data may not accurately reflect coverage trends for several reasons. First, the financial crisis led to a sudden proliferation of underserved informal urban settlement particularly in Montevideo. Although OSE has provided 5400 formal metered individual connections in Montevideo settlements since the crisis, a large number of these connections are informal (i.e., connected to the OSE network, but being measured as unaccounted for water) and are therefore not captured in the above coverage rates. Second, the drop in 2005 coincides with the re-incorporation of Maldonado into OSE books (since Maldonado, a seasonal costal resort area, had lower connection rates that overall OSE). Third, in-between national censuses, coverage rates are based on total population estimates In sum, coverage rates remain high, and may have even increased, in spite of the crisis.

[12] Excluding Montevideo, where the Montevideo Intendencia (IMM) is responsible for sewerage services.

treat sewage has also increased, with the construction of 3 new sewage treatment plants in *Minas, Treinta y Tres* and *Durazno*, which can now serve up to 60,000 people. These investments were partly financed by a World Bank loan – the *OSE Modernization and Systems Rehabilitation Project (APL-1).*

OSE's provision of water supply and sanitation services has improved, both in terms of consumer responsiveness, and quality of service. The role played by performance benchmarking has been well documented and helped promote transparency; the harmonization of systems and processes; efficiency improvements; improved collaboration between traditional commercial and operational silos; and more results-based decision-making. In particular, the simple act of measuring data (e.g. waiting times) has led to some immediate improvements in OSE's attention to clients, and helped remove glitches in existing operational processes (e.g., reducing the double counting of customer complaints). Overall, OSE's quality of service index has been generally improving, achieving its overall targets in 2 out of 3 cities. OSE's *quality of service indicators* also indicate that the level of commercial and operational claims is consistently rated excellent across all 5 Regions; the speed at which OSE is able to re-establish water supply service is rated excellent in 4 out of 5 Regions; and the quality of the water is rated good to excellent in all Regions. The 3 new sewage treatment plants not only help increase sewage treatment coverage, but their effluent quality is now being monitored on a monthly basis by new environmental monitoring systems established in all three plants, to ensure appropriate environmental standards (set by decree 253/79) are met. OSE also continues to benefit from very high levels of consumer satisfaction, with more than 80% of Uruguayan consumers satisfied with OSE's water services.[13]

Figure 20: Evolution of OSE coverage (2000-2006)



Source: OSE (2007)

Transport

Access to transport infrastructure in Uruguay is high. The road and port sectors record good levels of service quality and efficiency (although the railway sector is not as

[13] OSE Encuesta del Cliente (Client Survey), 2006.

competitive). Density and coverage indicators for the road and railway networks are the highest in Latin America, with most of the country's population within a short distance of transportation infrastructure. The road network provides good accessibility to practically anywhere in the country. During the SAL period and as a result of improvements mentioned below in the efficiency section, the roads sector's relative high levels of coverage and quality have been kept unchanged, despite the pronounced reduction of expenditures brought about by the 2001-2002 economic crisis. As shown in table 6, Uruguay consistently rates highest in the region in terms of rail and road network coverage and density.

