

**COLOMBIA**

**SOCIAL EMERGENCY PROGRAM**

**(CO-0268)**

**LOAN PROPOSAL**

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## BASIC SOCIOECONOMIC DATA

For basic socioeconomic data, including public debt information, please refer to the following address:

**English:**

<http://www.iadb.org/RES/index.cfm?fuseaction=externallinks.countrydata>

**Spanish:**

<http://www.iadb.org/RES/index.cfm?fuseaction=externallinks.countrydata>

## ABBREVIATIONS

|            |  |
|------------|--|
| ADC        | Andean Development Corporation               |
| CONFIS     | Supreme Fiscal Policy Council                |
| CONPES     | Economic and Social Policy Council           |
| DAPR       | Administrative Department of the Presidency  |
| DNP        | National Planning Department                 |
| FAEP       | Petroleum Stabilization Fund                 |
| FOGAFIN    | Financial Institution Guarantee Fund         |
| GDP        | Gross domestic product                       |
| HCB        | Community Welfare Home                       |
| HPE        | Health-promoting entity                      |
| HRM        | Health risk manager                          |
| ICBF       | Colombian Family Welfare Institute           |
| IMF        | International Monetary Fund                  |
| IPS        | Health Service Provider                      |
| ISS        | Social Security Institute                    |
| MEN        | National Education Ministry                  |
| MHCP       | Ministry of Finance and Public Credit        |
| MPS        | Ministry of Social Protection                |
| NFPS       | Non-financial public sector                  |
| PAB        | Basic Healthcare Plan                        |
| PAI        | Expanded Immunization Program                |
| PGN        | General National Budget                      |
| PSP        | Protected social program                     |
| RAS        | Social Support Network                       |
| RSS        | Social Solidarity Network                    |
| SGSSS      | General System of Social Security for Health |
| SIIF       | Integrated Financial Information System      |
| SISBEN     | Beneficiary Identification System            |
| SPS        | Social Protection and Security System        |
| SUH        | Single Accreditation System                  |
| SuperSalud | Superintendency of National Health           |
| UNDP       | United Nations Development Programme         |



## COLOMBIA

### IDB LOANS

APPROVED AS OF DECEMBER 31, 2003

|                                       | <i>US\$Thousand</i> | <i>Percent</i> |
|---------------------------------------|---------------------|----------------|
| <b>TOTAL APPROVED</b>                 | <b>8,827,767</b>    |                |
| DISBURSED                             | 7,906,901           | 89.6%          |
| UNDISBURSED BALANCE                   | 920,866             | 10.4%          |
| CANCELLATIONS                         | 936,719             | 10.6%          |
| PRINCIPAL COLLECTED                   | 4,210,941           | 47.7%          |
| <b>APPROVED BY FUND</b>               |                     |                |
| ORDINARY CAPITAL                      | 8,012,826           | 90.8%          |
| FUND FOR SPECIAL OPERATIONS           | 754,656             | 8.5%           |
| OTHER FUNDS                           | 60,285              | 0.7%           |
| <b>OUTSTANDING DEBT BALANCE</b>       | <b>3,695,960</b>    |                |
| ORDINARY CAPITAL                      | 3,492,888           | 94.5%          |
| FUND FOR SPECIAL OPERATIONS           | 202,814             | 5.5%           |
| OTHER FUNDS                           | 258                 | 0.0%           |
| <b>APPROVED BY SECTOR</b>             |                     |                |
| AGRICULTURE AND FISHERY               | 557,166             | 6.3%           |
| INDUSTRY, TOURISM, SCIENCE TECHNOLOGY | 509,844             | 5.8%           |
| ENERGY                                | 2,697,554           | 30.6%          |
| TRANSPORTATION AND COMMUNICATIONS     | 709,816             | 8.0%           |
| EDUCATION                             | 85,820              | 1.0%           |
| HEALTH AND SANITATION                 | 742,773             | 8.4%           |
| ENVIRONMENT                           | 130,835             | 1.5%           |
| URBAN DEVELOPMENT                     | 403,067             | 4.6%           |
| SOCIAL INVESTMENT AND MICROENTERPRISE | 1,087,805           | 12.3%          |
| REFORM PUBLIC SECTOR MODERNIZATION    | 1,868,720           | 21.2%          |
| EXPORT FINANCING                      | 0                   | 0.0%           |
| PREINVESTMENT AND OTHER               | 34,367              | 0.4%           |

\* Net of cancellations with monetary adjustments and export financing loan collections



INTER-AMERICAN DEVELOPMENT BANK  
Regional Operations Support Office  
*Operational Information Unit*

# COLOMBIA

## STATUS OF LOANS IN EXECUTION AS OF DECEMBER 31, 2002

(Amounts in US\$ thousands)

| APPROVAL PERIOD               | NUMBER OF PROJECTS | AMOUNT APPROVED *  | AMOUNT DISBURSED   | % DISBURSED   |
|-------------------------------|--------------------|--------------------|--------------------|---------------|
| <b><u>REGULAR PROGRAM</u></b> |                    |                    |                    |               |
| Before 1996                   | 8                  | 330,610            | 274,468            | 83.02%        |
| 1996 - 1997                   | 7                  | 241,944            | 184,387            | 76.21%        |
| 1998 - 1999                   | 6                  | 126,461            | 39,191             | 30.99%        |
| 2000 - 2001                   | 5                  | 1,093,000          | 671,286            | 61.42%        |
| 2002                          | 3                  | 100,700            | 910                | 0.90%         |
| <b>TOTAL</b>                  | <b>29</b>          | <b>\$1,892,715</b> | <b>\$1,170,243</b> | <b>61.83%</b> |

\* Figures are net of cancellations. Excludes export financing loans



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Operational Information Unit

## Colombia

### Tentative Lending Program

2003

| Project Number          | Project Name                                      | IDB US\$ Millions | Status |
|-------------------------|---|-------------------|--------|
| CO0268                  | Social Emergency Program                          | 1,250.0           |        |
| CO0258                  | Attorney General's Office Support & Strengthening | 14.0              |        |
| CO0139                  | Health Services Networks Modern. Prog.            | 100.0             |        |
| CO0265                  | Fiscal Sustainability                             | 400.0             |        |
| CO0266                  | Public Service Renewal Program                    | 70.0              |        |
| CO0241                  | Social Housing Program                            | 100.0             |        |
| CO0267                  | Environmental Sanitation of Bogota - Phase I      | 50.0              |        |
| Total - A : 7 Projects  |   | 1,984.0           |        |
| CO0263                  | Infrastructure Privatization and Concessions II   | 30.0              |        |
| *CO0259                 | Electrocaribe/Electrocosta                        | 22.5              |        |
| Total - B : 2 Projects  |   | 52.5              |        |
| TOTAL 2003 : 9 Projects |   | 2,036.5           |        |

2004

| Project Number            | Project Name                                  | IDB US\$ Millions | Status |
|---------------------------|---|-------------------|--------|
| CO0262                    | National Environmental System Support Program | 35.0              |        |
| CO0250                    | National Water Plan                           | 60.0              |        |
| Total - A : 2 Projects    |   | 95.0              |        |
| TOTAL - 2004 : 2 Projects |   | 95.0              |        |

Total Private Sector 2003 - 2004 22.5  
Total Regular Program 2003 - 2004 2,109.0

\* Private Sector Project

## SOCIAL EMERGENCY PROGRAM

(CO-0268)

### EXECUTIVE SUMMARY

|  |  |  |
|--|--|--|
| <b>Borrower:</b>                       | Republic of Colombia   |  |
| <b>Executing agency:</b>               | Ministry of Finance and Public Credit (MHCP)   |  |
| <b>Amount and source:</b>              | IDB (OC - Emergency Lending Facility):   | US\$1.25 billion   |
|  | Total:   | US\$1.25 billion   |
| <b>Financial terms and conditions:</b> | Amortization:  | 5 years  |
|  | Grace period:  | 3 years  |
|  | Disbursement:  | 12 months  |
|  | Interest rate:   | Six-month LIBOR in US dollars + 400 basis points per year. |
|  | Inspection and supervision:  | 1%   |
|  | Credit fee:  | 0.75%  |
|  | Currency:  | US dollars drawn from the Single Currency Facility         |
| <b>Objectives:</b>                     | The objectives of this program are to assist the government in maintaining macroeconomic and fiscal stability; to mitigate the potential effects of fiscal tightening and the economic and social crisis on population groups living in extreme poverty; and to prevent delays in implementing ongoing reforms in the social sector.   |  |
| <b>Description:</b>                    | Program disbursements will be conditional on actions in three areas: (i) agreement on a program with the International Monetary Fund (IMF) and putting it into effect; (ii) budgetary protection and monitoring of the execution of programs chosen because they target the poorest groups, and for their importance in mitigating the effects of the armed conflict; and (iii) support for continued implementation of ongoing social sector reforms. The program contains the following components: (i) agreement on a program with the IMF and putting it into effect; (ii) protection of priority social programs; and (iii) support for continued implementation of reforms in education, health and targeting. |  |



**The Bank's country and sector strategy:**

The *Bank's strategy for Colombia*, currently under preparation, establishes three fundamental objectives on which the Bank's actions in the country during 2003-2006 are premised: (i) to lay foundations for sustainable economic growth; (ii) to promote social development and ensure protection for the most vulnerable groups; and (iii) to promote the presence of efficient State institutions in national territory, and improve governance. Accordingly—in view of the Stand-by Arrangement with the IMF and market access restrictions—the Bank will use this emergency operation to support Colombia's financing needs and reforms aimed at eliminating fiscal imbalance. In terms of the fundamental areas of the Bank's country strategy, this operation will mainly contribute towards objective (ii). Firstly, it will support the most needy sectors and victims of the armed conflict; secondly, progress in ongoing reforms in education, health and targeting will help provide financially sustainable social services that are more effective in covering the population's needs and more resource-efficient. In addition, the protection of human capital investment raises the growth potential of the economy, thereby supporting objective (i).

**Coordination with other multilateral agencies:**

Support for Colombia, both in financing and in implementing reforms, is being closely coordinated between multilateral agencies and the Colombian government. The Stand-by Arrangement with the IMF serves as a reference framework for this support, which involves a financial commitment amounting to US\$7.349 billion approved for 2003-2006. Of this amount, approximately US\$4.2 billion would be in the form of fast disbursing loans (55% to be approved in 2003).

Financial support is complemented by the reforms being pursued by each body. In 2003, given the priority to reduce rigidities in expenditure and curtail the growth thereof, the IDB is providing support for the reform of government spending (pension reform, reform of the State, hospital rationalization, restructuring of the Social Security Institute (ISS)), while the World Bank is concentrating on budgetary management and greater rationalization of tax revenues. Also during 2003, both institutions are supporting government efforts to revive the economy, either through greater labor market flexibility (World Bank) or by supporting the housing sector (IDB). In subsequent years, the emphasis is likely to be placed on supporting economic growth and pressing ahead with reforms involving the judiciary and a second stage of State restructuring.

**Environmental and social review:**

Given its special characteristics, the program does not entail physical or any other type of investments, so it is not expected to have a direct environmental impact. In terms of social impact, the program

is intended to mitigate the effects of the fiscal adjustment and the armed conflict on population groups living in extreme poverty, thereby helping to alleviate poverty in the context of the emergency.

The programs to be protected have a major impact on the conditions of life of women and other high-risk groups. These include: the Social Support Network, the Social Solidarity Network, the Beneficiary Identification System (SISBEN) and the Colombian Family Welfare Institute (ICBF). In addition, reforms to enhance the efficiency of education and health services will benefit most of the population, but particularly people living in extreme poverty. Indigenous and Afro-Colombian groups are also important in several of the programs selected for protection in this operation.

|  |   |
|--|---|
| <b>Benefits:</b>   | One of the main objectives of this program is help the Government of Colombia maintain macroeconomic and fiscal stability, avoiding the adverse effects of imbalances on the population in general and vulnerable groups in particular. Budgetary protection and guaranteed execution of protected social programs (PSPs) will make it possible to avert a further worsening of the situation of the most vulnerable population groups —already badly affected by the 1998-99 crisis and by the civil conflict and its aftermath. By strengthening social reforms it will be possible to ensure that key actions for the sustainability and efficiency of social spending do not get postponed. |
| <b>Risks:</b>  | This program is subject to the following risks: (a) non-fulfillment of targets for resource transfers to PSPs, due to execution problems in the entities responsible for them; (b) implementation of the fiscal adjustment measures and structural reform program may proceed more slowly than expected; and (c) Colombia's public debt may become unsustainable (see paragraphs 4.5-4.9).  |
| <b>Special contractual clauses:</b>                        | The release of funds in each tranche will be conditional on fulfillment of the agreed policy measures, as specified in chapter II and in Annex I of this loan document.   |
| <b>Poverty-targeting and social sector classification:</b> | Since this is an emergency operation, it does not classify as a social equity-enhancing project, as described in the indicative targets mandated by the Bank's Eighth Replenishment (document AB-1704). The operation also does not qualify as a poverty-targeted investment.   |
| <b>Exceptions to Bank policy:</b>                          | None.   |
| <b>Procurement:</b>  | Not applicable.   |

## **I. BACKGROUND**

- 1.1 On taking office in August 2002 after winning the presidential elections in the first round of voting, the administration of Alvaro Uribe Velez had to address the economic and social effects of prolonged economic stagnation and an unprecedented resurgence of the domestic armed conflict. In response to these challenges, the new government defined an alternative strategy to subdue the civil conflict, and it prepared a structural reform plan aimed at reining in the fiscal deficit and reviving economic growth. These policies have started to have a favorable impact on the Colombian economy and on expectations among the population at large. The strategy, backed by the International Monetary Fund (IMF), forms the basis for a coordinated effort by multilateral agencies to support the country in achieving its objectives.

