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URUGUAY

GLOBAL CREDIT PROGRAM FOR SAFEGUARDING THE PRODUCTIVE FABRIC AND EMPLOYMENT

(UR-L1171)

LOAN PROPOSAL

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ABBREVIATIONS

ANDE	National Development Agency
BCU	Central Bank of Uruguay
BPS	Banco de Previsión Social [Social Security Bank]
BROU	Banco de la República Oriental del Uruguay
CND	National Development Corporation
CONAFIN-AFISA	Corporación Nacional Financiera Administradora de Fondos de Inversión S.A.
DGI	General Tax Directorate
ECLAC	Economic Commission for Latin America and the Caribbean
FONPLATA	Fondo Financiero para el Desarrollo de los Países de la Cuenca del Plata [River Plate Basin Development Fund]
GDP	Gross domestic product
IRR	Internal rate of return
MEF	Ministry of Economy and Finance
MSMEs	Micro, small, and medium-sized enterprises
NFS	Nonfinancial sector
PCR	Project Completion Report
PMR	Progress Monitoring Report
SiGa	National Guarantee System
WHO	World Health Organization

PROJECT SUMMARY

URUGUAY
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<table>
<tr><th colspan="5">Financial Terms and Conditions</th></tr>
<tr><td colspan="3">Borrower:</td><td colspan="2">Flexible Financing Facility[a]</td></tr>
<tr><td colspan="3">National Development Corporation (CND)</td><td>Amortization period:</td><td>25 years</td></tr>
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<tr><td>IDB (Ordinary Capital):</td><td>80</td><td>100</td><td>Weighted average life:</td><td>15.25 years</td></tr>
<tr><td>Total:</td><td>80</td><td>100</td><td>Approval currency:</td><td>U.S. dollars</td></tr>
<tr><th colspan="5">Project at a Glance</th></tr>
<tr><td colspan="5">Project objective/description: The general objective of this project is to support the sustainability of micro, small, and medium-sized enterprises (MSMEs) as employment providers in Uruguay amid the COVID-19 crisis. The specific objectives are to: (i) to support the short-term financial sustainability of MSMEs; and (ii) to promote the economic recovery of MSMEs through access to production-oriented finance.</td></tr>
<tr><td colspan="5">Special contractual conditions precedent to the first disbursement of the loan: The following will be special contractual conditions precedent to the first disbursement of the loan: (i) the entry into force of an agreement between the borrower and the executing agency for the transfer of the loan proceeds and associated obligations, under the terms previously agreed upon with the Bank; and (ii) the approval and entry into force of the credit regulations, under terms previously agreed upon with the Bank (paragraph 3.14).
Special contractual execution conditions: As a special execution condition, the borrower will submit evidence that it has the authorization of the guarantor for each request for disbursement of the loan proceeds (paragraph 3.15).</td></tr>
<tr><td colspan="5">Exceptions to Bank policies: None</td></tr>
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[a] Under the terms of the Flexible Financing Facility (document FN-655-1), the borrower has the option of requesting changes to the amortization schedule, as well as currency, interest rate, and commodity conversions, subject in all cases to the final amortization date and the original weighted average life. The Bank will take market conditions as well as operational and risk management considerations into account when reviewing such requests.

[b] Under the flexible repayment options of the Flexible Financing Facility, changes to the grace period are permitted provided that they do not entail any extension of the original weighted average life of the loan or the last payment date as documented in the loan contract.

[c] The credit fee and the inspection and supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank's lending charges, in accordance with applicable policies.

[d] SI (Social Inclusion and Equality); PI (Productivity and Innovation); and EI (Economic Integration).

[e] GD (Gender Equality and Diversity); CC (Climate Change and Environmental Sustainability); and IC (Institutional Capacity and Rule of Law).

I. Objective, Description, and Results Monitoring

A. Background, problem to be addressed, and rationale

1.1 **Background.** On 11 March 2020, the World Health Organization (WHO) declared the outbreak of COVID-19, the disease caused by the 2019 novel coronavirus, or SARS-CoV-2, which affects the respiratory system, a pandemic. As of 9 June, WHO has reported more than 7 million confirmed cases in 202 countries, resulting in more than 404,000 deaths.[1] In Latin America and the Caribbean, nearly 1.4 million confirmed cases of COVID-19 have been reported,[2] with more than 65,000 deaths.[3] In Uruguay, the first case was recorded on 13 March, and to date, 845 confirmed cases have been recorded, with 23 deaths, representing a fatality rate of 2.6%. Total spending and public spending on health in Uruguay (9.5% and 6.8% of gross domestic product (GDP), respectively) are among the highest in the region, and WHO ranks the country at level 3 of 5 in terms of its level of preparedness and capacity to manage public health events.[4]

1.2 **Macroeconomic and/or social context.** The economic impacts of COVID-19 will be felt through different channels at different times. The first, associated with the priority of saving lives in the very short term, involves the direct costs of the health sector response. The second includes the costs associated with the necessary changes in people's behavior to "flatten the curve" of COVID-19 progression, which will contribute to saving lives. These changes in behavior will lead to a very significant economic downturn with immediate manifestations and lingering effects, even once the health emergency is over. From a regional macroeconomic perspective, in addition to shrinking domestic demand, the Economic Commission for Latin America and the Caribbean (ECLAC) sees at least five channels through which the impacts of the crisis will be passed on to the Latin American and Caribbean economy:[5] (i) slowing economic activity of key trading partners that will impact the demand for exports; (ii) less demand for tourism services; (iii) interruption of global value chains; (iv) falling commodity prices; and (v) worsening financial terms.

1.3 In Uruguay, the government decreed a health emergency and has introduced mitigation measures to contain the spread of COVID-19.[6] The measures, implemented as of 13 March, include the temporary suspension of classes in schools and universities, the cancellation of public events, and the closure of shopping malls. Construction activities were also suspended for one month until 13 April. Uruguay's land borders with Argentina and Brazil have been closed, cruise ship passengers and crew cannot disembark at Uruguayan ports, and commercial airline traffic has been cancelled. The government has also mandated reduced

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1 See WHO COVID-19 Situation Dashboard at Covid19.who.int (9 June 2020).

2 At present, all countries in Latin America and the Caribbean have confirmed cases of COVID-19 (9 June 2020).

3 See PAHO status report (27 March 2020).

4 According to WHO Country Preparedness and Response Status for COVID-19 (19 March 2020).

5 See ECLAC press release (19 March 2020).

6 See: Measures adopted by the Government of Uruguay to address the COVID-19 health emergency (21 May 2020).

public transportation frequencies and teleworking protocols in both the public and the private sectors.

1.4 Uruguay's current macroeconomic prospects for 2020 have been downgraded. At the start of this year, the growth forecast was 2.1%,[7] but GDP is now expected to contract by 3%,[8] although uncertainty persists as to the final impact COVID-19 will have on the economy. As a result of the isolation measures, economic activity is expected to decline, leading to increased unemployment, reduced household income, and a drop in consumption. In addition to the contraction of domestic demand: (i) external demand is also expected to shrink, especially from Uruguay's main trading partners China, Brazil and the European Union; and (ii) the fiscal deficit and public debt will likely grow more than expected owing to the cost of the economic and social measures adopted in response to COVID-19. The behavior of domestic and external demand means that GDP is likely to fall in 2020 before returning to more normal conditions leading to a recovery in economic activity and consumption in 2021.[9]

1.5 **Current constraints on access to finance for micro, small, and medium-sized enterprises (MSMEs) in Uruguay.**[10] For the general features of the intervention, see optional link 2. In Uruguay, MSMEs are a fundamental part of the economy's production and employment fabric, representing over 99% of all Uruguayan private-sector firms (186,000 out of a total of 187,000) and employing more than 67% of all workers (630,000 out of 928,000 jobs). In terms of the sector distribution of their activities, MSMEs are mostly concentrated in services (51%) and commerce (39%), with just 10% of them in industry (see [1] of optional link 3).