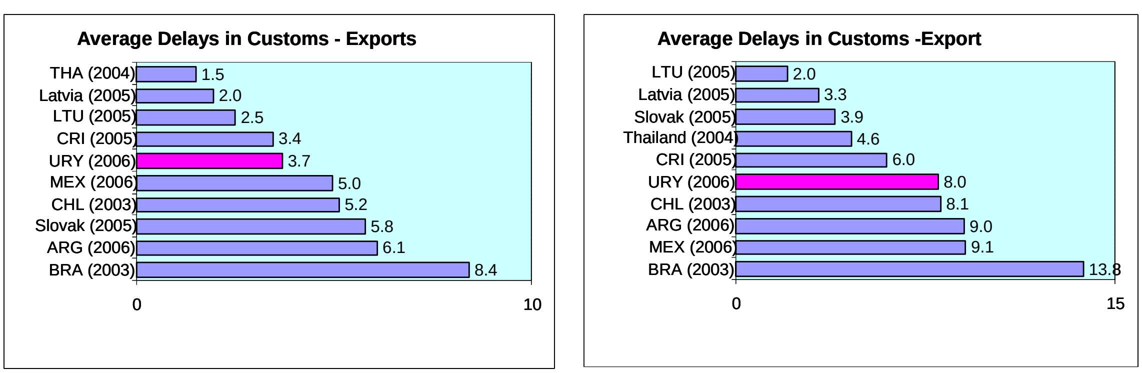
Average delays in Uruguayan customs are low for Latin-American standards as shown in figure 30, but are high in comparison to European and Asiatic comparable countries (Figure 21). Only 4 percent of firms in the investment climate survey considered transportation to be one of the top 3 obstacles to their business.

Table 6: Density and coverage of road and rail networks in Uruguay

Country	**Density** per population (km/1000 people)		**Network coverage** by area (km/1000 km^2)	
	Road	**Rail**	**Road**	**Rail**
Argentina	6,1	0,9	77,5	11,4
Brazil	10,3	0,2	201,8	3,4
Chile	5,3	0,7	104,9	13,2
Colombia	2,7	0,1	99,2	2,8
México	3,4	0,2	168,3	9,0
Paraguay	5,7	0,0	72,5	0,4
Peru	3,1	0,1	60,8	1,3
Uruguay	**21,4**	**0,9**	**401,4**	**17,0**
Indonesia	1,5	0,0	162,8	2,8
Malaysia	2,9	0,1	199,8	4,9
Philippines	1,0	0,1	111,9	7,9
Thailand	2,7	0,0	673,3	1,6

Source: World Bank (2007) Eficiencia en Infraestructura Productiva y Provisión de Servicios en Uruguay

Figure 21: Average Delays in Customs (Export and Import)



Source: Surveys for Investment Climate Assessment, World Bank 2007

Improved Efficiency

Overall, this outcome has been largely achieved and efficiency indicators have generally improved, mainly through progress in management and performance, increased participation of the private sector, more competition, and strengthened regulation to varying degrees in the different sectors.

The significant progress that has been made in the policy area of regulation has helped to improve operators' efficiency and to strengthen sectors' institutions. The process of strengthening and consolidating URSEA, the regulatory agency for energy and water and URSEC, the regulatory agency for communications, is attested by the following results:

- Both agencies are now well established entities that have continuously improved their technical and managerial capacities.
- The presence, roles and responsibilities of both URSEA and URSEC are now acknowledged and recognized, and their reputation and standing with the companies they regulate and with the public at large are sound.
- Both agencies show a relatively high and increasing degree of compliance with existing legislation in the markets they regulate, regularly publish performance indicators, develop strategies to foster growth and competition, and help focus public scrutiny on both private and public utilities.
- Both URSEA and URSEC enjoy a large degree of autonomy. Both agencies have now their own autonomous budgets; have defined and approved their own organizational structures; most of the staff, who were previously working as short-term consultants, have been fully incorporated as public employees through a competitive process; and have put in place and are implementing ambitious training programs.

Increased private sector participation has also helped to improve efficiency and competition, particularly in telecommunications were 18 new private companies began to provide international long distance services during the SAL implementation period and three new mobile companies began competing with ANCEL in the mobile phone market. Uruguay's economic growth and competitiveness have also been boosted by extensive private participation in the ports sector. As shown in table 7, 76 percent of the US$48.4 million invested in ports between 2003 and 2005 and 78 percent of the US$500 million expected to be invested in 2006-2009 represents private capital. Particularly important are those initiatives linked to the transport of forest related products, such as the ports of Nueva Palmira and M'Bopicuá which are strong contributors to the export of forest products.