### **A. Macroeconomic and fiscal situation**

- 1.2 Since the second half of the 1990s, the Colombian economy has slowed down significantly. Growth in per capita gross domestic product (GDP) dropped from an average of 2.3% per year between 1985 and 1994, to -1.1% between 1995 and 2002. This pattern has been repeated in many Latin American countries, and is partly the result of factors extraneous to the region—mainly turbulence on international financial markets which has caused capital flows to dry up. In particular, Colombia has been affected by financial contagion from other countries in the region, and by the collapse of international coffee prices.
- 1.3 External and internal shocks have contributed to a deterioration of fiscal accounts in recent years, stemming from expenditure growth, the transitory nature of current income, and increasing difficulties in obtaining alternative financing sources. The substantial rise in spending is the result of a transformation of the Colombian State. Firstly, government made a major effort to partially honor its “social debt”, by substantially increasing the transfers paid to territorial bodies to finance education and health services. Secondly, following the passing of Law 100, pension payments were made explicit in government finances, and the corresponding rates were raised substantially. In the third place, central government operating expenditures grew sharply because of wage hikes. Lastly, the intensification of the internal armed conflict generated an increase in defense spending. As a result of these rising trends, operating and investment expenditure by the non-financial public sector (NFPS) doubled in the space of 10 years, rising from 16.8% of GDP in 1990 to 33.5% in 2001 (excluding debt service). A major problem in economic-policy management is that a large proportion of expenditure items have become rigid components: in the 2003 budget, up to 80% of expenses are classified as “inflexible”.
- 1.4 In terms of financing sources, tax revenues have been unable cover expenses since 1995, forcing the government to implement six tax reforms in a ten-year period, in order to increase revenues. Growing expenditure of a permanent nature was mainly

financed by transitory tax resources, and these became insufficient as from 1995. As a result, the fiscal deficit grew from 0.3% of GDP in 1995 to 5% in 1999 and 4.1% in 2002. Between 1996 and 2001, the total NFPS debt grew from 22.9% of GDP to 47.7%. Over half of this increase resulted from a real depreciation of the Colombian peso and a rise in domestic interest rates.

- 1.5 To summarize, the Colombian economy has grown at relatively modest rates in recent years, and for 2003 growth is projected to be moderate (between 2% and 2.5% of GDP). The fiscal domain suffers from the following problems: (i) a high percentage of inflexible and growing expenditure; (ii) flat current revenue that does not make it possible to reduce the deficit below 4%; (iii) limited access to domestic and external financing; and (iv) a repayment profile that could seriously undermine the future sustainability of the debt. In 2003, the Colombian public sector has to make payments of principal and interest totaling about US\$4 billion, of which 25% corresponds to the Bank. This situation could worsen unless the proposed reforms are swiftly applied, since fiscal and debt instability would put strong pressure on expenditure, including social investment.
- 1.6 The government has acted on two fronts to resolve this situation: firstly, introducing a series of reforms aimed at cushioning the growth of rigid expenditures and overcoming the transitory nature of revenues; and secondly resolving the problem of short-term financing to enable the country to continue servicing its debt. The Stand-by Arrangement with the IMF, described below, encompasses this set of actions.

## 1. The program with the IMF

- 1.7 The US\$2.2 billion Stand-by Arrangement with the IMF was approved in January 2003 and will serve as a macroeconomic policy framework for the next two years. The program is premised on conservative assumptions regarding economic recovery, including modest growth rates of 2% in 2003 and 3.3% for the following year. Targets for growth, inflation, external current account and fiscal deficits are shown in table I-1.

**Table I-1**  
**Stand-by Arrangement Targets**

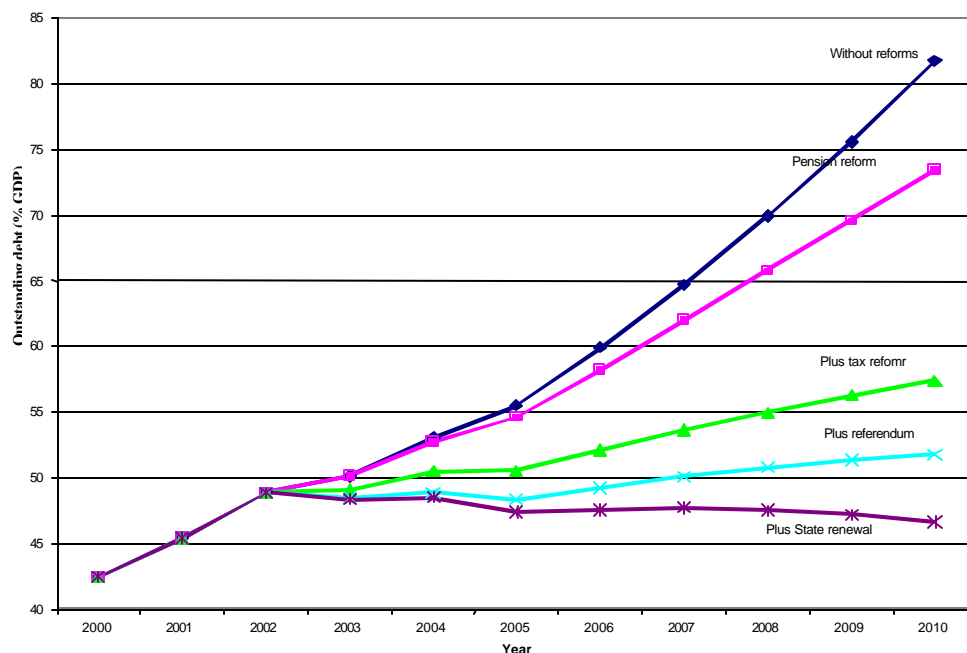
|                                       | 2002 | 2003 | 2004 |
|---------------------------------------|------|------|------|
| <b>Annual percentage variation</b>    |      |      |      |
| Real GDP                              | 1.6  | 2.0  | 3.3  |
| Inflation                             | 6.0  | 5.5  | 4.0  |
| <b>As a percentage of GDP</b>         |      |      |      |
| Current-account deficit               | -1.7 | -0.8 | -1.6 |
| Deficit of consolidated public sector | -4.0 | -2.5 | -2.1 |

- 1.8 *Monetary policy* will continue to be cast within an inflation-targeting floating exchange-rate regime. Inflation targets for 2003 and 2004 have been set at 5.5% and 4% respectively, although the planned increase in value added tax is expected to cause a transitory rise in inflation in 2003. The Banco de la República has set a quarterly path for inflation consistent with its annual target, and will review any significant divergence with the IMF. Growth of the monetary base is expected to slow, and the money supply will expand in line with nominal GDP.
- 1.9 In the *fiscal policy* domain, the recently approved tax reform has a key role to play in reducing the deficit, mainly by controlling evasion and expanding the tax base. The reform is expected to increase revenue by 1.6% of GDP in 2003 and 1.2% in 2004. In terms of expenditure control, the immediate measure of greatest impact involves freezing operating expenses at the territorial government level for two years (2003 and 2004), subject to approval in a national referendum to be held in mid-2003. This temporary measure is expected to generate savings of 0.7% of GDP in 2003 and 1.42% in 2004.
- 1.10 These short-term measures to expand tax revenue and curb spending are supported by a series of *sustained structural reforms* aimed at reducing the rigidity of expenditure and consolidating the fiscal situation. These include: the pension reform already approved; amendment of the Budget Law (making it possible to increase the flexibility of expenditure and improve fiscal administration); the State modernization program; reform of civil service regulations; reform of the Law on Contracting (Law 80); the Fiscal Transparency and Accountability Law currently before Congress (which establishes fiscal rules for national and territorial governments); and modernization of the health service network system, particularly public hospitals that currently account for the largest proportion of the territorial deficit.
- 1.11 The fiscal adjustment measures and structural reforms are expected to cut the deficit by 1.9% of GDP in 2003 and 2.2% in 2004.<sup>1</sup> The impact on debt up to 2010 is shown in figure I-1. It is important to highlight the magnitude of saving generated by the measures contained in the referendum.

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<sup>1</sup> Assuming a permanent increase in defense spending of 0.6% of GDP.

**Figure I-1**  
**Outstanding debt of the non-financial public sector (% GDP)<sup>2</sup>**



## 2. Government financing program for 2003-2004

- 1.12 *Domestic borrowing.* Net borrowing by the public sector will allow for adequate private-sector access to domestic credit, and is projected to decline from 3.1% of GDP in 2002 to 2.3% in 2003 and 1.7% in 2004. This will help stimulate economic recovery and prevent undue upward pressure on domestic interest rates.<sup>3</sup> Of total financing needs, the appropriate level of domestic borrowing will be determined through quarterly reviews with the IMF. As established in the Stand-by Arrangement, the government will not seek funding from the Banco de la República, unless major exogenous events restrict other funding sources, and then only if the program with the IMF is being successfully implemented.
- 1.13 *External financing.* The public-sector external financing program for 2003 is assured. Given limited access to institutional financial markets during much of 2002, the government sought increased support from multilateral agencies. For 2003, disbursements totaling US\$2.793 billion are scheduled from the IDB, the World Bank and the Andean Development Corporation (ADC) (see table I-2). In 2003, the Bank would provide financing in the amount of US\$1,410 million in

<sup>2</sup> Source: MHCP, CONFIS, 2003.

<sup>3</sup> Given the recent behavior of financial saving and low domestic credit demand, there is little risk of upward pressure on interest rates or of the private sector being “crowded out” during 2003.

freely available resources. This sum includes a disbursement of US\$750 million under the present program, US\$410 million in disbursements for sector loans (1381/OC-CO and 1335/OC-CO; see Annex V for a description), and US\$250 million under the fiscal sustainability program (CO-0261) now in preparation. In addition, the government has already sold US\$500 million of bonds it had earmarked for this year. Although no further access to international financial markets is envisioned for 2003, there is the possibility of pre-funding 2004 should opportunities arise in the market. Nonetheless, the public sector, including its financial segment, will restrict its net external borrowing to US\$950 million in 2003, as specified in the Technical Memorandum of Understanding with the IMF. The government is expected to deposit any net external borrowing in excess of this amount in its accounts abroad, for use in funding the 2004 budget.

**Table I-2**

| <b>Sources and uses of GNC financing - 2003</b> |              |                      |                  |
|---|--------------|----------------------|------------------|
|   |              |                      | <b>US\$ mill</b> |
| <b>Sources</b>                                  | <b>9,754</b> | <b>Uses</b>          | <b>9,754</b>     |
| <b>Disbursements</b>                            | <b>7,695</b> | <b>Deficit</b>       | <b>3,953</b>     |
| <b>External</b>                                 | <b>3,331</b> | <b>Amortization</b>  | <b>5,234</b>     |
| Bonds   | 541          | External             | 2,403            |
| Multilateral                                    | 2,793        | Domestic             | 2,831            |
| Not specifically assigned                       | 2,570        |                      |                  |
| IDB   | 1,410        |                      |                  |
| WB  | 960          |                      |                  |
| ADC   | 200          |                      |                  |
| Specifically assigned                           | 220          |                      |                  |
| <b>Domestic</b>                                 | <b>4,364</b> |                      |                  |
| Agreed  | 1,825        |                      |                  |
| Auctions  | 1,894        |                      |                  |
| Forced  | 551          |                      |                  |
| Short-term TES                                  | 30           |                      |                  |
| <b>Other</b>                                    | <b>64.6</b>  |                      |                  |
| <b>Adjustments for accruals</b>                 | <b>85</b>    |                      |                  |
| <b>Banco República profits</b>                  | <b>512</b>   | <b>Floating debt</b> | <b>567</b>       |
| <b>Use of portfolios and other resources</b>    | <b>1,462</b> |                      |                  |

Source: CONFIS

- 1.14 Accordingly, the Bank needs to complement IMF support for rapid and effective implementation of the reform program. Short-term financial support through an emergency loan is premised on two fundamental objectives. The first is to counteract negative shocks—both external (deterioration of the terms of trade) and domestic (intensification of the armed conflict)—which undermine the country's fiscal and financial sustainability. The second is to counteract short-term negative social effects that could be aggravated by the fiscal reforms. Contributing to social stability is an essential complement to the sustainability of fiscal reforms.

## **B. The social situation**

- 1.15 The prolonged recession and armed conflict have caused welfare indicators to deteriorate among the population at large and especially in the poorest sectors. Moreover, the adjustment needed to achieve fiscal balance could have major effects on the most vulnerable population groups, which rely on government social programs.

### **1. Poverty and inequality**

- 1.16 As a result of the growth slowdown and rise in unemployment, particularly among women and young people, poverty and inequality have increased and other indicators of the quality of life have deteriorated. The poverty rate currently surpasses levels seen a decade ago, with the most recent 2002 estimates putting it above 65% of the total population.<sup>4</sup> Figures for 1996-2000 show family incomes in freefall—sliding in real terms by 33.1% in the poorest segments of the income distribution (deciles 1-3) and by 21.1% in deciles 4-7. This is particularly accentuated in the case of workers with only primary education or none at all. The fall in income levels mainly reflects lower labor earnings as a result of unemployment. Inequality has also increased for the same reasons, and because of an unprecedented increase in the total demand for skilled workers throughout the economy during the second half of the decade. The economic crisis, together with the precarious nature of social protection mechanisms, has forced many poor families to sell productive assets and interrupt their investments in human capital (school attendance, consumption of nutritious food, etc.). This can be expected to affect the quality of life of this population segment far beyond the current situation.<sup>5</sup>

### **2. Internal armed conflict and displacement**

- 1.17 The civil conflict has substantial effects on the civil population and its welfare, including the forced displacement of people, which aggravates vulnerability, poverty and social exclusion among the affected groups. The available information suggests that the main causes of displacement are generalized threats (50%), armed confrontations (9%), massacres (7%), specific threats (29%), municipal occupations (2%) and other indiscriminate attacks on the population. Gauging the size of internal displacement is difficult because the available figures contain

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<sup>4</sup> The results of a household survey in urban areas conducted in the first half of 2002 (Fedesarrollo 2002) reveal falling expectations and a worsening economic situation among households, particularly the poorest, compared to the same period in 2001.

<sup>5</sup> Figures from the National Demography and Health Survey 2000 show that while chronic malnutrition (size for age) decreased slightly between 1995 and 2000, the reduction has been less pronounced among children whose mothers have no education or only primary schooling. Compared to a chronic malnutrition rate of 13.5% among the total under-five population, the rate is 24.1% for children whose mothers have no education, and 18.5% for those whose mothers have completed primary school.



discrepancies. Estimates from the Social Solidarity Network (RSS) suggest that between 1995 and June 2002 about 890,000 people have been displaced, half of them between 2000 and 2002.<sup>6</sup> The displaced population consists mostly of low-income women and children. In terms of ethnic groups, of the total number of displaced people registered with the government between 2000 and 2002, 18% correspond to the Afro-Colombian population and 4% to indigenous groups. These figures exceed the joint representation of the two ethnic groups in the total population of the country (11%).<sup>7</sup> According to the RSS, in 2002 the armed conflict spread, growing worse and causing additional internal displacement and exacerbating the humanitarian crisis of forced displacement.

- 1.18 It has been State policy to return displaced populations to their places of origin, but recent figures show a declining trend in returnees, from 37% in 2000 to 11% in 2002—reflecting the intensity of the civil conflict in recent years. The impossibility of return generates very high demand on available resources for relocation in new settlements; these are usually in large cities where the costs of care and social re-integration run extremely high.