Table 1. Distribution of firms in Uruguay by size and employment

Size	Number of firms	% of firms	Number of employees	% of employees
Micro	156,190	83.4%	228,735	24.6%
Small	25,187	13.4%	209,355	22.6%
Medium	4,904	2.6%	192,010	20.6%
Large	855	0.6%	298,073	32.2%
Total	**187,136**	**100%**	**928,173**	**100%**

Note: National classification of MSMEs (Executive Decree No. 504/007, 20 December 2007).

Source: Directory of Enterprises and Establishments (National Institute of Statistics, 2018).

1.6 Uruguayan MSMEs were already facing constraints in their access to finance prior to the economic difficulties caused by the COVID-19 containment measures. A study by the SME Finance Forum in 2018 found that 25% of formal MSMEs in Uruguay have unmet financial needs. The financing gap among formal MSMEs is estimated at approximately 1.7 times the current level of lending by the financial system, equivalent to over US$5.8 billion in unmet credit demand (equivalent to 11% of GDP) (see [2] of optional link 3). These data are consistent with the latest national MSME survey, which show that: (i) 83% of MSMEs start their activity using their own capital, while 8% begin with a bank loan; and (ii) 8% of MSMEs say they have full access to

[7] International Monetary Fund (IMF), 2019 Article IV Consultation, February, 2020.

[8] IMF, *World Economic Outlook*, April 2020.

[9] Oxford Economics, *Country Economic Forecast: Uruguay,* April 2020.

[10] See Bibliography (optional link 3).

credit, while 19% claim access with difficulty, 20% say they are excluded from access to credit, and the remaining 53% say they do not use bank credit at all (see [3] of optional link 3).

1.7 The credit data published by the Central Bank of Uruguay (BCU) confirm that MSMEs receive a minor share of the credit supplied by the financial system. Accordingly, the Uruguayan private sector is relatively underfinanced. In 2019, credit to the nonfinancial private sector represented 25% of GDP (one of the lowest ratios in the region, compared to Brazil 62%, Chile 116%, Colombia 50%, Mexico 35%, Peru 44%, and a world average of 129%) (see [4] of optional link 3). Total lending to the nonfinancial sector in Uruguay in 2019 is divided between credit to households (39%) and credit to businesses (61%). A breakdown of credit supply by firm size shows that the distribution has remained constant over the past 10 years; and that roughly 65% of financial system lending, both in dollars and Uruguayan pesos, is absorbed by large firms. In contrast, medium-sized firms receive 20%, small firms 10%, and microenterprises 5% (see [5] of optional link 3).

1.8 Uruguay's financial system is essentially a banking system, since 98% of the system's assets are held by 12 banks. The banking system consists of a public commercial bank (Banco de la República Oriental del Uruguay (BROU)), a public mortgage bank, nine private commercial banks, and four nonbank financial institutions. As of year-end 2019, the banking system's assets stood at US$38.05 billion, of which 45% were held by the BROU, 49% by private banks, and 5% by other financial intermediaries. As the country's largest bank, in 2019 the BROU lent US$4.165 billion to the nonfinancial sector (27% of total lending), of which US$2.489 billion was corporate credit channeled to the productive sectors. The vast majority of corporate credit is absorbed by agriculture (40%), manufacturing (23%), and services (20%) (see optional link 3).

1.9 The Uruguayan financial system has a healthy level of solvency enabling it to cope with adverse scenarios; but the slump in economic activity limits its capacity to increase its lending to MSMEs. As of December 2019, financial institutions in Uruguay were solvent, with capitalization averaging 90% above the required regulatory minimum; the quality of the nonfinancial sector credit portfolio was 16.6% in the highest risk categories; and the nonperforming loans rate in the business segment stood at 3.6% (see [6] of optional link 3). The nonfinancial sector portfolio is likely to deteriorate sharply, especially as households lose jobs and firms pare back their activity in the sectors worst affected by the economic slowdown, such as tourism, transportation, and commerce. Not only will the impact be felt in a deterioration of the loan portfolio, but the financial system is also likely to see its investment portfolios deteriorate and experience higher funding costs. Although the financial sector is resilient to this type of adversity, this scenario poses special challenges for meeting the demand for credit by MSMEs in the current situation.

1.10 The difficulties faced by MSMEs in obtaining finance in the Uruguayan financial system are set to worsen with the economic contraction of 2020. The main problem faced by MSMEs in the current context is the lack of liquidity to cover fixed costs and maintain jobs when faced by an abrupt reduction in their operating income. A recent Bank study used the wage bill among MSMEs in certain sectors that have seen their activity shrink the most to calculate short-term liquidity needs. The study shows that there could be major needs for additional funds to maintain employment levels in sectors such as manufacturing, commerce, hotels, restaurants, transportation, and storage. Table 2 presents an estimate of the monthly personnel costs facing

MSMEs in these sectors. Fifty percent of the personnel cost in these sectors represents about US$160 million per month (equivalent to 0.3% of GDP) (see [7] of optional link 3).

Table 2. Potential MSME liquidity needs as a function of wage costs

Sector	**20% of staff cost** *Monthly values, US$ million*	**50% of staff cost** *Monthly values, US$ million*
Manufacturing industry	13.0	32.4
Trade, hotels, restaurants	34.1	85.3
Transportation	11.8	29.5
Other service activities	5.4	13.5
Total	**64.3**	**160.8**

Source: Continuous Household Survey (National Institute of Statistics, 2018).

1.11 The cut in income raises MSME credit risk and causes the supply of credit to dwindle. A survey by the Chamber of Industries of Uruguay (CIU) conducted on 30 March, found that 69% of the firms surveyed had seen their sales volumes shrink as a result of the COVID-19 crisis; and 68% had either cut back or halted production. In both cases small businesses were disproportionately affected (see [8] of optional link 3). This situation heightens the perceived credit risk of the MSME segment; and the financial system doubles down on liquidity preference instead of continuing to lend to MSME customers that are experiencing economic hardship (see [9] of optional link 3). In this context, public policies have an important role to play in stimulating the supply of credit to provide liquidity to the productive sector, e.g. through new credit lines or credit guarantees (see [10] of optional link 3).

1.12 **Challenges and progress.** A key economic policy objective in the context of a profound but temporary shock is to prevent liquidity problems leading to firms becoming insolvent, with the consequent irreversible loss of capital and jobs for the economy. In shielding Uruguay's productive fabric and employment from the economic hardships associated with the COVID-19 crisis, the challenge will be to keep open as many as possible of the MSMEs that were commercially viable before the crisis, avoid short-term insolvencies, and enable these firms to gradually resume normal operations once the health emergency is over. In the case of Uruguay, this challenge is all the more important since unemployment has been edging up since 2015 (see [11] of optional link 3), and it is forecast to rise by an additional 1.1% in 2020 (see [12] of optional link 3).

1.13 The government has adopted public policies to address the economic consequences of the COVID-19 health emergency, including a set of measures to support MSMEs. These are aligned with the economic, monetary, and financial policy measures to provide financial support to MSMEs which have been adopted by developed and emerging countries and can be classified in three major groups: (i) providing additional liquidity to the financial system; (ii) preventing the depletion of working capital; and (iii) preserving access to credit to bolster short-term liquidity (see optional link 4). The measures adopted by Uruguay are summarized in Table 3 and have the specific objectives of maintaining the financial health of MSMEs in the face of a temporary shock, protecting their credit quality, and underpinning the payment chain that links producers, suppliers, and distributors.