Table 7. Public and Private Investment in Ports (2003-2009)

Investment (US$ million)	Public	Private	Total
Completed	11.8	36.6	48.4
Executed	16.0	20.0	36.0
Under procurement	101.3	387.0	488.3
Equipment	3.0	9.3	12.3
Total	132.1	452.9	585.0

Source: ANP (2006)

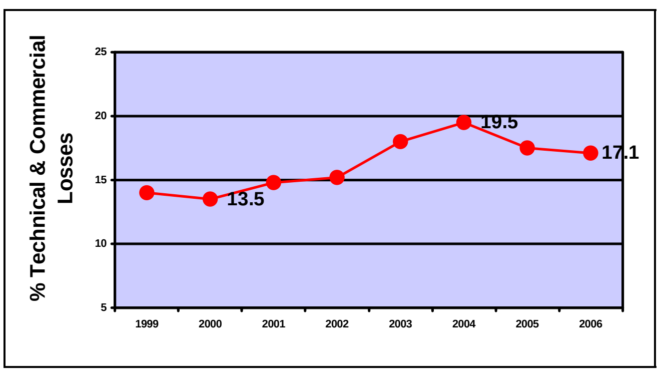
As discussed earlier and in annex 7, private sector participation has also played a significant role boosting efficiency and competition in airports and energy. In the energy sector, new private operators have joined the distribution market of LPG in the last four years, following URSEA's approval and implementation of regulation related to this fuel. Additionally, eight new private power generators have joined the market as co-generators, with a total generation capacity of 157.7 MW based in renewable sources (solid waste, wind power and biomass).

The following paragraphs review the main achievements in efficiency and competition in each of the sectors.

Energy

Before 2002, UTE had been gradually and consistently reducing its energy losses (both technical and commercial) through improved commercial management and a comprehensive network renovation and expansion plan. In year 2000 total losses were as low as 13.5%. However, the 2002-2003 economic crisis caused this figure to rise, reaching 19.5% in 2004. Both commercial and technical losses were affected by the economic crisis. Customers first reduced consumption and later on stopped paying bills, increasing bad debt and disconnection cases. Irregular connections and metering tampering rose as users sought to avoid service interruption (in Montevideo's marginal areas, illegal consumption reached 8.3%). Starting in July 2004, UTE launched a campaign to identify cases of fraud and raise consumer awareness, leading to a reduction in total losses from 19.5% in 2004 to 17.1% in 2006 (see figure 22). Total commercial losses were reduced from 10% in January 2005 to 7.7% in 2006. Except in marginal areas, commercial losses were further reduced to 3.3% in the same year. UTE is currently testing a pilot project in five marginal neighborhoods of Montevideo with the participation of public educators to work with the communities and promote an efficient use of energy. If the pilot is successful, it will be replicated in other marginal areas where losses are high.

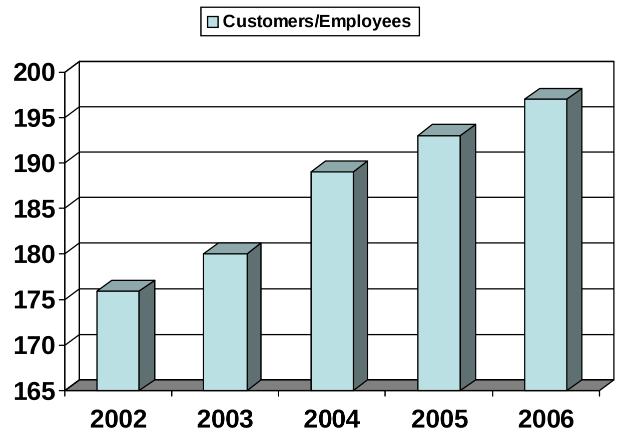
Figure 22: Total Losses (%) – Technical and Commercial



Source: World Bank (2007) Eficiencia en Infraestructura Productiva y Provisión de Servicios en Uruguay

As in other public utilities, UTE's labor productivity continued to improve in the last five years as a result of a gradual reduction and a better use of its labor force. Total staffing has been reduced from 6,760 in 2002 to 6,265 in 2006, while the customers per employee ratio has improved from 176 to 197 in during the same 4 years (see figure 23).