### **3. Social public spending**

- 1.19 Although social spending<sup>8</sup> grew substantially during the 1990s, public expenditure on social assistance programs targeting the most vulnerable population groups has behaved erratically in recent years. Social spending grew from around 8% in 1991 to 13% in 1999 (about 38% of total public spending). Excluding pensions, the figure was 5% of GDP in 1991 and 8.7% in 1999, a level that has been sustained to the present time (2002).<sup>9</sup> Nonetheless, the country has made a major effort to guarantee stable financing in the social sectors, especially education and health. This, together with recent reforms in the education and health sectors (Law 715 of 2001) aimed at making expenditure more efficient, and recent reform of the pension system, have generated a favorable situation for reorganizing sector finances and guaranteeing basic social services.
- 1.20 In contrast to this, in recent years expenditure on social assistance programs targeting people suffering from unemployment, extreme poverty and the effects of the armed conflict has mirrored the weak performance of the economy as a whole.

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<sup>6</sup> Other non-governmental sources suggest a much higher figure.

<sup>7</sup> The government has conducted an analysis of the impact of the civil conflict and displacement on ethnic populations; the corresponding document is available in the program's technical files.

<sup>8</sup> Under the DANE definition, social spending in Colombia covers the following categories: education, public health and social assistance (Social Support Network, Social Solidarity Network, ICBF and other programs caring for old people, children and the disabled), together with social security (pensions and health), housing, potable water supply, sanitation and other social services.

<sup>9</sup> Despite this significant growth, social spending in Colombia is below the Latin American average (US\$884 per capita in Colombia in 1996, versus US\$993 for the region as a whole and US\$1,568 in Mercosur).

The share of social assistance in total social spending remained constant during the first half of the 1990s, before increasing in 1995 and then retreating towards the end of the decade during the recession. During that period, the poverty rate rose by 15%. The low-level of funding for this type of expenditure has caused program coverage rates to shrink, just when they needed to be maintained or expanded to counter the effects of the recession.

- 1.21 In an earlier operation with the Bank—the Social Reform Program (1381/OC-CO) approved in 2001—the government decided to create an institutional mechanism to respond to these challenges in the medium term. This took the form of a social assistance expenditure stabilization fund that would accumulate resources during high growth periods, for release at times of crisis to finance targeted social assistance programs protecting extremely poor households.<sup>10</sup> Nonetheless, in the short run, and in the absence of the robust economic recovery that was expected for 2002, this key expenditure item remains in danger of being cut back to accommodate the need for significant fiscal tightening.

#### **4. Social assistance programs in Colombia**

- 1.22 Social assistance programs simultaneously help to reduce poverty and to protect and enhance the human capital investments of the poorest households and most vulnerable groups, especially at times of crisis. In recent years, Colombia has worked hard to construct a comprehensive social protection scheme, known as the Social Protection and Security System (see annex IV for further details). Implementation of this was a condition of the Social Reform Program (1381/OC-CO), which was approved in late 2001 and fully disbursed in January 2003. The system encompasses the following programs.
- a. The **Social Support Network (RAS)**, which was created with Bank support (loan 1280/OC-CO) to alleviate the impact of unemployment and protect the human capital of families living in extreme poverty. RAS subprograms are: (i) *Employment in Action*, which provides temporary employment for poor and unemployed workers on building sites that require unskilled labor (coverage in 2002: 170,739 jobs); (ii) *Families in Action*, which pays subsidies to families in SISBEN I,<sup>11</sup> to encourage them to invest in the health, education and nutrition of

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<sup>10</sup> Creating this fund required passing a law in Congress. Although the fund was included in the Tax Reform Act in December 2002, the articles finally approved contained amendments to the text originally proposed by the government, which made saving into the fund unviable during 2002-2008 under official economic growth projections. Accordingly, the government has implemented an alternative set of policies to help guarantee permanent funding for social assistance in the medium-term, including increased budget flexibility and greater efficiency in social programs. This should make it easier to reassign resources to social assistance at times of economic crisis (for further information see document PR-2639-1, Report for release of the second tranche and the third floating tranche, and waiver of contractual conditions).

<sup>11</sup> The Beneficiary Identification System (SISBEN) is described in paragraphs 1.35-1.37. The SISBEN I level is equivalent to the poorest quintile in the income distribution.

their children; this attacks the causes of poverty while also providing income support for extremely poor families (coverage in 2002: 325,000 families); and (iii) *Youth in Action*, which provides labor training and skills for young people in SISBEN I and II, through a competitive system (coverage in 2002: 44,658 young people). Until now, IDB- and World Bank-financed RAS programs have kept in sync with the project cycle projected at the design stage. The coverage of the employment and youth subprograms will not be maintained in 2003 because of their management capacity. However, an impact assessment with an experimental or quasi-experimental design that will permit decision making in late 2003 has been conducted under each subprogram in order to determine whether they are effective tools in poverty relief and human capital development, and therefore whether they will be part of ongoing social protection programs.

- b. The **Social Solidarity Network (RSS)**, which provides assistance to populations that have been displaced and affected by violence, as well as to indigent elderly people and ethnic minorities living in the poorest conditions. In 1999-2000, the RSS catered for an annual average of 40,000 displaced households, and 60,000 indigent elderly people. Based on the social reform supported by the program, and financed with the proceeds of the technical cooperation that accompanies Social Reform Program (1381/OC-CO), the subprogram catering for the needs of the country's indigent older adult population will be expanded. In its second stage, the program will cover 50,000 additional indigent older adults in SISBEN I, thereby raising the number of program beneficiaries to 145,000.
  - c. **Community welfare homes (HCBs)** run by the Colombian Family Welfare Institute (ICBF), which provide care and nutrition to 1.3 million children from poor communities; and the **School Meals** Program, also run by ICBF, which provides nutritional supplements to 2.2 million children in schools located in poor geographic areas. Under the labor market reform program approved by Congress in December 2002, para-fiscal funding for the ICBF is set to be scaled back in the years to come. Accordingly, there is an urgent need to target and improve the efficiency of these programs. These are already progressive in their incidence, but their design makes the effect of interventions uncertain. Impact evaluation is being funded by the Bank through loan 1382/OC-CO in 2003, and the results will serve as an input for subsequent program adjustment.
- 1.23 The present government has undertaken to continue these programs and to reform the remaining social protection schemes. Reform will include expansion of health insurance, development of new mechanisms to protect low-income workers against periods of unemployment, extension of the pension system to cover informal workers, and maintenance of the coverage of key social assistance programs. The government will also introduce reforms to improve the effectiveness of ICBF programs that are crucial for the protection of children living in conditions of

poverty and vulnerability; and they will also take other measures to rationalize education and health expenditure.

- 1.24 With support from this program, the government has decided to protect the allocation of expenditure in 2003 and 2004, to guarantee the execution of social assistance programs targeted on the lowest-income population. Given its importance to people living in extreme poverty and its susceptibility to budget cuts at times of austerity, expenditure on the expanded immunization program (PAI) (see paragraph 1.33) and the beneficiary identification system (SISBEN) will also be protected (see paragraphs 1.35-1.37). No protection will be provided to expenditure on education, social security for health, water and housing, since their levels are set by law as a fixed percentage of national government current income plus one inflation adjustment factor, which has become a long-standing model for increased spending on education and health over time. In 2003, nearly US\$4 billion, or 5,3% of GDP, was allocated to these two sectors. Moreover, except for expenditure on social security for health, the other areas have historically behaved neutrally with respect to the business cycle. Table I-3 describes the characteristics of protected social programs (PSPs), and their levels of funding are specified in Annex III.

**Table I-3 Characteristics of Protected Social Programs (PSPs)**

| Organization: Name of program  | Objective of program   | Target population (targeting instrument used)  | No. of beneficiaries prior to 2003  | Coverage to be achieved during 2003 * |
|--|--|--|---|---------------------------------------|
| Administrative Department of the Presidency (DAPR) /Social Support Network (RAS): Families in Action | To improve nutritional status and school attendance among children living in extreme poverty.  | Children under 17 years of age in SISBEN level 1 (SISBEN).   | 325,000 families (2002)   | 325,000 families                      |
| DAPR/RAS: Youth in action  | To enhance the employability of poor and unemployed young people through labor training.   | Unemployed young people not attending school, between 16 and 25 years of age at SISBEN levels 1 and 2 (SISBEN).            | 44,658 young people (2002)  | 35,000 young people                   |
| DAPR/RAS: Employment in Action   | To provide temporary income support for unemployed poor people.  | Unemployed persons in SISBEN levels 1-3 (SISBEN and self-targeting by wage level).   | 170,739 jobs (2002)   | 60,000 jobs                           |
| ICBF: School meals   | To improve nutritional status and school attendance among school-age children  | Children of school-age attending public schools in poor geographic areas (identified by poverty map).                      | 2,226,605 children (2000)   | 2,300,000 children                    |
| ICBF: Community Welfare Homes  | To provide childcare in poor communities.  | Poor children under four years of age (self-targeting).  | 1,308,235 children (2000)   | 1,400,000 children                    |
| Social Solidarity Network (attached to the Office of the President of the Republic)                  | To provide social assistance for displaced populations and victims of violence, as well as for indigent elderly people and ethnic populations. | Displaced persons and victims of armed conflict (self-targeting); indigent elderly people and ethnic populations (SISBEN). | 40,000 displaced households catered for on average per year (1999-2002);* and 60,000 indigent elderly people on average per year (1999-2002). | 145,000 old people                    |

| Organization: Name of program  | Objective of program   | Target population (targeting instrument used)    | No. of beneficiaries prior to 2003  | Coverage to be achieved during 2003 *  |
|--|--|--|---|--|
| National Health Institute and territorial bodies: Expanded Immunization Program. | To reduce child morbidity and mortality rates from avoidable childhood diseases.                                       | Universal for children under three years of age. | DPT: 79%; Triple Viral vaccine: 94.7% of children under one year of age; Polio: 84.8% of children under one year of age (2002 provisional data) | DPT: 90% for children under one; 95% effective coverage of triple viral and polio vaccine in children under one year of age. |
| National Planning Department (DNP): SISBEN                                       | To identify the population living in conditions of poverty in order to target social public spending more effectively. | Population living in poverty.                    |   | 66% of municipalities have applied the new SISBEN survey.  |

\* Given the unpredictable nature of the internal armed conflict, no coverage targets will be proposed for humanitarian care for victims thereof.  
Source: DNP 2002.

## 5. Challenges in education, health and targeting

1.25 The country has embarked upon reforms in education, health and targeting, and a legal framework has been established and supported by two sector programs approved by the Bank in 2001 (1381/OC-CO and 1335/OC-CO). As proposed in the National Development Plan 2002-2006, the current government has taken advantage of recent legal developments to start implementing these reforms, in order to increase the efficiency of social spending, improve expenditure targeting, and consolidate a social protection system to prevent economic crises from undermining the future prospects of the most vulnerable groups. The progress achieved in each area and the implementation actions covered by this program are described below.

### a. Education

1.26 The education sector in Colombia has made significant progress during the last two decades, in terms of service coverage and administration. Education coverage has improved at all levels, and administration of the education system has been decentralized to departments, districts and municipalities. Nonetheless, the country continues to suffer from serious educational shortcomings: primary education is still not universal, and the coverage of secondary education is insufficient; there are major differences in coverage across geographic zones and by socioeconomic level; and children's academic achievement is deficient. The low quality of teaching produces poor internal efficiency and yields low returns in the labor market. The economic crisis has increased dropout and repetition rates among children and young people from poor families.

1.27 Shortcomings in educational coverage, equity and quality are the result of constraints that impede sound management of the sector. In the last few years, several efforts have been made to improve the administration of public education through decentralization. The 1991 Constitution laid the foundations for the

decentralization process, which was further developed in Law 60 of 1993 (Law on the Allocation of Financial Resources and Territorial Competencies) and Law 115 of 1994 (General Education Act). Nonetheless, both the territorial competencies scheme and the framework of resource distribution in education, contained in Law 60, suffer from problems. Although the decentralization legislation generated greater interest in a number of municipalities, departments and education districts, it failed to resolve the problem of confused responsibilities at each level. In resource allocation terms, despite the existence of the formula approved by Law 60, the budget for basic and secondary education was allocated in practice according to the cost of teaching staff in territorial bodies.

- 1.28 Law 715 of 2001 sought to resolve problems of competencies and resource allocation generated by previous legislation, and to lay the foundations for efficient management of the sector. Transfers to finance public education were unified under a single mechanism; the resource allocation scheme was based on the number of children enrolled in schools; and territorial bodies were given greater flexibility to organize education from an institutional point of view. In addition, design of the national system for quality evaluation requires completion, based on experience garnered by the National Education Ministry (MEN) with the SABER program, and by the National Testing Service of the Colombian Higher Education Institute in assessing student achievement.
- 1.29 The government has identified two priority action areas in relation to the current loan. Firstly, it proposes to expand the coverage of basic and secondary education by about 1.5 million places to benefit the poorest population segments. To achieve this goal, the MEN intends to combine several strategies: 800,000 places will be obtained by reorganizing allocation and teaching resources as envisaged in Law 715; 640,000 additional places will be created using resources obtained from changes in the distribution of royalties and reform of the State; and the remaining 60,000 places will be obtained through programs targeting rural education. Secondly, in the coming months the Ministry will focus on fully implementing the measures approved in Law 715, regulating incomplete aspects and providing technical assistance to departments, districts and municipalities to enable them to fulfill their new roles in a decentralized system. Among such measures, the program will support the development of a new teacher career, together with consolidation of the education quality information system, by applying achievement tests to 5th and 9th grade students across the country. For this purpose, MEN also has access to funding from the New School System Program (1202/OC-CO), which has been adapted to support implementation of Law 715.

#### **b. Health**

- 1.30 The creation of the General System of Social Security for Health (SGSSS) in 1993, under Law 100, aimed to achieve universal coverage under two insurance regimes: a contributory regime covering about 70% of the population, and a subsidized

regime for the other 30%. The insurance was intended to guarantee equitable distribution of subsidies and fair access to health services, emphasizing basic prevention and promotion services. The system has made significant progress since its creation. Coverage has tripled; and sector spending, which doubled in the same period, has favored the poorest sectors of the population. Nonetheless, the recent fiscal crisis, together with rising unemployment and the continuation of supply subsidies both at the territorial level and in the Social Security Institute (ISS), have significantly restricted expansion of coverage in the subsidized health regime, and have reduced new affiliations to the contributory regime. These problems are being resolved in the Fiscal Sustainability Program and in the Health Service Network Modernization Program that the government will implement in 2003.