Table 3. Main public policy measures in support of MSMEs in Uruguay

Type of measure	Description
Providing liquidity to the financial system	• **Central Bank of Uruguay (BCU):** Temporary lowering of bank reserve requirements (3%-7%) in both national currency and indexed units, to increase the liquidity of the financial system. • Authorization for financial intermediaries to extend the maturity of loans granted to the nonfinancial sector by 180 days.
Preventing depletion of working capital	• **Directorate General of Taxation (DGI):** Postponement of the minimum VAT payment for the months of March and April. The amount in question will be financed in six installments to be added directly to the VAT returns payable as of May.
	• **Deferral of Social Security Bank (BPS) contributions:** Tax payments in the simplified (*monotributista*) regime and contributions by firms with up to 10 employees, falling due in April and May, are deferred. 60% of these contributions will be paid in six instalments starting in June, while the remaining 40% will be paid by the State.
Preserving access to credit	• **National Development Agency (ANDE):** Within the directed credit programs, a working capital credit and debt reprofiling line at a subsidized rate is created for firms directly affected by COVID-19. • Maturity extension for all beneficiaries of the ANDE financing programs. • New loans of up to Ur$12,000 available to 70,000 sole proprietorships.
	• **National Guarantee System (SiGa):** Creation of a new, more flexible guarantee line for MSMEs and reduction of the commission charged to operators (from 2.6% to 0.78%).
	• **Banco de la República Oriental del Uruguay (BROU):** New production-oriented credit line of US$50 million with more flexible conditions.

Source: Official websites of the BCU, DGI, BPS, ANDE, SiGa, BROU, and the Office of the President of the Republic of Uruguay.

1.14 Although Uruguay has deployed rapid measures to support MSMEs, it faces a major challenge in underpinning their financial sustainability and the employment they generate for the economy. The country's financial sector suffers from constraints in providing the full flow of financing that MSMEs require; and this problem is expected to become more acute in view of the economic contraction forecast for 2020 and the expected deterioration of the MSME credit portfolio. In order to avoid breaking the chain of financing for MSMEs in times of financial system stress, one of the international policy measures most widely adopted, and considered to be the most effective, are public credit guarantee mechanisms to ensure that financial intermediaries do not suddenly turn off their supply of credit. The objective of credit guarantees is that financial intermediaries continue to provide financing to MSMEs when: (i) it is more difficult for them to access external funding; (ii) they are less willing to lend in the face of heightened credit risk; (iii) they have to allocate additional funds for debt rescheduling or restructuring; and (iv) MSMEs themselves have less in the way of assets to provide as their own collateral to access credit (see [13] of optional link 3). One of the key measures adopted by the government to make it easier for MSMEs to obtain finance has been to use the National Guarantee System (SiGa) to increase the provision of credit guarantees to the financial system, and thus reduce credit risk and encourage financial intermediaries to continue lending to MSMEs.

1.15 SiGa was created in 2008 and includes guarantee funds covering loans granted by financial intermediaries to firms in Uruguay.[11] It has proven to be an effective tool for mobilizing credit to firms since it was launched in July 2009. The SiGa-PYMES guarantee fund exists to address the problems of MSME access to credit, and in 2009-2019 it extended 93% of all SiGa guarantees to the financial system. In 10 years, this fund has accumulated more than 19,300 guarantee operations totaling US$243 million, which represents credit mobilization of US$499 million. The financial intermediaries that have made greatest use of this guarantee fund to extend credit to MSMEs have been Santander (29%), BBVA (20%), BROU (14.3%), ITAU (11.8%), ScotiaBank (10%), and BANDES (8.2%).[12] The average guarantee was US$12,602, for an average loan size of US$25,762. This results in average coverage of 49% of the loan value and average leverage of 1.62%. Microenterprises accounted for 28% of the amount of these guarantees, small firms 41%, and medium-sized firms 31%, with the following sector distribution: commerce 42%, services 24%, agriculture 10%, industry 11%, and transportation 10%. Sixty-three percent of the loans in question are targeted to working capital, while 37% are for investment.[13]

1.16 SiGa is also proving to be an effective instrument for supporting the flow of credit needed by Uruguayan MSMEs in the current situation. As of 6 April 2020, the SiGa-PYMES guarantee fund expanded its activity and started offering the new SiGa Emergencia guarantee line, designed exclusively to assist MSMEs affected by the health emergency declared by the executive branch in March 2020. The main novelties of this credit line are that it increases the maximum guarantee amount to US$153,000. It also raises the maximum coverage to 80%, includes a debt restructuring option, and significantly reduces the fee payable to the financial intermediaries.[14] The performance of SiGa Emergencia in April and May showed the average guarantee amount rising to US$16,594 and coverage expanding to 70%. SiGa Emergencia posted a record volume of guarantee placement that exceeds the monthly rolling average for the period-2009-2019 by more than six times.[15] In view of the growing demand for guarantees, the Ministry of Economy and Finance (MEF) has already assigned US$30 million of its capital to support this new guarantee line.

1.17 **Proposed intervention.** In support of the public policy measures that Uruguay has adopted to ease MSME financing constraints, the proposed intervention will strengthen the public program of credit guarantees for enterprises in Uruguay and thus sustain financial system lending to MSMEs through a Global Credit Program. The program seeks to ease the constraints on access to credit faced by MSMEs affected by the COVID-19 crisis, in order to support their survival and preserve the jobs they generate for the economy. This, in turn, will minimize the burden on social protection systems and maximize the speed of economic recovery once the health emergency is over. The intervention will be coordinated through SiGa, which will receive support from the Bank to improve its capacity to provide credit guarantees so that financial intermediaries can continue to lend to MSMEs affected by the COVID-19 crisis.

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[11] See: https://www.siga.com.uy/.

[12] See List of SiGa operators (April, 2020).

[13] See SiGa management report (31 January 2020).

[14] See Circular 2020/04: Conditions of the SiGa Emergencia guarantee line (6 April 2020).

[15] See SiGa management report (30 April 2020).

1.18 The proposed program will target MSMEs in the economic sectors that comprise SiGa's guarantee portfolio, and in particular the SiGa Emergencia guarantee line. The demand for guarantees under SiGa Emergencia is concentrated in the commerce sector (54%), services (20%),[16] and industry (10%); and together with the agricultural sector, transportation, and construction, these are expected to be the main recipients of loans backed by SiGa Emergencia guarantees. The sectors in question have been hard hit by the COVID-19 crisis, so their credit risk has increased and they need additional collateral to obtain credit. Moreover, an analysis of productive sector vulnerability to COVID-19, conducted for Uruguay by the Bank, identified all of these sectors as severely vulnerable (see optional link 5).[17] The program therefore combines serving the needs of the most vulnerable groups of firms (MSMEs) and sectors, with flexibility in execution to provide a global solution that can be adapted to the uncertain evolution of the impact of COVID-19 on the different sectors of the economy.

1.19 **Demand analysis.** In May, SiGa held consultations and meetings with the financial intermediaries to obtain a more precise estimate of the likely demand for this guarantee product in the coming months (see [14] of optional link 3). The study showed that a sustained increase is expected over the next 24 months, with estimated requests for guarantees totaling US$337 million. This would imply credit mobilization of US$487.5 million, of which 80% is expected to be for working capital. Given this new reality, SiGa needs at least US$96 million of additional funding to be able to issue a substantially larger volume of credit guarantees than was customary prior to the COVID-19 crisis. The US$80 million of the present operation is expected to help cover SiGa's needs for additional funding to support this new demand for guarantees under the SiGa Emergencia guarantee line. With the proceeds from the operation, it is estimated that up to US$280 million could be provided in guarantees to mobilize up to US$400 million in credit for MSMEs.[18]

1.20 **Gender.** In addition to the systemic difficulties Uruguay's productive fabric faces in accessing finance, as described above, women are being more severely impacted by the COVID-19 crisis. From the production-related standpoint, women workers and entrepreneurs have a stronger presence in Uruguay's services sector, which is among the hardest hit by the crisis. In Uruguay, 14% of MSMEs are led or owned by women, with the majority in the microenterprise segment. It is estimated that 16% of MSMEs led by women in the formal sector face some type of restriction on access to finance in Uruguay, which is equivalent to a gap in access to finance of US$534 million ([18] of optional link 3). SiGa does not currently have mechanisms to measure guarantees granted to women-led or owned MSMEs, but is designing a

[16] Tourism can be considered within the service sector.

[17] When interpreting the results of the analysis, two factors need to be considered: (i) the sample is probably already affected by the economic impact of COVID-19, so a low vulnerability rating does not represent a normal situation; and (ii) the overall index should not be used as a way to prioritize the financing needs of the sectors analyzed.