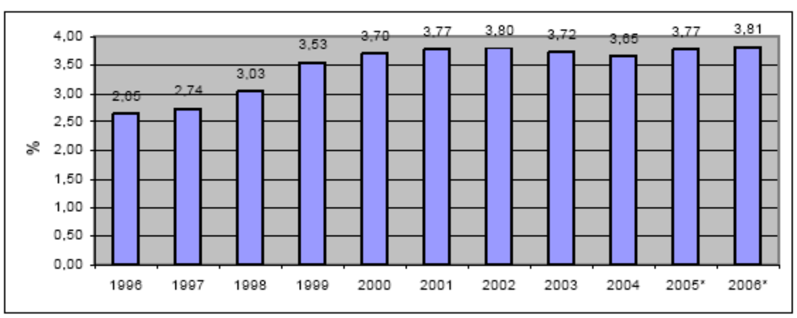
Figure 23. Labor Productivity in UTE (2002-2006)



Telecommunications

The telecommunication sector has steadily increased its volume of activity and contribution to the GDP which amounted to 3.81% in 2006 (the highest in 11 years). Whilst the sector still maintains a monopoly in the provision of fixed lines telephony for urban and national calls by ANTEL, competition has been introduced in the mobile telephony, international fixed telephony, internet and data transmission and cable TV markets. As well as a reduction in prices discussed in the next section, increased competition has contributed towards an increase in efficiency, quality and coverage of the services and overall sector performance.

Figure 24: Contribution of the Telecommunications Sector to GDP (%)



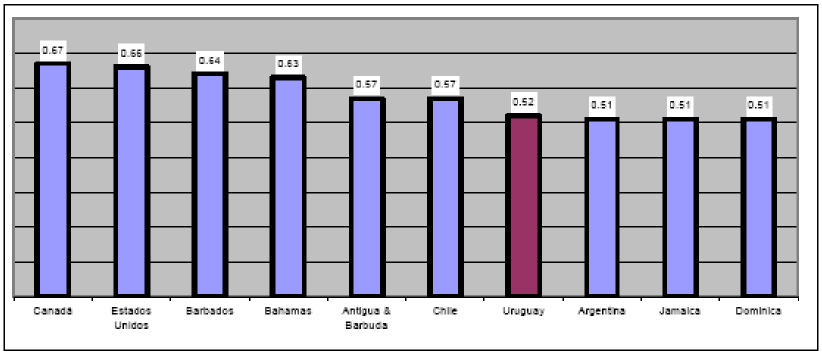
Source: URSEC

Improvement in the overall performance of the sector can be measured by the evolution of the Digital Opportunity Index (DOI)[14] which is based upon different groups of indicators and categories of targets/objectives. It is built upon three categories:

[14] The index was designed by the International Union of Telecommunications in June 2005.

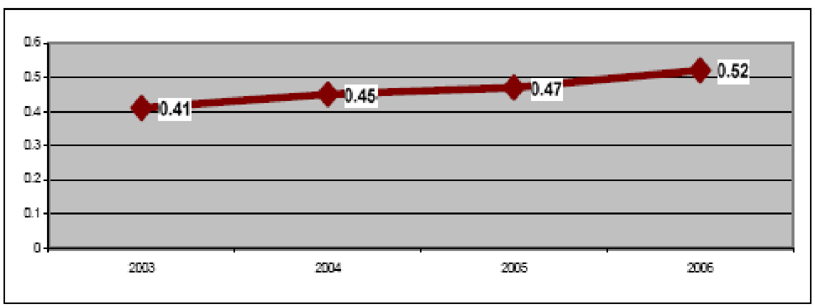
Opportunity (coverage and tariffs), Infrastructure and Utilization. Uruguay's DOI for 2006 was 0.52, one of the highest in the region. The index has positively evolved in the period 2003-2006, mainly due to increases in the categories of Infrastructure and Utilization. The first is driven by the increase in the volume of services of mobile telephony whilst the growth of internet access would account for the rise in the Utilization category, both correlated to increased competition.