- 1.31 *Quality of service.* In addition, the SGSSS has faced major constraints in guaranteeing service quality, public health and timely flow of resources within the subsidized regime, among other problems. With respect to the quality of service provided by public and private suppliers in the SGSSS, despite the legal framework established in Law 100, the State did not have effective supervision and regulation mechanisms to improve the clinical quality of the service and hence ensure adequate operation of the market on behalf of the patient. Law 715 of 2001, together with the Territorial Fiscal Reform Program (1335/OC-CO), defined the respective competencies of national and territorial governments in this area. The government has used the new legal framework as a basis for creating a quality assurance system with a regulatory framework to penalize and reward SGSSS providers, implementation of which will be a condition for this program. This graduated quality system will consist of the following:
- a. A Single Rating System (SUH), which will establish and oversee the minimum quality standards needed for a Health Service Provider (IPS) to enter and stay in the SGSSS;
  - b. The Healthcare Quality Improvement Audit, which will be used as a systematic and continuous mechanism to evaluate fulfillment of quality standards complementary to those defined as basic in the SUH; and
  - c. The Single Accreditation System, which is a set of self-evaluation, improvement and external evaluation activities aimed at demonstrating, evaluating and verifying compliance with superior quality standards by Health Service Providers, Health Promotion Agencies, Subsidized Regime Managers and Pre-Paid Medicine Firms, that voluntarily decide to participate in this process.
- 1.32 The Ministry of Health will develop quality standards, issue the necessary regulations to apply the system, ensure they are kept permanently up-to-date and that they are applied for the benefit of users; and it will provide technical guidance to system participants in fulfilling their responsibilities. The Superintendency of National Health (SuperSalud) will exercise supervision, inspection and oversight

functions within the system, and apply the sanctions available to it. Departmental, district and municipal bodies, in fulfilling their competencies, are required to comply and enforce in their own jurisdictions.

- 1.33 *Public health.* The cutback in resources for public health actions during the late 1990s has had a dramatic effect on inoculation rates across the country. Between 1995 and 1998, the coverage of vaccination against tuberculosis fell from 100% to 85%; against diphtheria, whooping cough and tetanus coverage (DPT) dropped from 94% to 73%, and against polio it fell from 94% to 75%. The coverage of vaccination against rubella (part of the triple viral vaccine, which also includes measles and mumps), was about 79% in 1999 and 2000. Although preliminary estimates for 2002 suggested this negative trend has been reversed (triple viral vaccine: 94.7%; polio 84.8%), a sustained recovery in vaccination coverage rates is urgently needed in Colombia. The low level of coverage against polio has generated a large group of people susceptible to this disease, at a time when epidemic outbreaks have been detected in African and Asian countries, and a few cases in the Dominican Republic. The drop in coverage of inoculation against diphtheria has led to outbreaks of this illness in cities such as Bogotá and Cali, calling for Ministry of Health intervention. Thus Colombia, which historically has had high inoculation rates, is currently exposing its population to health risks not seen in the country for several years; such risks tend to increase at times of crisis and conflict. Expenditure on inoculation was protected under the Social Reform Program (1381/OC-CO) in 2002, and it will also be protected under this program. Although guaranteed funding is a prerequisite for recovery of the inoculation rate, lack of decision and poor management in providing public health services among the respective territorial jurisdictions, along with health risk managers (HRM)—which operate as public insurance agencies—and health promoting entities (HPE), also have a negative effect on vaccination rates. Law 715 defined the corresponding responsibilities more clearly, and this program will support concrete progress in implementing the legislation at the national and municipal levels.
- 1.34 *Resource Flows.* Lastly, given the number of public and semi-public actors involved in the administration of the subsidized regime, financial flows to reimburse suppliers have continually been problematic, with long delays. The government sees this flow as one of the main obstacles to proper and sustainable functioning of the SGSSS. Accordingly, progress in reducing administrative delays will be included among the conditions of this program. Reductions will be achieved by setting explicit deadlines in the regulations, to be supervised by SuperSalud. The superintendency will also apply the sanctions in its power on HRM and HPE that fail to satisfactorily comply with the regulation.

### **c. Targeting**

- 1.35 The Beneficiary Selection System (SISBEN) is used to target social program subsidies on the country's poor and vulnerable groups. SISBEN is a welfare index



calculated in terms of basic unmet needs and income levels. It awards points to each household indicating its degree of poverty. As a targeting instrument, SISBEN is transparent, cheap and easy to apply; its horizontal efficiency (the ratio between the number of beneficiaries belonging to the poor population and the total size of that population group) is above 81%; and its vertical efficiency (percentage of total beneficiaries belonging to the poor group) is above 69%.<sup>12</sup> These figures are comparable to the performance of similar instruments in developed countries. Nonetheless, the coverage of SISBEN has been highly variable, partly because its application is a municipal responsibility, and municipalities have faced financial constraints in maintaining it—particularly the poorest among them. In addition, as a result of population displacement, it has been impossible to keep the system up-to-date to reflect the current status of the population living in poverty in certain municipalities. This is essential for activating basic social service provision in municipalities that receive displaced people.

- 1.36 The process of reforming SISBEN began under the Social Reform Program (1381/OC-CO). This included: (i) implementation of a central quality control and monitoring system within the DNP, to enhance transparency and accountability in identifying and selecting the beneficiaries that use SISBEN; (ii) updating and piloting of the survey format and the algorithm for determining eligibility, in order to reduce leakages and capture regional differences; and (iii) strengthening of administration, management and supervision of the instrument at the local level, which has also helped make the targeting process more transparent. The present government sees it as a key issue to continue with this reform process by updating SISBEN in all the country's municipalities, by means of a re-survey, using the new format and quality control procedures. The latter will ensure greater transparency and accountability in applying SISBEN. The new format, which uses variables that are more objectively verifiable, reduces the risk of interviewees' distorting the information provided to the questioner. In addition, both interviewees and the municipal authorities responsible for supervising application of the survey will be subject to a system of penalties in the event of falsifying information. At the same time, the national and municipal authorities have launched a campaign to disseminate information on SISBEN and its new application, in order to reduce the possibility of abuse by people not authorized to apply the survey.
- 1.37 Protection of budgetary appropriation and monitoring of its execution form part of the program's conditions. It also makes it possible to extend SISBEN throughout the country, with greater emphasis on poor municipalities and neighborhoods,<sup>13</sup> which until now have not had sufficient resources of their own to apply the survey.

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<sup>12</sup> DNP. Comprehensive evaluation of SISBEN. September 2001.

<sup>13</sup> Identified on the basis of a poverty map.

### **C. The Bank's strategy and justification for the program**

- 1.38 The *Bank's country strategy for Colombia*, currently under preparation, establishes three fundamental objectives on which its actions in the country for 2003-2006 are premised: (i) to lay the foundations for sustainable economic growth; (ii) to promote social development and ensure protection for vulnerable groups; and (iii) to promote the presence of efficient State institutions in national territory, and improve governance. The country strategy also identifies fiscal imbalance and the civil conflict as major constraints on the type of interventions and operational programs that can be undertaken by the Bank. Specifically, fiscal imbalance is a constraint that needs to be resolved in the short run to ensure the viability of any development strategy.
- 1.39 Thus—in the context of the financing provisions contained in the Stand-by Arrangement with the IMF, and given limitations on market access—the Bank will use this emergency operation to support Colombia's financing needs. In terms of the fundamental areas of the country strategy, this operation will mainly contribute to objective (ii). Firstly, it will support the most needy sectors and victims of the armed conflict; and secondly, progress in ongoing reforms in education, health and targeting will contribute to the provision of financially sustainable social services that are more effective in meeting the population's needs and more resource-efficient. In addition to this, protection of investment in human capital raises the economy's growth potential, thereby supporting objective (i).

### **D. The Bank's experience and lessons learned**

- 1.40 Given the difficult economic circumstances currently prevailing, the Country Paper (GN-2052-1) made it a priority for the Bank to support Colombia with sector loans in order to foster macroeconomic stability and promote structural reform. The Bank's experience in Colombia with fast-disbursing loans (three emergency operations approved in 1999 for US\$1.15 billion and two sector operations approved in 2001) can be summarized as follows: (i) they acted as an efficient counter-cyclical mechanism; (ii) together with other sector loans they promoted reforms mainly in the financial and territorial sector, which were crucial in eliminating one of the main sources of crisis in the private sector and deficit in the non-financial public sector (NFPS); and (iii) although these three emergency operations have had a significant effect on the repayment profile for 2003 and 2004 (especially in respect of amounts owed to the Bank), the reforms they supported and the timing with which the resources were delivered were necessary to avert a deeper crisis in Colombia. Annex V summarizes the Bank's experience in sector and emergency loans.
- 1.41 Taking this experience into account, it should be emphasized that, while the conditions contained in the current emergency operation focus on social protection, the financial support package is being accompanied by other operations that

promote structural change. The structural reforms being supported and coordinated by multilateral agencies will help the country absorb the extra repayment pressure arising from this loan during 2006 and 2007, so it should not face another funding crisis.

- 1.42 The Bank has gained useful experience in making social emergency loans in countries such as Argentina and Uruguay. These operations, carried out in coordination with the IMF and the World Bank, have made it possible to: (i) provide short-term calm to financial systems; (ii) provide the economy with liquidity, and finance the deficit; (iii) strengthen reform actions; and (iv) protect social program expenditure in order to mitigate the negative impact of welfare fluctuations among the most vulnerable groups.
- 1.43 This operation is framed by the guidelines on emergency loans approved by the Bank's Board of Executive Directors (GN-2031-10); it incorporates lessons learned during the preparation of similar programs, including: (i) conditions that focus on protecting social spending, which acts as a cushion during times of fiscal tightening; (ii) a small number of contractual conditions; and (iii) coordination between the Bank and other multilateral agencies.
- 1.44 This operation also complements and strengthens the impact of social investment operations from the Bank's active portfolio and loan program.
  - a. To support the implementation and evaluation of policy actions and reforms promoted in the **Social Reform Sector Program** (1381/OC-CO), a parallel technical cooperation (1382/OC-CO) was approved to provide technical assistance for the following activities in particular: (a) implementation of performance agreements in education; (b) implementation of the new labor regulations; (c) progressive updating of SISBEN; (d) a quality-of-life survey that will generate data for activity (f); (e) nutritional assistance impact evaluations; and (f) an ex-post evaluation of the sector program. Although there have been delays in meeting one of the conditions precedent to initial disbursement (fulfilled on 6 November 2002), execution of the operation is about to begin. The program has an assigned budget and contracts in place for undertaking the various activities.
  - b. In terms of **social assistance**, the Bank is supporting the Social Support Network (RAS) (1280/OC-CO), approved in 2000, the characteristics of which are described in paragraph 1.22 (a). The RAS is included among programs protected by this operation.
  - c. In the **education** area, the Bank is implementing the New School System Program (1202/OC-CO), approved in 1999, whose objective is to consolidate reforms in the Colombian educational system, aimed at strengthening decentralized and autonomous management and improving the efficiency and

social equity of resource allocation. This program is supporting the Ministry of Education (MEN) in implementing measures adopted in Law 715 of 2001. Its actions are consistent with the conditions set out in the policy matrix of this program.

- d. In the **health** area, the Bank approved the Health Sector Reform Support Program (910/OC-CO). Although execution of this program began slowly, loan processing was streamlined through the reorganization of studies and effective implementation of the technical support unit in 1998. At the present time, the outstanding balance of the program is about US\$10 million, and the aim is to execute most of this in 2003 to set up an information system for use in monitoring key health system indicators. The Bank and the country are currently preparing a program (CO-0139) to support upgrading and reform of the public health services network, particularly public hospitals.

#### **E. Coordination with other multilateral agencies**

- 1.45 Support for Colombia, in financing terms and in implementing reforms, is being closely coordinated among multilateral agencies and the Colombian government. The Stand-by Arrangement with the IMF serves as a reference framework for this support, which in financial terms involves commitments by multilateral agencies totaling US\$7.349 billion in approvals for 2003-2006. Of this amount, approximately US\$4.2 billion will be fast disbursing (55% to be approved in 2003).
- 1.46 Financial support is complemented by the reforms being promoted by each agency. In 2003, given the priority of reducing spending rigidities and stemming the growth trend in expenditure, the Bank is providing support for the reform of government spending (pension reform, reform of the State, hospital rationalization, restructuring of the ISS), while the World Bank is focusing on budgetary management and an increase in tax revenues and their rationalization. In the context of this program, the definition and monitoring of PSP coverage targets has been coordinated with financing from both the IDB and the World Bank, in order to ensure this protection is maintained through time.

## II. PROGRAM OBJECTIVES AND DESCRIPTION

### A. Objectives

- 2.1 The program's objectives are to help the government maintain macroeconomic and fiscal stability; mitigate the potential effects of fiscal tightening and the economic and social crisis on populations living in extreme poverty; and prevent delays in implementing ongoing reforms in the social sector.

### B. Description

- 2.2 Program disbursements will be conditional on actions in three areas: (i) fulfillment of the Stand-by Arrangement with the IMF; (ii) budgetary protection and monitoring of execution of programs selected because they target the poorest or most vulnerable groups; and (iii) support to avoid setbacks in implementing ongoing social-sector reforms. Annex I contains the policy matrix setting out disbursement conditions.
- 2.3 The timeframe with which the program's policy matrix has been constructed makes release of the first tranche conditional on actions to implement budgetary protection and strengthen ongoing reforms in the social sectors. In view of the financial provisions contained the program with the IMF in 2003, the first tranche will be for up to US\$750 million. Release of the second tranche requires fulfillment of budgetary execution and physical targets for 2003 and continuation of this protection in 2004, together with specific milestones for fulfillment of ongoing sector reform actions, for up to US\$500 million.
- 2.4 **Component A: Agreement and implementation of a macroeconomic program with the IMF.** The objective of this component is to ensure a macroeconomic context that is consistent with the program's objectives. Both tranches require Colombia to comply with a current Stand-by Agreement with the IMF (conditions 1 and 2).
- 2.5 **Component B: Protected social programs (PSPs).** The objective of this component is to guarantee availability of the financing needed for timely execution of protected social programs (PSPs), aimed at cushioning the impact of fiscal tightening and civil conflict on people living in extreme poverty. PSPs include the Social Support Network, the Social Solidarity Network, the food and childcare programs run by the ICBF, the Expanded Immunization Program (PAI) and DNP/SISBEN. The PSPs were chosen on the basis of the following criteria: (i) targeting on the poorest or vulnerable population groups; or (ii) support for ongoing reform actions. The annual cost of these programs amounts to 1.27 billion Colombian pesos at October 2002 prices (approximately US\$440 million), or

0.5% of GDP in 2002.<sup>14</sup> According to current rules on project preparation and budgeting, these amounts are already adjusted for inflation projected for the fiscal year.<sup>15</sup>

- 2.6 For the first tranche (condition 3), the allocation of resources to be transferred to the PSPs in 2003 will be assured (see annexes III and IV), along with the programming of executed expenditure (annex III) and the physical coverage to be satisfied (table I-3). The second tranche (conditions 4 and 5) requires verification of the fulfillment of resource transfer targets as programmed in annex III; and a report will be submitted on progress made in satisfying coverage indicators agreed for each PSP in 2003. The allocation and programming of PSP expenditure and coverage for the following year will also be established, in order to maintain coverage levels. In particular, it will be verified that the General National Budget Bill for 2004, allocates resources equivalent to at least 0.5% of GDP to social assistance programs.<sup>16</sup> These could include the programs specified in Annex III together with new programs satisfying the characteristics of PSPs specified in paragraph 2.5.<sup>17</sup>
- 2.7 **Component C: Actions to monitor reforms in education, health and targeting.** In an unfavorable economic scenario there is a tendency to hold back social sector reform actions, especially those with impacts in the medium term. To prevent this from happening, this component will support the government in its efforts to keep the reform process moving in the social area and avoid delays.
- 2.8 **Education (conditions 6 and 7).** Law 715 created a suitable framework for improving resource allocation and competencies in education, thereby making such expenditure more efficient. The program aims to help the government to: (i) regulate the allocation of additional funds for use in extending coverage targets in basic and secondary education; (ii) establish a new contest for entry into the teacher career; and (iii) devise and apply an achievement test for 5th and 9th grade students enrolled in public and private schools.