[18] The calculation used the SiGa Emergencia parameters as the approach best suited to the profile of use of the program's resources. The leverage ratio allowed for SiGa Emergencia is 3.5; so with the program's US$80 million, guarantees of up to US$280 million could be granted. If the average SiGa Emergencia guarantee is US$16,594, a total of 16,874 guarantees can be expected. When the total number of guarantees is adjusted by the average repetition rate of 1.1, i.e. firms taking out more than one SiGa Emergencia guarantee, then the potential number of final beneficiaries is 15,214. As the SiGa Emergencia average coverage rate is 70%, it is estimated that US$280 million of guarantees will mobilize US$400 million, with an average guaranteed loan of US$26,292.

strategy to incorporate the generation of data on women entrepreneurs into its guarantee lines. The program plans to support SiGa in this effort.

1.21 **The Bank's experience.** The Bank has extensive experience in designing sovereign guaranteed loan programs aimed at improving MSME access to finance through financial intermediaries ([15] of optional link 3). These programs have been implemented in times of economic expansion, when support focuses on access to long-term finance for production-oriented investments, and in times of economic recession, when support focuses on ensuring that MSMEs do not lose access to liquidity to continue their economic activity. In the last financial crisis confronted by the region in 2007, the Bank played a countercyclical role by expanding the amount of financing and facilities used to address the lack of access to credit faced by the region's MSMEs. For example, liquidity programs for economic growth sustainability were approved in 2008 and 2009[19] with the aim of reestablishing access to finance for working capital and foreign trade in the productive sectors. This helped to temporarily offset part of the deficit in financing flows to MSMEs resulting from the international financial crisis. With the same objective of stimulating the supply of credit to the productive sectors, the period following the crisis (2009-2013) saw the approval of contingent credit lines[20] for providing liquidity to the financial system, as well as global multisector credit programs and productive financing programs for MSMEs (see [16] of optional link 3).

1.22 Specifically, the Bank has supported public credit guarantee funds which, like SiGa, aim to improve MSME access to finance by providing guarantees to financial intermediaries that supply credit to the economy. The Bank has approved programs to enhance MSME access to finance, with components that create or support credit guarantee funds, in a variety of the region's countries, including: Argentina (loan 1914/OC-AR), Barbados (loan 3390/CH-BA), Chile (loan 4272/OC-CH), Haiti (loan 2416/GR-HA), Jamaica (loan 4115/OC-JA), Nicaragua (loan 3042/BL-NI), and Paraguay (loan 3354/OC-PR-1).[21]

1.23 **Lessons learned.** The Bank has generated lessons learned from the operations mentioned above (paragraphs 1.21-1.22) and the most important ones for this program are summarized below. For MSME credit risk mitigation public policies to be effective, it is crucial that credit guarantee programs like SiGa: (i) identify the market failure to be addressed; (ii) be designed to contribute the greatest possible mobilization of credit to the economy; (iii) strengthen collaboration between the public and private sectors to prevent market distortions; (iv) have communication and dissemination strategies aimed at the end beneficiary to explain the advantages of the product; (v) have adequate institutional capacity for rapid, streamlined management of the execution of guarantees; and (vi) include data collection systems that enable the evaluation of the effectiveness of the guarantee programs from a public policy perspective (see [17] of optional link 3).

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19 In 2008, the IDB created the Liquidity Program for Growth Sustainability under the category of emergency lending (document GN-2492-1).

20 "Development Sustainability Contingent Credit Line" under the Proposal to Establish Contingent Lending Instruments of the IDB (document GN-2667-2).

21 Specifically, efficient guarantee allocation mechanisms are highlighted as one of the main tools for streamlining credit.

1.24 The lessons learned by the Bank have been applied in the design of this program so that: (i) the expansion of SiGa guarantees plays a countercyclical role at times when the credit supply contracts; (ii) the greater leverage features of the SiGa Emergencia line have a greater impact on mobilizing credit for the economy; (iii) the supervision by SiGa of the financial terms under which guarantees are provided to end users prevents market distortions and ensures that the additionality is not diluted; (iv) the SiGa Emergencia program takes communication considerations into account to send a clear message and the opportunity it provides to improve access to finance for MSMEs; (v) SiGa continues to ensure the viability of executing the guarantee to avoid bottlenecks and delays in the execution of guarantees affecting the credibility and benefits of the instrument's use; (vi) CONAFIN-AFISA systematically compiles, manages, and maintains program data so the results can be analyzed and continue to be used in future interventions; and (vii) the Bank supports the institutional capacity of CONAFIN-AFISA, as the program's executing agency, to implement the intervention and evaluate and monitor the guarantees granted.[22]

1.25 **Coordination with other Bank projects.** The program coordinates efforts with various supports, such as: (i) strengthening of fiscal policy and management; (ii) response to the health emergency; and (iii) safety nets for vulnerable populations, which the Bank is working on with the country. Between January and June 2020, the Bank supported the country with disbursements totaling US$1,050,750,000 in unrestricted funds resulting from fulfillment of the conditions for five policy-based loans with a deferred disbursement option. The Bank is also supporting the country in its health emergency phase with the procurement of medical supplies, including ventilators. Also worth noting is the coordination with the Program to Strengthen Public Policy and Fiscal Management in Response to the Health and Economic Crisis Caused by COVID-19 in Uruguay (loan 5034/OC-UR) for US$350 million approved on 21 May 2020. This program contains policy conditions to strengthen the countercyclical effect of fiscal policy through the temporary introduction of measures to increase firms' liquidity during the health and economic crisis, including SiGa's establishment of the SiGa Emergencia guarantee line to address the credit needs of MSMEs stemming from the health emergency in order to ensure loan operations for working capital, investment capital, and the restructuring of prior loans. This coordination seeks to leverage synergies to increase the impact of the Bank actions, consistent with fiscal sustainability, through: (i) the temporary application of the measures so that their short-term impact on the public finances is controlled, and (ii) support in financial terms for MSMEs, to ease the cost of financing and preserve jobs, thus contributing to a recovery in tax revenue.

1.26 **Coordination with other multilateral and/or cooperation agencies.** The Bank has played a major part in the response that Uruguay is receiving from organizations and other donors to support the financial sustainability of MSMEs. Actions by the different donors have been coordinated with the MEF. A loan of US$15 million has been made by the River Plate Basin Development Fund (FONPLATA) for a program to provide financial assistance to the MSMEs that are most vulnerable to the COVID-19 health emergency. This loan aims to alleviate the temporary impacts of

[22] Section IV of the Support to SMEs and Financial Access/Supervision Sector Framework Document (document GN-2768-7) discusses a more extensive and detailed set of lessons learned from the Bank's experience in the sector, as well as the experience of other multilaterals, academic researchers, and other major stakeholders in public policy design to support MSMEs.

the health emergency on these firms. In addition, the ANDE channels the funds through its directed credit program (see Table 3), with a view to preventing temporary negative effects from becoming permanent and thus causing the loss of the economic fabric built up in recent years. The specific objective of this operation is to reduce the risk of an interruption in the payment chain during the period from April to July 2020, by providing a monthly injection of liquidity to enable regular obligations to be fulfilled at a time when incomes are diminished owing to the health emergency. In a subsequent phase of the program, a sustainable and permanent mechanism will be designed within ANDE to address the problems of MSME access to working capital credit on competitive terms. That intervention will be aligned with, and complementary to, the support proposed in this operation.

1.27 **Strategic alignment.** The program is consistent with the second Update to the Institutional Strategy (document AB-3190-2) and is aligned with the challenge of productivity and innovation, through support for productive financing for MSMEs. The operation is also consistent with the strategic focus area of resource mobilization, through the proposed mechanisms to stimulate the mobilization of financial sector resources for MSME finance, as well as the company shareholders' own funds. The program will contribute to the Corporate Results Framework 2020-2023 (document GN-2727-12) through the indicator of the number of micro, small, and medium-sized enterprises financed. The program is consistent with the Proposal for the IDB Group's Governance Response to the COVID-19 Pandemic Outbreak (document GN-2996), as part of the support for safeguarding the productive fabric and employment and is consistent with the Support to SMEs and Financial Access/Supervision Sector Framework Document (document GN-2768-7), which emphasizes the importance of promoting access to finance by the productive sector.