Figure 25: Ranking of top 10 countries with the highest digital opportunity index in the Americas



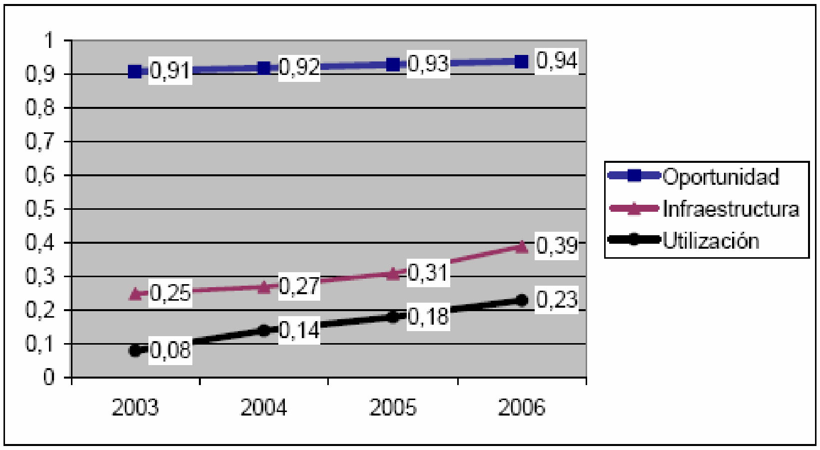
Source: URSEC

Figure 26: Evolution of the Digital Opportunity Index (DOI) in Uruguay (2003-2006)



Source: URSEC

Figure 27: Evolution of the Categories of the Digital Opportunity Index (DOI) in Uruguay from 2003 to 2006



Source: URSEC

Water and Sanitation

Improved regulation, performance benchmarking, along with the SAL's efforts at the macro-economic level to support Uruguay's recovery, have contributed to OSE's improved financial health and efficiency gains. The deep recession of 2001-2003 weakened OSE's financial situation. The steep depreciation of the Uruguayan Peso increased the burden of OSE's debt and payment obligations. Its tariffs decreased in real terms losing its margin to operating costs. The end result was deterioration in OSE's financial and operational indicators. The stabilization of the economy after 2004 improved OSE's financial results: debt structure improved as well as operating cost to revenue ratios.

OSE made some steady efficiency gains since 2002 and has fully recovered from the financial crisis. Key commercial and operational efficiency indicators have improved (see Table 8). Between 2002 and 2006, OSE successfully increased labor productivity from 5.4 employees/1000 connections to 4.3, decreased operating costs from US$ 0.98/m3 to US$ 0.81/m3; and increased operating margins from 37% to 43%. Collection rates also recovered rapidly, from a low of 87% in 2003 to 93% in 2006 (Figure 28). Revenues increased 6% in real terms, given that a real loss of 4% in tariffs[15] was offset by a 12% increase of volume of water billed. Additionally operating costs decreased 3% in real terms which helped to improve financial results (see Table 9).