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<sup>14</sup> As described in paragraph 1.24, protection will only be given to social assistance expenditure that satisfies the specified criteria. Legislation was passed to ensure that social spending particularly on education and healthcare was maintained over time. In 2003, it accounted for \$11 billion, or 13% of GDP (Source: DNP 2002-2006).

<sup>15</sup> In Colombia any draft budget, *including the PSPs covered by this program*, must be formulated in constant price terms to prevent the cost of the project being distorted by inflation. Projects registered in the General National Budget (PGN), are expressed in constant prices from the time of their formulation, evaluation and registration. Projected inflation is automatically applied to adjust the figures to 2003.

<sup>16</sup> The GDP figure to be used to verify this condition will be the projected 2003 GDP growth figure at the end of the first semester, as published by the DNP Economic Studies Directorate. The same figure is used in preparing the PGN.

<sup>17</sup> The same list of programs would not be used because some are in the evaluation process and might be adjusted or replaced with other programs, depending on the results of impact evaluations. Such is the case of ICBF food and childcare programs, and the programs run by the Social Support Network.

- 2.9 **Health (conditions 8 and 9).** Law 715 also set reform targets at the territorial level in the health sector, in order to rationalize public provision, improve the quality of services and extend insurance coverage. The program will support the following measures, to be coordinated between the Health Ministry and territorial bodies: (i) creation and progress in introducing regulatory mechanisms to improve the quality of health services provided by the SGSSS; (ii) definition of national and territorial responsibilities in the public health domain (Basic Healthcare Plan - PAB) and monitoring of implementation of the PAB, particularly the PAI immunization program, at the territorial level; and (iii) creation and progress in introducing mechanisms to facilitate financial flows within the SGSSS.
- 2.10 **Targeting (conditions 10 and 11).** This subcomponent will support the process of updating SISBEN in two-thirds of the country's municipalities, using the new format and quality-control procedures. For release of the first tranche (condition 10) agreements will be prepared between the municipalities and the DNP for the SISBEN re-survey in 10% of the country's municipalities. For the second tranche (condition 11), the SISBEN re-survey will be completed in at least two-thirds of municipalities.

### **III. PROGRAM EXECUTION**

#### **A. Execution**

- 3.1 The Ministry of Finance and Public Credit (MHCP) will act as executing agency for the loan, through its technical under-secretariat, which will be responsible for general program supervision as regards the fulfillment of objectives and targets, in terms of time and content. The Ministry of National Education (MEN), together with the Ministry of Labor and Health, the Administrative Department of the Presidency (DAPR), the Social Solidarity Network, the Colombian Family Welfare Institute (ICBF), the National Health Institute and the DNP, will be responsible for executing the protected social spending. These agencies will also be responsible for carrying out sector actions to support the continuation of reforms in the education, health and targeting areas.
- 3.2 For the purposes of program coordination and monitoring, a task force will be set up in the MHCP, with representatives from the agencies involved. The task force will be presided by a general coordinator appointed by the MHCP, and by sector coordinators appointed by the respective sector agencies involved in the program. The general taskforce coordinator will act as national government interlocutor with the Bank, assuming responsibility for compiling and sending out technical, legal and administrative information as required for the release of each tranche.
- 3.3 The coordinator and the taskforce will be responsible in particular for ensuring: (i) timely allocation of resources to the protected programs; (ii) monitoring of their financial and physical execution; and (iii) fulfillment of actions to support the continuation of reforms. Within this framework, the MHCP will coordinate the organization and presentation of project reports specified in each area, and ensure timely allocation of resources to the protected programs. The DNP will make sure the actions envisaged in each program are properly executed by the corresponding sector agencies.

#### **B. Monitoring and evaluation**

- 3.4 In view of the multisector nature of the program and its national scope, a quarterly monitoring plan has been agreed with the government in order to oversee timely fulfillment of PSP financial targets and coverage indicators, and progress in ongoing reform actions described in the policy matrix. The task force coordinator will submit the quarterly monitoring report on the program's financial and physical targets to the Bank, no later than 30 days following the end of the respective quarter. The inputs for these reports will come from the MHCP, in the case of financial targets, and from the DNP in coordination with ministries and administrative departments, in the case of physical targets. The task force



coordinator will also be responsible for preparing the technical bases for the second disbursement.

- 3.5 *Monitoring of PSP expenditure.* The MHCP will monitor execution of PSP expenditure through the Integrated Financial Information System (SIIF). This financial management system includes execution of the income and expenditure budget based on general accounting standards. Among other things, it covers all economic-financial transactions carried out by the National Treasury, thereby making it possible to monitor PSP expenditure. Based on such data, the MHCP will prepare the financial content of the quarterly report on the program's financial and physical targets for publication on the MHCP website.
- 3.6 *Monitoring of coverage and sector actions.* In the framework of the National Results Assessment System (Sinergia), the DNP will carry out quarterly monitoring and make annual evaluations of the results of commitments, which are contained in the government's National Development Plan 2002-2006. The aim is for evaluation to help make State policies, programs and institutions more effective, and to establish a suitable accountability framework that actively incorporates social oversight by citizens, with a view to achieving more efficient and transparent allocation of social investment resources.
- 3.7 To achieve this, Ministers and directors of administrative departments, in accordance with their sector responsibilities, will formulate the indicative plan for their sector, based on the established commitments. This will be used to guide actions and available resources in fulfilling the targets. The quarterly monitoring results and the annual evaluation of this plan, which will be submitted for approval by the Economic and Social Policy Council (CONPES), will be the main instruments used to review the progress of social programs. Quarterly results indicating progress towards target coverage levels will be reported on a quarterly basis to the task force coordinator, for consolidation in a report. The results will also be published on the DNP website and through a Sinergia dissemination scheme. This will make it possible to contract sector management on a results basis, and also facilitate social oversight of public administration by citizens.
- 3.8 *Evaluation.* The authorities have intimated to the project team that they are unlikely to want to finance an ex-post evaluation of the program. Nonetheless, the government has undertaken to ensure the availability of data needed for an ex-post evaluation to be financed by the Bank.
  - a. *Justification and evaluation topics.* The project team considers an ex-post evaluation of this program to be important, in order to document the effects of emergency sector operations on the objectives of protecting targeted programs and maintaining reforms in progress. As the program's financial and fiscal impact will be evaluated by the IMF in the framework of its Stand-by Arrangement, this evaluation will seek to answer two fundamental questions

concerning the sector conditionality of the policy matrix: (i) whether PSP expenditure and coverage was maintained through time in real terms; and (ii) whether ongoing reforms in the social sector were maintained over time.

- b. *Financing of the ex post evaluation.* The Bank will defray the costs of the ex post evaluation. Given the highly sophisticated level of the system for monitoring and evaluating development indicators (Synergy), most of the costs of documenting, compiling, and recording the data on the indicators has already been absorbed by the government. Accordingly, for purposes of the ex post evaluation, the Bank will provide financing for a consultant or consulting firm to be hired in accordance with Bank standards. The consultant will be responsible for compiling and interpreting the information on the progress made in the performance indicators specified below in subparagraph c.
- c. *Performance indicators to be evaluated.* Table III-1 below summarizes the performance indicators to be measured through time to evaluate PSP budgetary appropriations and the direct effects of ongoing reforms in the social sector. The table contains baseline values, together with levels to be achieved at the time of the second tranche (forming part of the conditionality) and targets for 2006 in order to demonstrate the evolution of the government's program over time. The indicators have been chosen because of their direct relationship with the actions of this program. With respect to the coverage of PSPs and their impact on the objectives of interest, the findings of impact assessments of these programs (ICBF, RAS), which are also being financed under other IDB programs, will be recorded too. The performance indicator results are reflected in the pertinent documents (1382/OC-CO for ICBF programs and 1280/OC-CO for RAS programs). These evaluations measure the impact of each program on the human capital and poverty relief variables.
- d. *Expected final outcome.* The evaluation will also provide information on the outcome indicators shown in indicative form in table III-1, in the different sectors. These cover poverty, school enrolment, health conditions, and the level of social expenditure targeting, corresponding to the aims of the conditions agreed upon. It should be emphasized that, given the design of the evaluation and the duration and nature of this program<sup>18</sup>, changes recorded in outcome indicators will not be attributable to the actions of the program, and therefore target values have not been established.
- e. *Measurement methodology.* The DNP will measure the indicators described in item (c) using Sinergia (see paragraph 3.6), which in turn makes use of routine

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<sup>18</sup> The guidelines for the emergency programs (GN-2031-10) stipulate that in the case of emergency loans, performance indicators will be established, taking into account the unique nature of the instrument and specific circumstances in which they are employed.

household surveys (Quality of Life Survey, Demography and Health Survey), and the information systems of expenditure executing agencies in Colombia.

**Table III-1**  
**Program performance indicators**

| Condition/Indicator   | Base line value (year) *   | Value to be attained for the second tranche         | Value by 2006                                       | Expected final outcome  |
|---|--|---|---|---|
| <b>Social assistance:</b> % of GDP allocated to social assistance   | 0.3% GDP (2002)  | 0.5% GDP  | 1% GDP  | Families in the first quintile maintain expenditure over the business cycle, in order to protect their human capital investments. |
| <b>Education:</b> Extension of coverage in education/total number of school places in pre-school, basic and secondary education.  | 7,400,000 places (2002)  | 7,700,000 places                                    | 8,900,000 places                                    | Percentage gross coverage of school-age population in pre-school, basic and secondary education.                                  |
| <b>Education:</b> Implementation of information system on education quality/percentage of municipalities evaluated using census tests for 5th and 9th grades.   | 35.2% (2002)   | 60%   | 95%   | Information on the quality of education available for decision-making.  |
| <b>Health:</b> Implementation of SGSSS quality guarantee system/number of IPS, HPE and/or HRM accredited under the new system.  | 0  | 23 (in progress)                                    | 150   | Improved beneficiary perceptions of service quality in the SGSSS.   |
| <b>Health:</b> Strengthening of expanded immunization program/effective coverage of diphtheria, whooping cough, and tetanus (DPT), and polio, rubella, measles, and mumps (Triple viral) vaccinations, in children under one year of age. | DPT: 79% (2002)<br>Polio: 84.8% (2002)<br>Triple viral vaccine: 94.7% (2002) | DPT: 90%<br>Polio: 95%<br>Triple viral vaccine: 95% | DPT: 95%<br>Polio: 95%<br>Triple viral vaccine: 95% | Reduction in the incidence and prevalence of DPT, polio, measles, rubella, and mumps.   |
| <b>Health:</b> Implementation of regulations concerning speed of resource flows between SGSSS agents/reduced processing time from charging to effective payment in the SGSSS.   | 167 days (2002) (National level to HRMs)                                     | 110 days (National level to HRMs)                   | 60 days (National level to HRMs)                    | Reduction of SGSSS administrative costs.  |
| <b>Targeting:</b> SISBEN re-survey completed/percentage of municipalities with re-survey completed.   | 0  | 726 municipalities                                  | 1098 municipalities                                 | Reduced exclusion and leakage in social programs.   |

\* Source: DNP 2002.

### C. Execution period and disbursement timetable

3.9 Although the maximum execution period allowed for an emergency loan is 18 months, this operation is expected to be disbursed over a 12-month period. The initial disbursement of US\$750 million should be made immediately following the signing of the loan contract. The second disbursement of up to US\$500 million will

be made in the first quarter of 2004, in accordance with financing provisions reflected in the IMF Stand-by Arrangement.

**D. Policy letter**

- 3.10 The Bank and the borrower have agreed the Policy Letter attached as Annex IV to this document. The letter summarizes the economic and social policies implemented by the Government of Colombia in the framework of this program. It also restates the government's commitment to the actions described in this document, and sets guidelines for monitoring program actions in the future.

**E. External audit**

- 3.11 The Bank reserves the right to request financial reports from the borrower on the utilization of the loan proceeds, audited by independent auditors previously accepted by the Bank.

**F. Inspection and supervision**

- 3.12 The Bank will establish the inspection procedures it deems necessary for satisfactory execution of this operation. The borrower will co-operate with the Bank in this process, providing assistance and information as necessary.

## **IV. BENEFITS, RISKS, VIABILITY, AND ENVIRONMENTAL AND SOCIAL IMPACT**

### **A. Benefits**

- 4.1 One of the main objectives of this program is to help the Government of Colombia maintain macroeconomic and fiscal stability, and avoid the adverse effects of imbalances on the population in general and vulnerable sectors in particular. In addition, PSP budgetary protection and guaranteed execution should make it possible to avoid further deterioration in the situation of the most vulnerable population groups, which have been seriously harmed by the crisis, and by the armed conflict and its consequences. The strengthening of social reforms will ensure that actions which are crucial to the sustainability and efficiency of social spending do not get postponed.
- 4.2 Given its special characteristics, the program does not entail physical investments or investments of any other type, so it is not expected to have a direct environmental impact. In terms of social impact, the program will help mitigate the effects of the fiscal adjustment and the armed conflict on the most poor, thereby helping to alleviate poverty in the emergency context.
- 4.3 The programs to be protected have been chosen for their impact on living conditions among women and other high-risk groups. The following are included: the Social Support Network, which provides conditional subsidies to motivate indigent mothers to keep their children in school and adequately nourished, as well as work opportunities and labor training for young people and unemployed persons; the Social Solidarity Network, which provides humanitarian assistance to displaced people, mostly low-income women and children, and finances subsidies for indigent older adults; the PAI, which protects children of both sexes from transmissible diseases; the SISBEN, a targeting instrument that makes it possible to declare eligibility for health insurance and social assistance for people living in extreme poverty; and the ICBF, which provides childcare and nutrition services for children under three. Reforms to promote efficiency in education and health will benefit the population as a whole, but especially people living in extreme poverty.
- 4.4 Indigenous and Afro-Colombian population groups are important in several of the programs chosen for protection in this operation. Among other things, the Social Solidarity Network has been appointed to coordinate State policy towards ethnic populations, and to oversee and cater for the victims of the civil conflict, in which Afro-Colombian and indigenous populations are over-represented.