B. Objectives, components, and cost

1.28 **Objectives.** The general objective of this project is to support the sustainability of MSMEs as employment providers in Uruguay amid the COVID-19 crisis. The specific objectives are to: (i) to support the short-term financial sustainability of MSMEs; and (ii) to promote the economic recovery of MSMEs through access to production-oriented finance.

1.29 **Sole component. Support for MSME financing (US$80 million).** This intervention is structured as a loan with the following subcomponents.

1.30 **Subcomponent 1. Support for improvement of short-term financial capacity (US$60 million).** Resources under this subcomponent will be used to help MSMEs affected by the COVID-19 crisis to overcome temporary liquidity problems and enable them to fulfill their commercial and financial obligations, and thus continue operating. Financing will be provided in a way that makes it possible to normalize their commercial cycle. The subcomponent will provide funds to SiGa to support the issuance of guarantees for loans granted by financial intermediaries to MSMEs. The guarantees to be financed under this component aim to facilitate MSMEs access to financing for: (i) new short-term loans; and (ii) the restructuring of existing short-term loans.

1.31 **Subcomponent 2. Support for access to production-oriented finance for economic recovery (US$20 million).** Resources under this subcomponent will be used to support the economic recovery of MSMEs affected by the COVID-19 crisis, to provide them with ongoing access to finance and enable them to restore their

productive capacity, finance productive restructuring needs, or meet a specific increase in demand that may arise as a result of the crisis. The subcomponent will provide funds to SiGa to support the issuance of guarantees for loans granted by financial intermediaries to MSMEs. The guarantees to be financed under this component aim to facilitate MSMEs access to financing for: (i) new medium-term loans; and (ii) the restructuring of existing medium-term loans.

1.32 **Beneficiaries.** The intervention will target its resources on formally established MSMEs that are affected by the COVID-19 crisis. A total of 15,214 MSMEs could potentially benefit from this program through SiGa guarantees.

C. Key results indicators

1.33 **Expected outcomes.** The program's expected impact is to support the sustainability of MSMEs amid the COVID-19 crisis, as measured by: (i) employment in the sectors supported by the program as a percentage of total MSME employment in Uruguay; and (ii) average sales in the MSME sector. The program's outcome indicators will be: (i) the arrears rate in the relevant portfolio of working capital or production-oriented financing at 6, 12, and 24 months after the program start, relative to the rate in private banks; and (ii) the total value of the relevant production-oriented finance portfolio attained as a result of program support.

1.34 **Economic viability.** The economic evaluation identifies the flows of benefits and costs generated by the program. The benefits consist of the economic value of the reduction in sales revenue losses, the benefits derived from a higher rate of business survival, and the benefits of jobs preserved as a result of the program. Calculations of the aforementioned flows (discounted at a rate of 12%) yield benefits of US$461.4 million and an internal rate of return of 26%. In addition, the sensitivity analysis shows that the results are robust to reasonable variations in key parameters (reduction of sales, output rate, coverage of guarantees) (see optional link 1).

II. Financing Structure and Main Risks

A. Financing instruments

2.1 The total program amount proposed here will be US$80 million in resources from the Ordinary Capital. The operation will be structured as a global credit loan, since it involves financial intermediation to the beneficiary MSMEs. The disbursement period will be two years.

Table 4. Estimated program costs (US$ millions)

Component	IDB (Total)	%
Sole component. Support for MSME financing	80	100
Subcomponent 1. Support for improvement of short-term financial capacity	60	75
Subcomponent 2. Support for access to production-oriented finance for economic recovery	20	25
Total	**80**	**100**

Table 5. Disbursement schedule (US$ millions)

Source	Year 1	Year 2	Total
IDB	40	40	80
Total	**40**	**40**	**80**
%	**50%**	**50%**	**100%**

B. Environmental and social risks

2.2 In accordance with directive B.13 of the Environment and Safeguards Compliance Policy (Operational Policy OP-703), this operation cannot be classified ex ante, since it involves financial intermediation. The environmental and social due diligence was performed in compliance with Directive B.13, analyzing the program's potential socioenvironmental risks, the applicable regulatory framework, and the executing agency's ability to manage these risks. Based on the due diligence findings, and given the low risk profile of the eligible loans with program resources, this operation is considered a low financial intermediation risk (FI-3). Given their size (loans to guarantee with a maximum amount of US$200,000) and nature (support for the short-term financial sustainability of MSMEs and their economic recovery through access to production-oriented financing), the loans will be in category "C." Loans in categories "A" and "B" will be ineligible for financing.

2.3 The following will not be financed with the proceeds of this loan: no activities on the program exclusion list, including activities/sectors posing a higher socioenvironmental risk or activities that: (i) involve involuntary physical or economic resettlement; (ii) entail negative impact on indigenous groups; (iii) may cause damage to cultural sites or critical cultural sites; (iv) involve a negative impact on protected areas or Ramsar sites; and (v) involve the use of invasive species.

2.4 The requirements for managing and mitigating potential environmental and social impacts will constitute an Environmental and Social Risk Management System that will be included in the credit regulations, which will be approved as a condition precedent to the first disbursement (see Environmental and Social Management Report).

C. Fiduciary risks

2.5 The institutional capacity assessment of the executing agency, Corporación Nacional Financiera Administradora de Fondos de Inversión Sociedad Anónima (CONAFIN-AFISA), found that it meets the necessary conditions to fulfill fiduciary management activities for the loan operation; accordingly, the fiduciary risk is deemed low.

2.6 As CONAFIN-AFISA has not previously served as the executing agency of sovereign-guaranteed loans from the Bank, its execution capacity was analyzed, covering its structure, organization, and processes. The evaluation showed that the entity has a satisfactory institutional capacity and a satisfactory level of development. It also has a staff qualified to discharge the functions in question and execute the program. The institutional capacity analysis revealed no weaknesses in project coordination, so it is expected that the program can be executed with solvency.

D. Other key risks and issues

2.7 **Development risk.** There is a medium risk that the resources will be insufficient to meet the demand for MSME finance. To mitigate this risk, the Bank has designed the intervention to yield the maximum possible impact and has sought to coordinate with all relevant stakeholders, to ensure that the response is commensurate with the financial system's loan guarantee needs for MSME financing.

2.8 **Public management and governance risks.** There is a medium risk that implementation of the measures included in this program will be delayed as a consequence of the emergency priorities managed by the government, so the resources might not reach the beneficiary MSMEs in a timely manner. To mitigate this risk, the Bank has designed the program to expedite approval processing and execute rapidly, based on its experience with the borrower and the implementation agreements reached with the executing agency.[23]

2.9 **Macroeconomic and fiscal sustainability risk.** There is a medium risk that the combination of the increased spending to address the economic emergency and external factors such as capital outflow and the devaluation of the peso, may significantly impact the country's fiscal and debt positions, jeopardizing fiscal sustainability and the country's sovereign investment-grade rating. To mitigate this risk, the Bank, together with other international organizations, is providing technical assistance to the country to prepare and monitor the implementation of post-pandemic economic and fiscal recovery plans that will help put the public finances back on a sustainable trajectory.[24]

2.10 **Execution risks.** Based on the institutional capacity assessment of the executing agency, medium execution risks were identified associated with the response capacity to the growing demand for guarantees and SiGa's monitoring system. To mitigate this risk, the Bank will provide nonreimbursable technical assistance in two areas: (i) building the executing agency's institutional capacity to manage the growing demand for guarantees that SiGa is experiencing in the current economic situation; and (ii) strengthening SiGa's monitoring and evaluation system to improve the measurement of the guarantee program's benefits as a public policy tool for safeguarding the business fabric and employment in a context of economic recovery.