[15] The calculation was made for the average tariff of water and sewerage

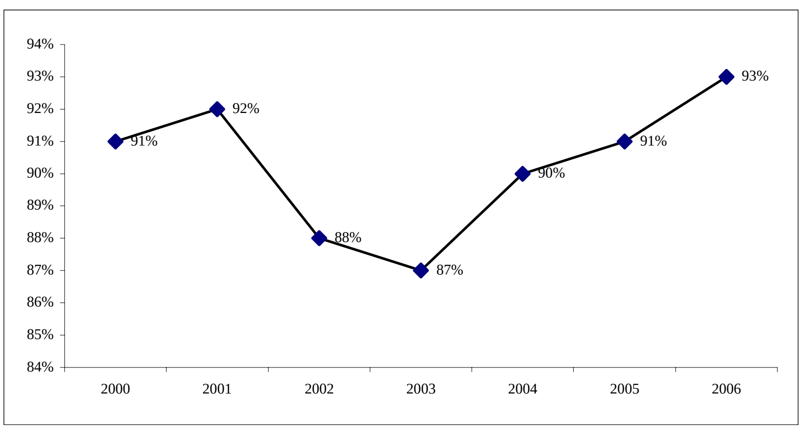
Table 8: Commercial and Operational Efficiency

Commercial Efficiency	***2000***	***2001***	***2002***	***2003***	***2004***	***2005***	***2006***[e]
Accounts receivable comparator (days)	59	66	65	59	49	60	60
Revenue Collection rate	91%	92%	88%	87%	90%	91%	93%
Bad debts/operating revenue	9%	3%	15%	12%	12%	6%	6%
Operational Efficiency	***2000***	***2001***	***2002***	***2003***	***2004***	***2005***	***2006***[e]
Unaccounted for water (UFW)	49.5%	50.8%	52.1%	52.4%	54.1%	54.7%	56.8%
Micro-metering (%)	94.9%	96.2%	97.0%	97.0%	96.4%	96.7%	97.5%
Personnel Costs/Operating costs	57%	58%	54%	50%	49%	46%	46%
Employees/1000 water & sewerage connections	5.7	5.5	5.4	5.2	4.9	4.3	4.2

Table 9. Indicators of Cost Recovery

	2000	***2001***	***2002***	***2003***	***2004***	***2005***	***2006***[e]
Operational Margin	36%	36%	37%	38%	38%	41%	43%
Net Income margin	0%	0%	-64%	-5%	9%	16%	12%
Operating ratio (Operating costs (with dep)/ op revenue)	75%	76%	77%	75%	75%	71%	69%
Working ratio (Operating costs (w/o dep)/ op revenue)	64%	64%	63%	62%	62%	59%	57%
% Investment financed with own sources	14%	62%	52%	46%	9%	64%	74%

Figure 28: OSE Collection Index (2000-2006)



Source: OSE

Other important operational and commercial efficiency gains are directly attributable to OSE's performance indicator benchmarking initiative. This initiative, supported by the SAL, compares the utility's performance across regions based on 8 service quality indicators and then disseminated the results both internally and publicly (including directly to the regulator). This benchmarking exercise promoted efficiency gains, by shifting a deeply entrenched public company culture and promoting transparency; the harmonization of systems and processes (e.g. removed double counting of consumer complaints); better consumer service (e.g. reduced waiting times); improved collaboration between traditional commercial and operational silos (e.g. reduced average re-connection time to the network); and more results-based decision-making. OSE has also made efforts to prioritize investments more strategically and efficiently (e.g., OSE commissioned a comparative feasibility analysis to prioritize sanitation works across the 75 Uruguayan cities).

OSE's operational efficiency remains hindered by high rates unaccounted for water (UFW) – which increased from 52% to around 57% from 2002 to 2007. OSE's efforts to award a performance based contract for reducing UFW in Montevideo, supported by the SAL, were stalled following the 2004 Constitutional Amendment. Nevertheless, OSE's new well functioning UFW unit has successfully helped reshape OSE's strategic visioning of the issue, enabling OSE to tackle UFW more holistically, across the traditional engineering/commercial institutional divide and to provide a hot-bed for testing and rolling-out innovative approaches – including successful new financial incentive systems (the meter replacement rate has now almost quadrupled since 2002). It has been widely recognized that addressing UFW is a complex long-term issue, which will be the focus of the second phase of the World Bank *OSE Modernization and Systems Rehabilitation* APL, approved by the Board in June 2007.