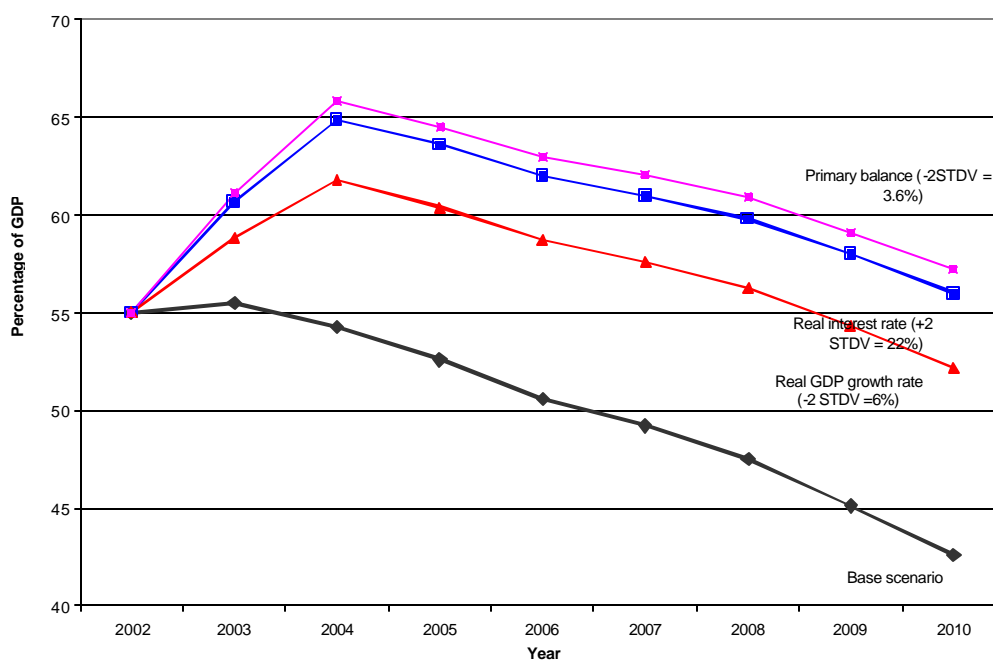
## **B. Risks**

- 4.5 **Non-fulfillment of PSP targets.** There is a risk that PSP resource transfers may not achieve their targets, because of: (i) a possible intensification of the internal armed conflict, which could restrict access to some of the country's municipalities; (ii) the possibility that the referendum on constitutional reform to allow fiscal tightening may fail to gain approval, thereby forcing additional cuts in public expenditure; and (iii) the possibility of management problems in the PSPs, limiting their execution capacity.<sup>19</sup> On the first point, the PSPs have been designed to operate in the current context of civil conflict. During 2002 the effects of the conflict have been concentrated in 122 of the country's municipalities, and coverage targets have been set with this constraint in mind. As regards the second point, the macroeconomic program agreed with the IMF, which provides a framework for this program, specifies alternative adjustment strategies should the referendum fail to be approved (see paragraphs 4.8-4.9). With respect to the third point, PSP monitoring systems will reduce the risk of execution delays arising from management shortcomings.
- 4.6 **Sustainability of the debt.** An additional risk relates to the sustainability of the public debt. It is estimated that between 2003 and 2006 Colombia will have to repay 50% of its total debt, with 2003 and 2004 being the most difficult years. In terms of the maturity profile, a large proportion of external public debt amortization payments fall due in 2003 and 2005, while repayment of internal public debt is concentrated in 2003 and 2004. In view of the economic slowdown, this repayment profile has increased the risk of public debt becoming unsustainable. Estimates of the primary balance needed to make it sustainable range between 1% and 3.5%, depending on the assumptions made about growth, the level of military spending and interest rates, and which debt categories are included in the calculation.
- 4.7 The medium-term projections made by the IMF assume a basic scenario involving growth at the rate established in the Stand-by Arrangement, later stabilizing at 4%, together with a nominal exchange-rate depreciation of 8% in 2003, which slows down over time to stabilize at 2%. Under these basic *scenario assumptions*, the debt is forecast to peak at 55% of GDP in 2003 and then converge to 42% by 2010. The sensitivity analysis displayed in figure IV-1 shows how the debt responds to significant changes in the primary balance, the interest rate and the growth rate. Although these scenarios display slow convergence paths (especially in the case of the primary balance and interest rate), the assumptions made about the trend of control variables represent extreme values that are highly unlikely to occur.

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<sup>19</sup> A related risk is the possibility of a change of program executor; in this case the necessary steps will be taken to ensure operations are unaffected.

**Figure IV-1**  
**Sensitivity analysis. Changes from historical levels during 2003-2004:**  
**minus (plus) two standard deviations<sup>20</sup>**



- 4.8 The reforms being supported by IMF, IDB and World Bank loan operations are key elements of the government's strategy to mitigate this risk. Nonetheless, the authorities recognize that there are other risks that could threaten the implementation of fiscal adjustment measures and structural reforms, and hence make the debt unsustainable. Such risks include the following: volatility on external markets; an unforeseen increase in security expenditure; or insufficient support for the government's economic initiatives, especially those contained in the referendum (a temporary freeze on government operating expenses and elimination of special and exceptional pension regimes).
- 4.9 To mitigate these risks, the Stand-by Arrangement specifies contingency measures to ensure control of the fiscal deficit and maintain financial stability. These include: raising tax rates on products only recently included in the tax base; and making additional expenditure cuts, particularly in public administration at the national level. In the event of financing shortfalls, the government will consider making temporary use of resources from the Petroleum Stabilization Fund (FAEP), which currently stands at about 1.5% of GDP. If the additional resources plus the contingency measures indicated still prove insufficient, the government would consider issuing long-term bonds under concessional terms.

<sup>20</sup> Source: IMF 2003.

**POLICY MATRIX**  
**SOCIAL EMERGENCY PROGRAM (CO-0268)**

| Component   | First tranche (\$750 million)   | Second tranche (\$500 million)   |
|---|---|--|
| <b>A – Macroeconomic stability</b>  | (1) Agreement and implementation of a macroeconomic program with the IMF.   | (2) Agreement and implementation of a macroeconomic program with the IMF.  |
| <b>B – Protection of expenditure in key social programs</b><br><br><i>Objective: to ensure the availability of funding for timely execution of programs intended to cushion the impact of fiscal tightening and the civil conflict.</i> | (3) 2003 budgetary appropriations to protected social programs (PSPs) (see paragraphs 2.5-2.6 of the Project Report), and programming of resource transfer and coverage for same in 2003 (see annex III).   | (4) Resources transferred to PSPs in 2003, as agreed in Annex III.<br><br>(5) Allocation of resources in 2004 General National Budget Bill to social assistance programs, amounting to at least 0.5% of 2003 GDP.  |
| <b>C – Support for ongoing reforms in the social sector</b>   |   |  |
| <b>Education and health</b><br><br><i>Objective: to enhance the efficiency and quality of expenditure on education and health services.</i>   | (6) Measures to improve the efficiency and quality of education: <ul style="list-style-type: none"> <li>➤ Regulation governing allocation of additional resources for use in extending coverage.</li> <li>➤ Establishment of a contest for entry into the new teaching career.</li> <li>➤ Operational plan to apply achievement tests in 5th and 9th grades in public and private schools.</li> </ul> | (7) Continuation of measures to improve the efficiency and quality of education: <ul style="list-style-type: none"> <li>➤ Progress in expanding places at the pre-school, basic and secondary levels (specific target: 300,000 additional places).</li> <li>➤ Contest for entry to the new teaching career operating throughout the country.</li> <li>➤ Application of achievement test to 60% of children from 5th and 9th grades in public and private schools.</li> </ul>   |
|   | (8) Measures to improve the efficiency and quality of health services: <ul style="list-style-type: none"> <li>➤ Creation of regulatory mechanisms to improve the quality of the SGSSS health service.</li> <li>➤ Definition of national and territorial responsibilities in public health (PAB).</li> <li>➤ Regulations approved to streamline SGSSS financial flows.</li> </ul>                      | (9) Measures to improve the efficiency and quality of health services: <ul style="list-style-type: none"> <li>➤ Implementation of regulatory mechanisms to improve quality (specific targets: 23 IPS, HPEs, and/or HRMs in process of accreditation under the new system).</li> <li>➤ Implementation of PAB (specific target: 95% coverage for polio and triple viral vaccinations in population under one year of age; 90% coverage in DPT vaccinations in children under one).</li> <li>➤ Implementation of regulations to streamline SGSSS financial flows (specific target: processing time from National level to HRMs reduced to 70% of present value).</li> </ul> |
| <b>Targeting</b><br><br><i>Objective: to enhance the targeting of social spending, by providing continuous support to the SISBEN reform process.</i>  | (10) Agreement for SISBEN re-survey prepared between the DNP and at least 10% of the country's municipalities (110 municipalities).   | (11) SISBEN re-survey completed in at least 66% of the country's municipalities (615 additional municipalities).   |



**MEANS OF VERIFICATION**  
**SOCIAL EMERGENCY PROGRAM (CO-0268)**

| COMPONENT   | MEANS OF VERIFICATION  | AGENCY RESPONSIBLE               |
|---|--|----------------------------------|
| <b>FIRST DISBURSEMENT</b>   |  |                                  |
| <b>A. Macroeconomic stability</b>   |  |                                  |
| Agreement and implementation of program with the IMF.   | Copy of Stand-by Arrangement approved on 15 January 2003.  | MHCP                             |
| <b>B. Protection of expenditure in priority social programs</b>   |  |                                  |
| 2003 budgetary appropriations for PSPs (see table 1 of Appendix I of the aide memoire of the negotiations). | a) 2003 General National Budget Law.<br>b) Commitment of additional budgetary resources agreed for PSPs in 2003 by national government, expressed in a letter of intent from the Ministry of Finance and Public Credit and the DNP to the Bank.<br>c) 2003 financial plan approved, and CONFIS document describing and reflecting the additions agreed upon. | MHCP<br>MHCP and DNP<br><br>MHCP |
| Programming of resource transfers to PSPs during 2003.  | Letter of intent from MHCP and DNP containing programming of transfers to PSPs in 2003 (see table 1 of Appendix I of the aide-memoire of the negotiations).  | MHCP and DNP                     |
| <b>C. Support for ongoing reforms (education)</b>   |  |                                  |
| Regulation for allocating additional resources to be used to extend coverage.                               | a) MEN resolution regulating use of resources of Law 21 of 1982 to expand coverage.<br>b) Draft decree regulating the use of the surpluses of cooperatives for expansion of education coverage (article 10 of Law 788 on tax reform).  | MEN<br><br>MEN                   |
| Preparation of regulations governing the establishment of a contest for entry into the new teaching career. | Draft decree establishing contest to enter the new teaching career.  | MEN                              |
| Achievement test for 5th and 9th grade children in public and private schools.                              | Operating plan for applying achievement test in 5th and 9th grades in public and private schools for 2003.   | MEN                              |
| <b>C. Support for ongoing reforms (health)</b>  |  |                                  |
| Creation of regulatory mechanisms to improve the quality of the SGSSS.                                      | Decree 2309 (15 October 2002) of the Ministry of Health, defining the Compulsory SGSSS Healthcare Quality Guarantee System.  | MPS                              |

| COMPONENT   | MEANS OF VERIFICATION   | AGENCY RESPONSIBLE |
|---|---|--------------------|
| Definition of national and territorial responsibilities in public health (PAB), with financial incentives for adequate provision.   | External circular 0052 (12 December 2002) of the Ministry of Health, laying down guidelines for the use of resources allocated to public health in 2003, and actions of strict compliance with the Basic Healthcare Plan.   | MPS                |
| Regulation approved to streamline SGSSS financial flows.  | Decree 050 (13 January 2003) of the Ministry of Health.   | MPS                |
| <b>C. Support for ongoing reforms (targeting)</b>   |   |                    |
| Agreements drawn up for SISBEN re-survey in at least 10% of the country's municipalities (110 municipalities).  | Report on agreements drawn up and/or signed between DNP/UNDP and municipalities to carry out the SISBEN re-survey.  | DNP                |
| <b>SECOND DISBURSEMENT</b>  |   |                    |
| <b>A. Macroeconomic stability</b>   |   |                    |
| Agreement and implementation of program with the IMF.   | IMF agreement in force, and progress report for 2003.   | MHCP               |
| <b>B. Protection of expenditure in priority social programs</b>   |   |                    |
| Resources transferred to PSPs in 2003 as agreed in table 1 of Appendix I.   | (a) Budgetary Supplement Law and/or inter-administrative agreements demonstrating compliance with 2003 resource allocation specified in table 1 of Appendix I of the aide-memoire of the negotiations.<br>(b) Evidence of budgetary expenditure in 2003 of at least 80% of the total value specified in table 1 of Appendix I of the aide-memoire of the negotiations (SIIF reports). Payment of the reserve corresponding to PSP allocations for 2002 and the use of resources from 2003 allocations will constitute such evidence.<br>(c) Report on coverage targets achieved in PSPs during 2003 (based on Sinergia data). |                    |
| Appropriations to social assistance programs (including those specified in table 1 of Appendix III, together with new government programs that fulfill the characteristics of PSPs as specified in the Project Report) in General National Budget Bill 2004, amounting to at least 0.5% of mid-2003 GDP. <sup>1</sup> | a) General National Budget Bill for 2004 approved.  | MHCP               |
|   | b) Letter from MHCP and DNP containing programming of transfers to social assistance programs in 2004.  | MHCP               |

<sup>1</sup> The GDP to be used to verify fulfillment of this condition will be the figure for projected GDP growth for the first half of 2003 published by the Office of Economic Studies of the National Planning Department. This is the figure being used to prepare General National Budget for 2004.