2.11 **Sustainability.** The program is expected to contribute to mitigating temporary difficulties of access to financing faced by MSMEs as a result of the economic shock caused by COVID-19. Nonetheless, it provides the country with the opportunity to leave these public policy measures in place for the financial support of MSMEs. The demonstration effect of the interventions by SiGa is also expected to allow it to maintain the current credit guarantee lines and programs, as well as to develop new guarantee products to ease the vulnerability of access to finance experienced by MSMEs in Uruguay.

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[23] This experience and these agreements are included in the Credit Regulations, which are in an advanced stage of preparation and are expected to take effect when the loan contract is signed.

[24] Ministry of Economy and Finance (MEF). May 2020. "Sovereign Debt Report."

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation arrangements

3.1 **Borrower and guarantor.** The borrower for this operation will be the National Development Corporation (CND),[25] in its role as the entity legally responsible for the administration of SiGa. The loan will be guaranteed by the Eastern Republic of Uruguay.

3.2 **Executing agency.** The executing agency will be CONAFIN-AFISA, as SiGa trustee. CONAFIN-AFISA is an investment fund and trust administrator that was set up to administer SiGa. Its exclusive purpose is to manage investment funds and stand as trustee in financial trusts. It is 100% owned by the CND and holds BCU authorization to operate. CONAFIN-AFISA has administered SiGa since the start of its operations in 2009; and, as trustee, its responsibilities include the following: (i) implementing guarantee trusts; (ii) issuing guarantees on loans made by creditors; and (iii) monitoring customer compliance with payments on loans guaranteed by specific guarantee funds, and adopting measures as necessary to regularize cases of arrears. The executing agency will be responsible for the administration, execution, control, and monitoring of the loan proceeds.

3.3 **SiGa.** SiGa was created in 2008[26] to extend guarantees on loans granted by financial intermediaries to firms in Uruguay. It currently has five guarantee funds,[27] which are set up as specific guarantee trusts. The largest of these is SiGa-PYMES,[28] which operates the SiGa Emergencia guarantee line. The BCU supervises SiGa and oversees its maximum permitted leverage policies, as well as portfolio risk indicators. SiGa is led by a board of directors[29] which approves, for each specific guarantee trust, the guarantee lines to be offered to the financial system. These include: (i) the mechanisms for allocating quotas to each financial intermediary; (ii) leverage within the maximum allowed by the BCU; (iii) coverage percentages; (iv) fees; (v) criteria for accepting operators; (vi) sanctions; and (vii) indicators for measuring nonperformance, among other items (see optional link 7 for SiGa's institutional, operational, and performance data).

3.4 **Execution and administration.** CONAFIN-AFISA will execute the program from within its current organizational structure. It will manage the program's resources through the existing SiGa trusts, to support guarantee lines that are framed by the program's sole component and are eligible under the credit regulations. It is initially envisaged that the loan proceeds will be used entirely to support the SiGa Emergencia guarantee line. To this end, CONAFIN-AFISA will be responsible for managing the planning, coordination, operational monitoring, legal monitoring,

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[25] The CND is a non-State legal entity under public law, established by Law 15.785 of 4 December 1985. It is well capitalized and is financially sound. By law, at least 60% of the CND's capital is held either by the State itself or by other State entities. Currently, 100% of the CND's capital is under State control. The law also authorizes the CND to contract loans both in Uruguay and abroad. In recent years it has been a Bank borrower in two operations (loans 3578/OC-UR and 4824/OC-UR).

[26] Article 505 of Law 18362 of 6 October 2008 and Decree 773/008 of 22 December 2008.

[27] There are specific funds, such as SiGa-MICRO serving microenterprises; SiGa-FOGALE the dairy sector, or SiGa-Arroceros for the rice sector.

[28] The MEF is the trustor of the SiGa-PYMES specific guarantee trust, which was set up under a contract between the State and CONAFIN-AFISA on 9 June 2009.

[29] The SiGa Board of Directors consists one member appointed by the CND, one appointed by the MEF, and one appointed by the ANDE.

accounting and financial control, tracking, evaluation, and any other function needed to effectively administer the program's subcomponents.

3.5 To execute the program, CONAFIN-AFISA will deploy its institutional structure, which has clearly defined and duly formalized systems and processes. CONAFIN-AFISA has had successful experiences in executing infrastructure programs with the Andean Development Corporation (CAF) and in an energy stabilization program with the World Bank. For the execution of this program, it will receive support from the CND in processing disbursements and their respective justifications to the Bank. In addition, under a service provision agreement, the CND will provide support to CONAFIN-AFISA on legal management and internal audit matters.

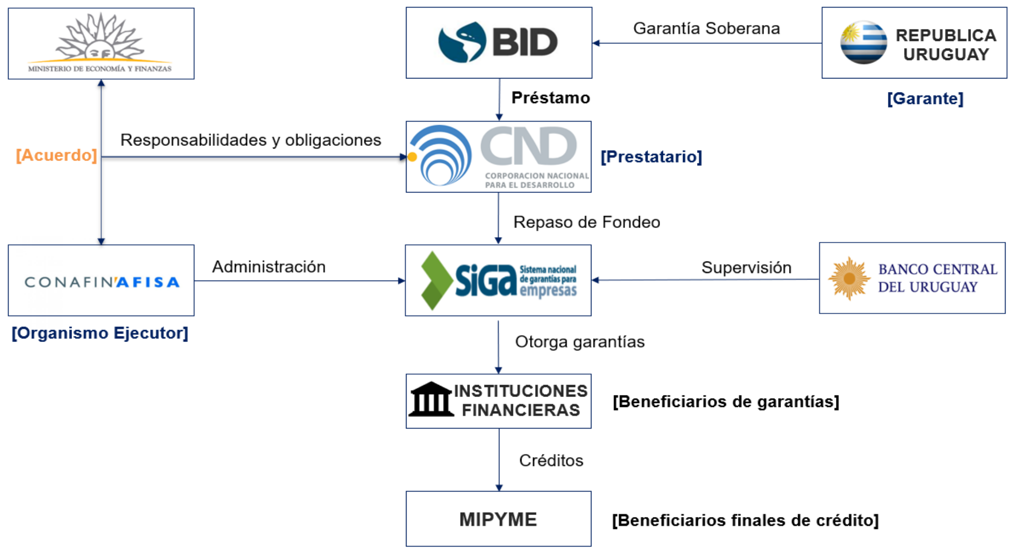
3.6 CONAFIN-AFISA will have fiduciary responsibility for the program resources and will fulfill the following functions: (i) using the loan proceeds to provide the guarantees to financial intermediaries under the SiGa Emergencia guarantee line or other SiGa guarantee lines for MSMEs that are eligible under the loan contract and credit regulations; (ii) managing the loan proceeds through a separately managed account; (iii) monitoring and ensuring that the guarantees granted comply with the provisions of the loan contract, the program objectives, and the terms of the credit regulations; (iv) preparing execution and physical/financial progress reports for the Bank; (v) monitoring compliance with environmental and social safeguards and the provisions on prohibited practices, in accordance with the loan contract and the credit regulations; and (vi) monitoring and evaluating the program.

3.7 **Implementation considerations.** Through the program, the CND will transfer resources to CONAFIN-AFISA for the purpose of funding SiGa's guarantee lines. The CND will sign an agreement to transfer the loan proceeds to CONAFIN-AFISA, which will manage the resources as SiGa trustee pursuant to the loan contract and the credit regulations. These funds will be used to support credit guarantees issued through the SiGa Emergencia guarantee line, or other SiGa guarantee lines that may be approved under the existing guarantee trusts to support MSMEs within the operation's objectives. The eligibility criteria for loans submitted to SiGa and for its guarantee lines, to be financed from the program, will be governed by the credit regulations. The credits to be guaranteed and the guarantees to be granted will be subject to the maximum limits approved by the BCU for SiGa, which are currently US$153,000, and the provisions of the credit regulations.