The OSE APL2 Project envisages a total investment of US$ 68 million in the rehabilitation and improvement of water treatment facilities, reduction of non-revenue water and increased sewerage service coverage. With this significant investment and the commitment to further reforms under the agreement with the Bank, OSE is undergoing one of the countries' most drastic transformations in public utilities, as was recently declared in the press by the Director of the Budgeting and Planning Office.[16]

Transport

Greater competition and outsourcing practices in road maintenance and management of the road infrastructure has produced significant improvements in performance. In fact, competition has introduced the concept of results-based performance for all public sector and private activities. For example, MTOP's transfers to the Departments to maintain their road networks are based on their performance and include incentives towards achieving the targets. Although the roads sector was not explicitly included as part of loan conditionality, it is also worth mentioning that MTOP has fully complied with the Roads maintenance and rehabilitation plan and the sector allocation budget from 2002 to 2005. The number of DNV employees was reduced from 3,700 in 1995 to 1,800 in 2004, which is an illustration of the shift in responsibilities of DNV, from carrying out 100 percent of road maintenance to one that formulates policy and regulates and controls the private and public sector enterprises that provide these services today**.** Currently, 42 percent of the road network managed by the DNV is maintained through contracts with the private sector under different modalities: performance-based contracts, micro enterprises, Contracts for Rehabilitation and Maintenance (CREMA); and road concessions. The concession of 1,200 km of the national roads to a special purpose

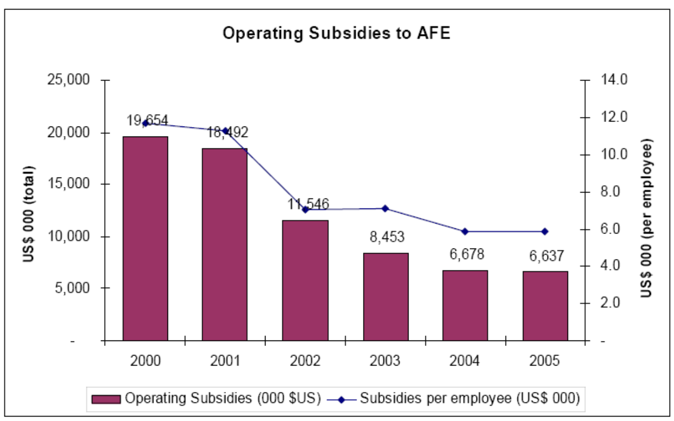
[16] *Crónicas Económicas,* October 2007

institution (*Corporación Vial del Uruguay*) has stood for 25 years and still continues, allowing private sector financing to be raised for 1,200 km road network.

With regards to the railroad subsector, in spite of the absence of a regulatory framework, AFE improved its efficiency between 2000 and 2005, and operating subsidies have significantly decreased. As shown in Figure 29, operating subsidies to AFE (and DNV) decreased by 66 percent from US$19.6 million in 2000 to US$6.6 million in 2005. During the same period, the number of employees decreased from 1,677 to 1,128 through a voluntary retirement scheme. This allowed AFE to improve its operating performance and play a bigger role in 2005 than it did in 2002, when the labor reform took place and railways operation was separated from infrastructure. Between 2002 and 2005, operating expenses as a ratio of operating revenues decreased from 4.2 to 2.0. At the same time, freight transportation increased by 60 percent from 822,700 tons to 1,318,000.

Reforms initiated in the late 1990s to improve the operational efficiency in **ports** were continued during the SAL implementation period. Consequently, the sector has achieved higher levels of operational efficiency. Cargo traffic and productivity has increased. Ship turn-around and docking times have decreased, tariffs have been reduced, and investment in port infrastructure and service provision has increased. Montevideo is again a preferred port of call for mainline services.

Figure 29: Operating Subsidies to AFE



Source: WB staff calculation