| COMPONENT  | MEANS OF VERIFICATION  | AGENCY RESPONSIBLE              |
|--|--|---------------------------------|
| <b>C. Support for ongoing reforms (education)</b>  |  |                                 |
| Progress in expanding school places at pre-school, basic and secondary levels (300,000 new places in 2003).                                    | Report from MEN and DNP on expansion of places at pre-school, basic and secondary levels in 2003; specific target: 300,000 additional places created in 2003.  | MEN                             |
| New contest operating for entry to the new teaching career.  | Decree approved and operating for contests to enter the new teaching career.   | MEN and Office of the President |
| Application of 5 <sup>th</sup> and 9 <sup>th</sup> grade achievement tests in public and private schools in 60% of municipalities during 2003. | Report on application of achievement tests in 5th and 9th grades in 2003.  | MEN                             |
| <b>C. Support for ongoing reforms (health)</b>   |  |                                 |
| Progress in implementation of regulatory mechanisms to improve the quality of the SGSSS.   | Report from the Ministry of Health and DNP on progress made in implementing the system. Specific targets: (1) creditor institution operating (entity selected, entity fulfilling the first four functions described in Resolution 1474); (2) 23 institutions preparing for accreditation (MPS is supporting the process in 10 public institutions and promoting it in 13 private ones). Verification is performed by means of certification of the 23 entities under evaluation. | MTPS                            |
| Targets to be fulfilled in the Basic Healthcare Plan.  | Report from Ministry of Health and DNP on progress made in implementing the PAB. Specific targets: (1) 95% coverage for polio and triple viral vaccination in children under one year of age; (2) 90% coverage of DPT vaccination in children under one.   | MTPS                            |
| Progress in implementing the regulation approved to streamline SGSSS financial flows.  | Report from Ministry of Health and DNP on progress made in implementing regulation approved to speed up financial flows.   | MTPS                            |
| <b>C. Support for ongoing reforms (targeting)</b>  |  |                                 |
| SISBEN re-survey carried out in 66% of the country's municipalities in 2003.   | DNP report.  | DNP                             |

**Social Emergency Program (CO-0268)**  
**Program of resource transfers to PSPs, Colombia 2003 ( October 2002 pesos)**

| Name of program         | Budgetary Code | January-June    | July-September  | October-December  | Total             |
|-------------------------|----------------|-----------------|-----------------|-------------------|-------------------|
| RAS                     | 530 1000 0004  | 161,973,340,000 | 132,500,000,000 | 92,500,000,000    | 386,973,340,000   |
| - Families              |                | 102,986,667,997 | 53,993,336,002  | 53,993,336,002    | 210,973,340,001   |
| - Employment            |                | 18,700,957,717  | 24,792,378,284  | 38,506,663,999    | 82,000,000,000    |
| - Youth                 |                | 40,285,714,286  | 53,714,285,714  | -                 | 94,000,000,000    |
| SISBEN                  | 520 1000 0010  | 9,000,000,000   | 7,500,000,000   | 7,500,000,000     | 24,000,000,000    |
| ICBF                    | 320 1501 0131  | 302,557,922,640 | 204,336,838,680 | 204,336,838,680   | 711,231,600,000   |
| RSS*                    | 320 1501 0125  | 27,378,445,229  | 22,335,047,423  | 22,335,047,423    | 72,048,540,075    |
| PAI                     | 320 0301 0004  | 49,624,750,000  | 14,178,500,000  | 7,089,250,000     | 70,892,500,000    |
| <b>Total for period</b> |                | 550,534,457,869 | 380,850,386,103 | 333,761,136,103   | 1,265,145,980,075 |
| Cumulative              |                | 550,534,457,869 | 931,384,843,972 | 1,265,145,980,075 |                   |

\* Given the nature of humanitarian care for victims of the armed conflict, budgetary execution and coverage targets will be programmed only for the older adults care program (22 billion pesos).

Bogotá, Tuesday, 18 February 2003

**Mr. ENRIQUE IGLESIAS**

President

Inter-American Development Bank

Washington, D.C.

Dear Mr. President,

The wide-ranging loan program put together by the Inter-American Development Bank for 2003-2006, has been one of the dearest signs of support for Colombia since the Uribe-Vélez administration took office in August 2002. The announcement of programs by multilateral development agencies, particularly the IDB and the World Bank, has helped to restore confidence in the stability of the Colombian economy and re-establish market access. This vote of confidence has been crucial in implementing an ambitious program of reforms, many of which have already been approved by Congress.

Following the 1998-1999 crisis, Colombia has worked to reduce the imbalances that were threatening to scupper economic growth and social progress. Inflation has been brought down, financial stability has been restored, and private-sector activity has recovered, albeit in fits and starts. On the other hand, labor market indicators have worsened and poverty has increased. Internal security, the construction of social equity, and economic recovery are the new government's top priorities. The government is also fully committed to fiscal stability and to implementing structural reforms to enable all Colombians to benefit from the opportunities offered by a robust economy. In the present context of adjustment and reform, it is also determined to provide basic social services and protect the country's most vulnerable population groups.

The national government is committed to building a community State: a State based on legitimate authority, with no power for the perpetrators of violence; a State that serves its citizens and is free from the scourges of corruption and cronyism; a State dedicated to eradicating misery which acts in pursuit of social equity and conditions of security; a State that strives to ensure resources reach its citizens; a State that exists for the people and gives political responsibility to citizens through participation in defining, executing and overseeing public actions.

The government realizes there are risks that could threaten full implementation of its program. These include the possibility of an unforeseen increase in security-related expenditure, insufficient support for the economic initiatives contained in the referendum, and heightened volatility on external markets. It has therefore drawn up contingency measures to safeguard its program, including additional taxes and early implementation of some of the measures discussed in this document.

The attached document describes the background and context on which the IDB's Social Emergency Program for Colombia is premised and developed. The policies included in this operation emerged from a broad exchange of ideas between the teams from the Bank and the government. The latter included the Ministry of Finance and Public Credit, the National Planning Department (DNP), the Ministries of Education and Health, and institutions responsible for executing ongoing social protection programs. As a result of this dialog, a program was put together that will enable the government to mitigate the potential negative effects of adjustment and reform processes on the poorest population groups.

Lastly, the government is committed to the program set out in this document, and it welcomes IDB assistance and financial support. The government is grateful to the Board of Directors of the Bank for their speedy consideration of an emergency credit line for up to US\$1.25 billion covering the period 2003-2004.

Sincerely,

/original signed/  
**ROBERTO JUNGUITO BONNET**  
Minister of Finance and Public Credit

/original signed/  
**SANTIAGO MONTENEGRO TRUJILLO**  
Director General of the National Planning  
Department

## **I. Ensuring macroeconomic stability**

1. In 1998-1999 Colombia suffered its worst recession for 70 years. Gross domestic product (GDP) grew by just 0.5% in 1998, and shrank by 4.2% in 1999. The recession undermined the fiscal accounts of the non-financial public sector (NFPS), which posted a record deficit of 4% of GDP in 1999. This was largely the result of excessive spending at the central and territorial government levels, particularly since 1994, which rendered public finances unsustainable especially when compounded by the global crisis that erupted in late 1997.
2. The crisis situation that Colombia has been enduring has four main causes: (i) fiscal imbalance, which despite the efforts and reforms introduced by the national government, still generates a deficit of 2.5%, or around three percentage points of GDP. The deficits recorded in 1996-1999, in conjunction with the financing strategy in those years, led to an unprecedented rise in the cost of borrowing, which unsurprisingly reduced private-sector investment to historically low levels (investment plummeted from 25% to 10% GDP between 1994 and 1999). The interest rate has fallen over the last two years, but private investment has not yet returned to its pre-recession levels; (ii) the difficult public-order situation seems to be having a negative effect on agents' expectations, to the detriment of stronger investment growth. In addition, attacks on the hydrocarbons transport system have caused the oil sector to shrink by about 33%; (iii) Colombian households and firms have suffered a significant reduction in wealth, from which they have been struggling to recover; this, in conjunction with unfavorable expectations, has squeezed domestic demand; and (iv) the prices of some of Colombia's main export products have been on a downward trend.
3. Despite worsening violence and the prevalence of a negative international climate, Colombia has managed to stage a recovery from the 1998-1999 crisis. Fiscal consolidation has moved ahead, inflation has been brought lower, and the financial system has been restructured. By early 2002, these achievements were sufficient to allow access to international credit markets and guarantee exchange rate stability.
4. Nonetheless, in mid-2002, the country was hit by the shockwaves of turbulence in the region: sovereign bond spreads widened substantially and the peso devalued as a result. This situation was compounded by an expanding fiscal deficit and by the most serious worsening of the armed conflict in recent times linked to developments in ongoing peace processes.
5. In this adverse regional environment the new government has acted swiftly to address the country's enormous fiscal problems. Firstly, it proposed (and gained approval for) major budget cuts for 2003, such that non-interest expenditure is set to grow by less than the expected rate of inflation this year. Secondly, it established a one-off wealth tax and submitted an unprecedented package of tax and expenditure-control measures to Congress. Thirdly, it issued decrees cutting expenditure, benefits

- or subsidies: the Tax Reimbursement Certificate (CERT) was reduced to a zero rate, along with non-mandatory benefits at the territorial level, and vacancies that had not been filled since July 2002 were eliminated. At the same time, the government began to design and put in motion an ambitious program to downsize and restructure public administration.
6. In 2002, real GDP growth came in at around 1.7%, inflation was 6.99%, the current-account deficit held steady around 1.8% of GDP, and net international reserves grew by approximately US\$220 million. Expectations for 2003 are for a recovery of economic growth with stability: the rate of growth is projected between 2% and 2.5%, inflation will be in the 5%-6% range, and the current-account deficit should narrow to 0.8% of GDP.
  7. On the fiscal front, at the close of 2002 the consolidated deficit stood at 4% of GDP—1.4 percentage points above the target initially agreed with the International Monetary Fund (IMF). This divergence is largely explained by higher outlays (partly relating to the electoral process) and by the slowdown in economic growth during 2001 and the first half of 2002, which resulted in lower tax revenues.
  8. In 2003, the fiscal deficit of the consolidated public sector is projected to fall to 2.5% of GDP. In order to achieve this target, the government has implemented a two-pronged strategy. Firstly, the Referendum Bill which, if approved, will freeze State operating expenditures in nominal terms during 2003 and 2004. This is expected to generate direct savings amounting to 0.7% of GDP (US\$1.5 billion) in 2003, and 0.5% of GDP (US\$1.2 billion) in 2004. The second element consists of a tax reform which should increase revenues by 1% of GDP during 2003 and 2004, and by 1.8% starting in 2005. The additional revenue will be obtained mainly through a drastic expansion of the VAT tax base, supported by a gradual reduction of income tax exemptions, an income tax surcharge, and a series of improvements in tax administration.
  9. The government's program aims to guarantee fiscal sustainability, and ultimately restore security, regain economic growth and improve social equity. Fiscal tightening and structural reforms will ensure these objectives are achieved within a framework of macroeconomic stability, backed by prudent monetary policies and a strengthening of the financial system. At the same time, steps will be taken to strengthen social assistance programs, expand the coverage of education and health services, and mitigate the impact of higher public utility charges on the poorest population groups.
  10. In this framework of macroeconomic stabilization, the Colombian government signed a Stand-by Arrangement (SBA) with the IMF for 1.548 billion SDR over the next two years. One of the main objectives of that program is to reduce the fiscal deficit by two percentage points of GDP. This will be achieved through higher tax revenues resulting from the new tax reform, and a freezing of national government



current expenditures for a two-year period. In the medium-term, structural improvements, such as pension reform (recently approved by Congress) and the State modernization program, will help to keep borrowing within sustainable limits and consolidate the adjustment process initiated by the government. As key targets for 2003, the SBA envisages an NFPS deficit of 2.5% of GDP, a current-account deficit of 0.8% of GDP and inflation between 5% and 6%.

11. The strengthening of public finances is one of the key strategies to restore confidence and economic growth. Gradualness in curtailing excess public expenditure will be financed from savings generated by adjustment in the private sector. The credibility of the adjustment in the public sector is underpinned by the scope of the structural reforms being implemented. The stated aim is to reduce the consolidated public-sector deficit from 4.0% of GDP in 2002 to 2.5% in 2003 and 2.1% in 2004, and to consolidate the process further in the ensuing years. Fiscal tightening will increase the primary NFPS surplus from 0.7% to 3.0% of GDP, and it is expected to lower the debt of the non-financial public sector below 50% of GDP.
12. The government realizes that public debt sustainability must be based on solid structural reforms, rather than on optimistic economic-growth scenarios or heroic assumptions about exchange-rate or interest-rate behavior.
13. It realizes there are a number of risks that could threaten full implementation of its program. These include an unforeseen increase in security expenditure, inadequate support for the government's economic initiatives, including those contained in the referendum, and volatility on external markets. The government has therefore drawn up contingency measures to safeguard the program against such eventualities, including additional taxes and expenditure cuts, together with early implementation of measures such as raising the VAT on new items included at a 7% rate.
14. In the event of funding shortfalls, the government will consider making temporary use of resources from the Petroleum Stabilization Fund (FAEP), which currently amount to about 1.5% of GDP. In relation to security expenditure, preliminary information suggests that the wealth tax earmarked for this purpose is yielding more revenue than expected. If the additional resources plus the contingency measures mentioned above prove insufficient to finance unforeseen military spending, the government would consider issuing long-term bonds on concessional terms.

## **II. Protection of expenditure on key social programs**

15. The national government has taken steps to consolidate a strategy to protect the poorest and most vulnerable population groups, by developing social prevention and assistance instruments. For this purpose, the National Development Plan will implement a Social Protection and Security System (SPS) to coordinate State policies and address the harmful effects of poverty and vulnerability.
16. The SPS will seek to protect the most vulnerable groups by coordinating and executing social programs, supported by funding mechanisms that guarantee their timely intervention. A set of programs has been developed under two strategies: one for prevention and the other for mitigation.
17. The mitigation strategy includes programs of labor training for the unemployed, child nutrition and school attendance subsidies, and microcredit, among other things. The basic aim is to protect workers against the contingencies of unemployment, partially and temporarily compensating for loss of income. In addition, a labor-market strengthening program will be designed for small and medium-sized businesses that create jobs for heads of households and hire unemployment subsidy beneficiaries.
18. Bearing in mind that social assistance expenditure is procyclical, it is proposed to implement a Social Equilibrium and Protection Fund as a complementary mechanism for funding the system. This would guarantee stability of expenditure, while maintaining or expanding the coverage of the main social programs when negative economic shocks occur. The proposed fund will fulfill a countercyclical function, complementing public expenditure on targeted social programs through the Potential Beneficiary Identification System (SISBEN).