3.8 Implementation as regards the issuance, management, and payment of the individual guarantees backed by the program will be based on SiGa's operational policies, as set out in its operating regulations. These follow international best practices for the management of public guarantee funds and have proven to be a transparent, efficient, and effective management framework. MSMEs can submit a loan application in any SiGa-affiliated financial institution. The latter is responsible for analyzing the MSME's creditworthiness and processing the guarantee automatically through its online computer system. If the information is entered correctly and satisfies the established eligibility criteria, the system initiates the guarantee confirmation process. SiGa then registers the guarantee once the information is checked and the liability to be guaranteed is accepted. One of the requirements for the guarantee to be registered is acceptance by the MSME of the terms and conditions of the guarantee to be attached to the loan. As the guarantees are registered in the system, the status of the guarantee is constantly monitored. Thus, the financial intermediaries' guaranteed portfolios are subject to annual and

random audits. All details of SiGa operations can be found in the operating regulations published on the institution's website.[30]

Figure 1. Program execution diagram



Source: Prepared by the authors.

3.9 For financial intermediaries to be eligible, they must be qualified as SiGa operators. There are currently 15 of these, including eight of the country's main financial institutions, so SiGa offers a global solution to the financial system. To become a SiGa operator, financial institutions must: (i) have at least three years of audit reports filed by auditors registered with the BCU; and (ii) sign an affiliation agreement. This agreement implies that the financial intermediary accepts conditions including those established in the SiGa Operating Regulations regarding: the guarantee application and assignment process, the terms of coverage, portfolio inspections and audits, payment procedures, conditions for claiming on the guarantee, recovery agreements, grounds for nonpayment of guarantees, penalties, etc.

3.10 For MSMEs to be eligible, they must meet the following requirements: (i) be a company incorporated under the laws of Uruguay; (ii) be up to date with its obligations to BPS and the DGI; and (iii) meet all other eligibility criteria agreed upon with the Bank, applicable to guarantees granted under the program, as established in the credit regulations.

3.11 **Interagency agreement.** An agreement will be signed between the borrower (CND) and the executing agency (CONAFIN-AFISA)[31] containing the following: (i) a commitment by the CND to transfer the loan proceeds to CONAFIN-AFISA in accordance with the terms defined in the loan agreement; and (ii) a commitment by CONAFIN-AFISA to administer and supervise the use of the resources pursuant to the loan agreement and the credit regulations. The MEF may also sign this

30 SiGa, 2016. Operating Regulations.

31 As of June 2020, the parties have already begun the dialogue for preparation of the agreement that is expected to be signed at the same time the loan contract is signed.

agreement, confirming its commitment to transfer the necessary budgetary resources to the CND to enable it to meet its financial obligations under the loan agreement with the Bank. Once this specific agreement has been approved by the Bank, any amendment or modification thereof will require the Bank's prior no objection.

3.12 **Credit regulations.** The rules governing the execution of this operation, along with the eligibility criteria for granting the guarantee lines to be backed by the loan proceeds, and other parameters or restrictions governing the use of those resources, will be defined in the credit regulations agreed upon between the Bank, CONAFIN-AFISA, and SiGa's board of directors, and approved by the Bank and the SiGa board. The credit regulations will also include: (i) a description of responsibilities in the areas of administration, risk management, and coordination between the executing agency and the Bank; and (ii) the agreements on program management, monitoring, and evaluation, among other arrangements.

3.13 **Interagency coordination.** In addition to the interagency agreement between the MEF, the CND, and CONAFIN-AFISA specifying the obligations and responsibilities of the institutions involved in this program (paragraph 3.11), there are additional interagency coordination mechanisms such as SiGa's own board of directors. The latter is responsible for overseeing the management of SiGa by CONAFIN-AFISA, and for approving the operational policies governing SiGa operations. Within this governance framework, the MEF and the CND, as board members, have a constant and fluid dialogue with each other and with CONAFIN-AFISA, so interagency coordination should be efficient.

3.14 **Special contractual conditions precedent to the first disbursement of the loan proceeds. The following will be special contractual conditions precedent to the first disbursement of the loan proceeds: (i) the entry into force of an agreement between the borrower and the executing agency for the transfer of the loan proceeds and associated obligations, under the terms previously agreed upon with the Bank; and (ii) the approval and entry into force of the credit regulations, under terms previously agreed upon with the Bank.** These conditions are necessary to define the responsibilities of each institution, to regulate the flow of resources devoted to the repayment of the Bank loan, and to establish the structure, guidelines, and procedures to be followed by the executing agency for successful program execution.

3.15 **Special contractual execution conditions.** As a special execution condition, the borrower will submit evidence that it has the guarantor's authorization for each request for disbursement of loan proceeds. This condition reflects the MEF's responsibility for centralizing public debt management and control of direct and contingent fiscal liabilities assumed by the country.

3.16 **Retroactive financing.** The Bank may retroactively finance eligible expenditures made by the borrower prior to the loan approval date for the granting of guarantees to financial intermediaries associated with loans granted to MSMEs under the program for up to the amount of US$16 million (20% of loan amount), provided that requirements substantially similar to those established in the loan contract and the credit regulations were met. These expenditures will have been made on or after 6 April 2020, the date on which the SiGa Board of Directors formally approved the new SiGa Emergencia line of guarantees to serve MSMEs affected by the health emergency caused by COVID-19. Although this date is prior to the date the project

officially entered the pipeline (document GN-2259-1), due to the exceptional circumstances the crisis is expected to have on the deterioration of the MSME portfolio, and considering the large growth in demand for loan guarantees under the SiGa Emergencia line of guarantees since its creation, exceptional authorization of retroactive financing as of this date is justified.

3.17 **Procurement.** As a demand-driven financial intermediation program, no procurement of goods, works, nonconsulting services, or consulting services is likely to be required as part of execution. No project execution plan or procurement plan is therefore included in this proposal. Any procurement of nonconsulting or consulting services required as part of program administration and/or evaluation will be conducted in accordance with the Policies for the Procurement of Goods and Works Financed by the IDB (document GN-2349-15) and the Policies for the Selection and Contracting of Consultants Financed by the IDB (document GN-2350-15), or as subsequently updated. For additional details, see the Fiduciary Agreements and Requirements (Annex III).

3.18 **Disbursements.** For purposes of program execution, the IDB will disburse the resources under any of the modalities established in the Financial Management Guidelines for IDB-financed Projects (document OP-273-12). Disbursement requests will be accompanied by the information listed in the credit regulations. The program resources will be disbursed by the IDB to the CND, and then will subsequently be transferred to CONAFIN-AFISA. The CND will request disbursements from the IDB, upon prior authorization by the guarantor. Disbursements will be made under terms previously agreed upon with the Bank. Disbursements will be verified on an ex post basis, subject to onsite review of the guarantees granted.

3.19 **Financial statements and audit.** The executing agency will submit audited annual financial statements for the program in accordance with the terms of reference agreed upon with the Bank, within 120 days following the close of the executing agency's fiscal year. The final financial statements for the project will be delivered within 120 days after the date of the last loan disbursement. The project audit will be conducted by the Office of the Auditor General or a Bank-eligible independent audit firm, under the procedures established in the current audit guidelines.

B. Summary of arrangements for monitoring results

3.20 **Monitoring.** Program execution will be monitored via semiannual progress reports prepared by the executing agency and delivered within 60 days after the close of each six-month period. The reports will be based on the reporting commitments included in the Results Matrix, as well as compliance with the eligibility criteria set out in the credit regulations (see monitoring and evaluation plan). These reports will be reflected in the progress monitoring reports (PMR).

3.21 **Evaluation.** The strategy to evaluate the program's outcomes will follow: (i) the submission by the executing agency to the Bank of a final evaluation report, within 180 days after the date of the last disbursement of the loan proceeds; and (ii) a reflective evaluation, before and after the program, showing the scope of the outcomes and impacts; and a qualitative analysis that will be included in the Project Completion Report (PCR), which will aim to answer the following questions: (i) what were the main weaknesses and challenges for project execution; (ii) what were the measures implemented to remedy the weaknesses and challenges in execution; and (iii) what lessons learned and proposals were generated by execution of the

project. These studies will assess impacts on the reduction of lost sales revenue and the benefits of jobs preserved as a result of the program. The evaluation strategy is described in the monitoring and evaluation plan. The executing agency will bear the costs of evaluation and monitoring in all cases.