### **The structure of social spending**

19. The relative magnitude of social spending for 2003 (43% of the General National Budget) reflects the government's policy of guaranteeing coverage increases. The largest items in the social spending category are labor and social security (42%), followed by education (34%) and health (18%). These major shares reflect the fact that expenditure on education and health is fully protected from the vagaries of the business cycle.
20. Law 715 guarantees growing and stable funding for these sectors up to 2008. The new organization of the system makes it possible to correct for inter-regional inequalities, overlapping competencies and cost overruns in services, which are not reflected in greater coverage or better quality. The new model for distributing competencies and allocating resources gives greater autonomy to the regions, and generates a clear system of incentives to enhance the quality of services and provide them more efficiently. This encourages transparency in the process, enhances

- monitoring and social oversight, and facilitates the planning of territorial government finances and investment levels.
21. Education funding caters for 7.4 million students at the pre-school, primary and secondary levels, in addition to 340,000 in higher education. Healthcare resources cater for over 11 million people affiliated to the subsidized regime. Funds destined for labor and social security are used mostly to operate the pension system.
  22. Social assistance administered by the Colombian Family Welfare Institute (ICBF) caters for 1.4 million children under seven years of age in community homes, providing them with 73% of their daily nutritional requirements, together with eight hours' childcare. School canteens are responsible for providing breakfast, lunch and a fortified snack for 2.5 million children and teenagers.
  23. Programs in the Social Support Network (RAS) will be subject to rigorous impact evaluation, with established entry and exit criteria. The results are scheduled for government review in 2004, to decide whether they should be included among permanent social protection programs.
  24. The RAS is divided into the following subprograms: (i) *Employment in Action*, which provides temporary employment for 35,000 poor and unemployed workers in building works requiring unskilled labor; (ii) *Families in Action*, which pays subsidies to 325,000 families in SISBEN I, to encourage them to make investments in the health, education and nutrition of their children; this attacks the causes of poverty while also providing income support for extremely poor families; and (iii) *Youth in Action*, which provides training and labor skills to 35,000 young people in SISBEN I and II through a competitive system.
  25. The 2003 Budget Bill allocates 167 billion pesos to RAS programs, together with 77 billion pesos for the Social Solidarity Network (RSS) and 14 billion pesos for SISBEN. The government is committed to increasing budgetary appropriations for these programs to 240 billion pesos, of which 140 billion pesos correspond to the additional RAS budget for 2003 that Colombia negotiated with the IMF. This expenditure is already included in both the Financial Plan and the current targets agreed with the Fund. The resources will be sourced, in proportions yet to be defined, from a supplementary budget to be submitted to Congress, and by signing interagency agreements allowing funds to be transferred from programs with outstanding budgetary allocations.
  26. In order to cater to displaced and other vulnerable population groups, the government increased the 2003 budgetary appropriation to the Social Solidarity Network from 22 billion to 77 billion pesos. This will make it possible to cater for 35,000 households in the main components, namely prevention, humanitarian care, and resettlement. In addition, programs aimed at other vulnerable population groups will continue to receive funding. These include comprehensive care for at least

70,000 indigent older adults; and programs catering for the needs of indigent populations, (through food-for-work and productive project schemes), and for collectors of recyclable material and the disabled.

27. Table 1 displays the programming of resource transfers for Protected Social Programs (PSPs). Once the additional appropriations have been made, these programs will have a total budgetary allocation of 1.28 billion pesos. The government anticipates that this level of funding will be sufficient to cater to the needs of a very high proportion of the country's vulnerable population, and to substantially expand coverage in each program. Funding in excess of the amounts contemplated could overwhelm the execution capacity of the bodies responsible for them.

**Table 1. Programming of transfers for Protected Social Programs**  
**Program of resource transfers to PSPs, Colombia 2003**

| Name of program         | Budgetary code | January - June         | July - September       | October - December     | Total                    |
|-------------------------|----------------|------------------------|------------------------|------------------------|--------------------------|
| RAS                     | 530 1000 0004  | 161 973 340 000        | 132 500 000 000        | 92 500 000 000         | 386 973 340 000          |
| - Families              |                | 102 986 667 997        | 53 993 336 002         | 53 993 336 002         | 210 973 340 001          |
| - Employment            |                | 18 700 957 717         | 24 792 378 284         | 38 506 663 999         | 82 000 000 000           |
| - Youth                 |                | 40 285 714 286         | 53 714 285 714         | -                      | 94 000 000 000           |
| SISBEN                  | 520 1000 0010  | 9 000 000 000          | 7 500 000 000          | 7 500 000 000          | 24 000 000 000           |
| ICBF                    | 320 1501 0131  | 302 557 922 640        | 204 336 838 680        | 204 336 838 680        | 711 231 600 000          |
| RSS*                    | 320 1501 0125  | 27 378 445 229         | 22 335 047 423         | 22 335 047 423         | 72 048 540 075           |
| PAI                     | 320 0301 0004  | 49 624 750 000         | 14 178 500 000         | 7 089 250 000          | 70 892 500 000           |
| <b>Total for period</b> |                | <b>550 534 457 869</b> | <b>380 850 386 103</b> | <b>333 761 136 103</b> | <b>1 265 145 980 075</b> |
| Cumulative              |                | 550 534 457 869        | 931 384 843 972        | 1 265 145 980 075      |                          |

\* Given the nature of humanitarian care for victims of the armed conflict, budgetary execution and coverage targets will be programmed only for the older adults care program (22 billion pesos).

### **The efficiency of social spending, and changes in operational structure**

28. Given the difficult fiscal situation currently prevailing, the government is aware of the need to make far-reaching changes in the way public funds earmarked for social spending are used. The aim here is to utilize resources more efficiently within each institution, while at the same time establishing the SPS to coordinate and ensure overall consistency in the supply of State social services. The first step will entail creation of a Ministry of Social Security, which will act as lead agency in implementing the system. This new Ministry will be formed by merging the current Ministries of Labor and Health, with a view to bringing most social-service-providing institutions under one roof, and designing integrated and efficient policies to minimize functional overlap, especially in the administrative area.

29. A start has also been made on designing and implementing a series of complementary measures to institutionally restructure existing social protection agencies (SENA, Cajas de Compensación, ICBF), and to create a legal and conceptual framework for the SPS.

### **Targeting**

30. Inefficiencies and inequities still persist in the targeting of social spending. These stem from factors such as: lack of information, political leakages, ineffective control and oversight mechanisms, lack of social control and regulation of targeted programs. Despite these constraints, it is essential to target social spending on the poorest and most vulnerable population groups. For this purpose it is necessary to maintain, fine-tune and consolidate targeting strategies in social services such as health, education, housing and potable water supply.
31. The DNP has taken on the task of updating the individual targeting system, in compliance with its legal obligations, and pursuant to Law 715 of 2001 and recommendations contained in Conpes Social document 055. For this purpose it designed and validated the new instrument, together with quality control mechanisms and software, and it also prepared technical manuals and provided training for support staff. In addition, a scheme of sanctions has been designed to penalize unlawful conduct arising from misuse of the SISBEN.
32. Within a period no longer than 1½ years starting in January 2003, the national government expects to train territorial government bodies, set up quality controls, and conduct a new survey in all of the country's municipios. This will allow for greater efficiency in public expenditure, and make it possible to target emergency employment programs, as well as those run by the Social Support Network and the Social Risk System.

### **III. Support for ongoing reforms in the social sector**

33. The country has embarked upon reforms in education, health, targeting and labor training. For this purpose the present government is relying on recent legal developments to make social spending more efficient, improve its targeting, and consolidate a social protection system to prevent economic crises from undercutting the future possibilities of the most vulnerable groups.

### **Education**

34. Education is a crucial factor in human, social and economic development, and a fundamental tool for building social equity. It is therefore worrying that, despite the efforts and undeniable progress that have been made, Colombia has still not managed to universalize access to high-quality basic education. Indicators of coverage, efficiency and quality in the education system show that progress has been

- slow and insufficient; and on several occasions coverage increases have been gained at the expense of quality. Lack of education is a key factor behind the persistence of inequality and the concentration of opportunities.
35. The coverage and quality of education are the most decisive factors in a country's competitiveness. Socioeconomic development is directly linked to productivity growth, which in turn depends on an appropriate interaction between technology improvements and the expansion of education and skills among the labor force. Experience shows that countries which manage to develop organized interactions, with linear, rapid and balanced transitions, achieve faster and more sustainable increases in productivity and growth. This points up the need to promote policies that guarantee linear and gradual increases in coverage and quality at the different education levels.
  36. The strategy of the education revolution seeks to attain the coverage and quality required to enhance conditions for social and economic development in Colombia, and to improve the population's quality of life. The expansion policy at the preschool, basic and secondary education levels aims to raise gross coverage from 82% to 92%, by creating 1.5 million school places, paying special attention to the most vulnerable groups and promoting greater equity in service provision.
  37. This will be achieved through a number of complementary efforts: (i) strengthening of reorganization in departmental and municipal bodies and schools, in order to improve balance and equity in the distribution of physical, human and financial resources, ensure optimal use of installed capacity and prioritize the number of children catered for; up to 800,000 new places will be generated through this mechanism; (ii) creation of a further 640,000 new school places using resources obtained from fiscal savings resulting from the elimination of posts such as Territorial Comptrollers under the State Political Reform Project, together with 56% of the National Royalties Fund and other additional resources; and (iii) implementation of support projects that promote demand, increase retention rates and enhance the efficiency of the education system.
  38. In the case of higher education, the national government will promote equitable access, implementing three mechanisms for retaining and incorporating 400,000 students: (i) a program, supported by loan funding, in which new financing schemes will be created and strengthened to benefit lower-income students, together with incentives for improvements in education quality.
  39. In order to improve the quality of education, national bodies will support territorial entities and schools in institutional and managerial improvement, to ensure that students develop basic, professional, labor and civic skills.
  40. In this context, the aim is to modernize sectoral administration and management at the national, departmental and municipal levels. Four mechanisms will be developed

for this purpose, to improve productivity, efficiency and sectoral transparency, and ensure the quality of investments: (i) institutional modernization of the National Education Ministry; (ii) modernization of departmental and municipal bodies; (iii) reconciliation of management and performance plans; and (iv) development of the education sector information system.

### ***Health***

41. The main objective in this sector is to increase the coverage of social protection and security policies, and to cater on a differential basis for the needs of the most vulnerable population groups. Coverage in the subsidized regime will be expanded by replacing supply subsidies with demand subsidies, thereby increasing the capacity of public hospitals to finance their expenditure through the sale of services. To complement this, an attempt will be made to increase the revenue collected by national government and local bodies, and the structure of funding sources will be altered.
42. With regard to the General System of Social Security for Health (SGSSS), mechanisms will be implemented to underpin the financial sustainability of the system, and to increase coverage and enhance quality in the provision of health services in their different levels and categories. Specific aims in the public health sector include: increasing vaccination coverage rates to reduce the incidence of malaria and dengue fever; lowering infant and maternal mortality rates; preventing teenage pregnancy, and tackling the problem of sexually transmitted diseases. In addition, it is intended to implement a pension policy that avoids financial imbalances, while improving coverage and implementing mechanisms to cover the retired population in a way that guarantees intra- and intergenerational equity.
43. Assistance and protection for the most vulnerable groups will be based on coordination of social assistance and protection programs by implementing the Social Risk System (SSR), using a reformed SISBEN as its key targeting instrument. Special attention will be given to the needs of displaced people.
44. The top priority in public health actions is to achieve and sustain high vaccination coverage levels, in excess of 95% among children under five years of age, in all the biologicals contained in the expanded immunization program. To achieve this goal, the national government will underwrite the necessary resources in the General National Budget to acquire the biologicals in each case, and ensure adequate distribution and conservation. It will also develop the strategies needed to achieve high levels of vaccination coverage.
45. In short, by pursuing the strategy discussed above, Colombia is making great strides towards resolving the main problems in the social sector. The government is committed to making the necessary policy changes, and to ensuring continuity in the process of rationalizing and extending the social protection network.

## COLOMBIA - SECTORAL AND EMERGENCY OPERATIONS 1998-2001

| Loan No.                              | 1159/OC*  | 1166/OC  | 1231/OC   | 1335/OC   | 1381/OC  |
|---------------------------------------|---|--|---|---|--|
| Name                                  | Electric power sector loan  | Fiscal reform sector loan  | Financial sector reform   | Territorial fiscal reform   | Social reform  |
| Type                                  | Emergency   | Emergency  | Emergency   | PBL   | PBL  |
| Objectives                            | (i) To promote financial sustainability in the electric power sector; (ii) to consolidate the regulatory function in the electric power sector; (iii) to define a rural energy policy in non-interconnected areas; (iv) to promote institutional organization of the electric power sector with regard to environmental issues; (v) to facilitate private involvement in domestic electricity distribution firms. | To support public finance reform through measures to reduce fiscal imbalance on a sustained basis, and to improve the allocation of resources in the public sector economy. Specifically it seeks to: (i) increase tax pressure; (ii) rationalize the public sector and increase expenditure efficiency; (iii) modernize the social security system; (iv) minimize duplications in public spending; and (v) facilitate fiscal balance among territorial government bodies. | (i) To improve the legal and regulatory framework, as well as techniques and procedures for the liquidation of financial institutions; (ii) to improve the institutional capacity of bodies responsible for supervision and liquidation of institutions; (iii) to resolve the situation of first-tier public banks and institutions subject to FOGAFIN control and/or support; (iv) to resolve the situation of cooperative institutions supervised by the Superintendent of Banking; and (v) to promote effective execution of measures implemented to confront the impact of current economic circumstances on the sector | The operation seeks to support a deepening of the decentralization process, improving institutional arrangements and promoting a culture of fiscal accountability. It specifically seeks: (i) to create and implement mechanisms for fiscal restructuring in territorial bodies; (ii) to clarify jurisdictions in order to minimize duplications in health and education expenditure; (iii) to create rules that facilitate the fiscal viability of territorial bodies; and (iv) to implement institutional strengthening programs in territorial bodies. | The operation's general objective is to improve the impact, effectiveness and coordination of investments in the social protection network in Colombia. It specifically seeks: (i) to create counter-cyclical and transparent financing mechanisms for social protection at times of crisis or emergency; (ii) to strengthen and make more transparent the targeting of social protection investments, and to establish clear rules in defining the jurisdictions of central government and territorial bodies on health and education issues. |
| Approval                              | 16 December, 1998   | 25 January, 1999   | 8 December, 1999  | August 2001   | 19 December, 2001  |
| Completion of disbursements           | 19 December, 2001   | 19 February, 2000  | 10 May, 2001  | 29 January, 2003  | 31 January, 2003   |
| Current value approved (US\$ million) | US\$245 million   | US\$550 million  | US\$300 million   | US\$400 million   | US\$390 million  |
| % Disbursed as at 31 January 2003     | 100.0%  | 100.0%   | 100.0%  | 100.0%  | 100.0%   |

\* This operation was originally approved for an amount of US\$350 million.