3.22 **Information for program monitoring and evaluation.** The executing agency will be responsible for maintaining data gathering and monitoring systems (see monitoring and evaluation plan). The executing agency will commit to maintain a system for monitoring and evaluation of all subcomponents, which it will use to prepare the reports and data delivered to the Bank. For the purposes of the evaluation, the executing agency will compile, store, and safeguard all of information, indicators, and parameters necessary to prepare the PCR, including annual plans and the final evaluation. The executing agency will bear the costs of evaluation and monitoring in all cases. The additional information required for the evaluation process will be drawn from national and international secondary sources of statistical data and, potentially, reports of relevant organizations.

Development Effectiveness Matrix		
Summary	UR-L1171	
I. Corporate and Country Priorities		
1. IDB Group Strategic Priorities and CRF Indicators		
Development Challenges & Cross-cutting Themes	-Productivity and Innovation	
CRF Level 2 Indicators: IDB Group Contributions to Development Results	-Micro / small / medium enterprises financed (#)	
2. Country Development Objectives		
Country Strategy Results Matrix		
Country Program Results Matrix		The intervention is not included in the 2020 Operational Program.
Relevance of this project to country development challenges (If not aligned to country strategy or country program)		See paragraphs 1.12 to 1.19 of the loan document
II. Development Outcomes - Evaluability		Evaluable
3. Evidence-based Assessment & Solution	9.6	
3.1 Program Diagnosis	3.0	
3.2 Proposed Interventions or Solutions	3.6	
3.3 Results Matrix Quality	3.0	
4. Ex ante Economic Analysis	10.0	
4.1 Program has an ERR/NPV, or key outcomes identified for CEA	3.0	
4.2 Identified and Quantified Benefits and Costs	3.0	
4.3 Reasonable Assumptions	1.0	
4.4 Sensitivity Analysis	2.0	
4.5 Consistency with results matrix	1.0	
5. Monitoring and Evaluation	7.0	
5.1 Monitoring Mechanisms	2.5	
5.2 Evaluation Plan	4.5	
III. Risks & Mitigation Monitoring Matrix		
Overall risks rate = magnitude of risks*likelihood	Low	
Identified risks have been rated for magnitude and likelihood	Yes	
Mitigation measures have been identified for major risks	Yes	
Mitigation measures have indicators for tracking their implementation	Yes	
Environmental & social risk classification	B.13	
IV. IDB´s Role - Additionality		
The project relies on the use of country systems		
Fiduciary (VPC/FMP Criteria)	Yes	Financial Management: Budget, Treasury, Accounting and Reporting, External Control, Internal Audit. Procurement: Information System.
Non-Fiduciary		
The IDB's involvement promotes additional improvements of the intended beneficiaries and/or public sector entity in the following dimensions:		
Additional (to project preparation) technical assistance was provided to the public sector entity prior to approval to increase the likelihood of success of the project		

Note: (*) Indicates contribution to the corresponding CRF's Country Development Results Indicator.

Evaluability Assessment Note *: The operation UR-L1171, for USD80,000,000, is part of the Bank's operational response to the COVID-19 Pandemic Global Credit Program for Safeguarding the Productive Fabric and Employment. The general objective of the program is to support the sustainability of Micro, Small and Medium Enterprises (MSME) during the COVID-19 crisis as support of employment in Uruguay. The specific objectives are (i) support financial sustainability of MSME in the short run; and (ii) promote their economic recovery through access to productive credit.*

The loan proposal presents a solid diagnosis of the problem, as well as a review of international evidence. The proposed solutions are an appropriate response to the problems identified in the proposal and its contributing factors. The results matrix is consistent with the vertical logic of the project, presenting adequate indicators at the level of outcomes and impacts. The outcome indicators are appropriately defined to measure the achievements of the project's specific objectives. The impact indicators reflect the contribution to the economic (sustain the percentage of MSME employment in the country and sustain MSME average sales) objectives of the operation.

The economic evaluation shows that the operation is efficient, with an Internal rate of Return of 26% (higher than the 12% discount rate used in the analysis) a NPV of USD461.4 Million. In a context of high uncertainty, the analysis considers the benefits in employment and labor income derived from the reduction of firm's exit rate and reduction in sales drop, while the costs are those associated with the implementation of a financial guarantees.

The monitoring and evaluation plan proposes a reflective analysis of the outcome and impact indicators included in the result matrix, complemented by a review of the theory of change, an updated review of international evidence and qualitative studies. The monitoring and evaluation activities will be carried out by the executing agency, CONAFIN, in coordination with the Bank.

RESULTS MATRIX

Project objective:	The general objective of the program is to support the sustainability of micro, small, and medium-sized enterprises (MSMEs) as employment providers in Uruguay amid the COVID-19 crisis. The specific objectives are to: (i) to support the short-term financial sustainability of MSMEs; and (ii) to promote the economic recovery of MSMEs through access to production-oriented finance.

EXPECTED IMPACT

Indicators	Unit of measure	Baseline 2020	Final target	Means of verification	Comments
GENERAL OBJECTIVE: SUPPORT THE SUSTAINABILITY OF MSMES AMID THE COVID-19 CRISIS					
Indicator 1: Percentage of employment in MSMEs over total employment in the country.	%	57.6	67.8	National Statistics Institute (INE), Directory of Enterprises and Establishments.	The program is expected to help maintain the MSME sector's share of total employment in the country. The baseline corresponds to the most recent measurement of the Directory of Enterprises and Establishments published (corresponding to 2018), considering a loss of 15% consistent with the scenarios of the economic analysis (based, in particular, on differentials found for U.S. firms during the 2008 financial crisis. This is a conservative assumption, since the data already take into account the economic policies implemented for recovery and the country's level of economic development compared to Latin America and the Caribbean).
Indicator 2: Average sales in the MSME sector.	US$ thousands	139.5	164.1	INE (Directory of Enterprises and Establishments, household surveys, wage update index, and national accounts).	The program is expected to help maintain the MSME sector's sales. The baseline corresponds to the calculation using 2019 data and a nominal exchange rate with respect to the U.S. dollar of 43.5, considering a loss of 15% consistent with the scenarios of the economic analysis (based, in particular, on differentials found for U.S. firms during the 2008 financial crisis. This is a conservative assumption, since the data already take into account the economic policies implemented for recovery and the country's level of economic development compared to Latin America and the Caribbean). The exchange rate at the time of the final target is assumed to be 43.5.

EXPECTED OUTCOMES

Indicators	Unit of measure	Baseline 2020	Final target	Means of verification	Comments
Specific objective 1: Support the short-term financial sustainability of MSMEs					
Indicator 1: Rate of arrears in the relevant portfolio of working capital financing or guarantees six months after the start of the program compared with the rate of arrears of private banks.	unit	11.5	6.8	Program monitoring information gathered by SiGa and the Office of the Superintendent of Financial Services.	The relative rate of arrears in the SiGa-PYMES portfolio at the time of program preparation is 3.15 times higher than the rate of arrears of private banks. Considering the importance of public banks in times of crisis, the current situation and the historical evolution of the relative arrears of public banks with respect to private banks must be taken into account to approximate the relative rate of arrears to be expected in a crisis situation. The relative rate of arrears of public banks to private banks at the time of the most recent measurement was 1.54. In turn, the median value of this arrears, which includes periods like those subsequent to the 1998 Asian financial crisis, the 2002 crisis, and the 2008 crisis, is 3.31 (resulting in an expansion factor of 2.15). In turn, the value corresponding to the 75th percentile of the distribution of this arrears is 5.63 (expansion factor: 3.66). To approximate the arrears without the program, the expansion factor corresponding to the 75th percentile is considered (expansion factor: 3.65), while in the situation with the program, the expansion factor corresponding to the 50th percentile is used (2.15), since it is assumed that the program will help sustain the payment chain and the survival of companies), resulting in a relative arrears with the program of 6.8.
Indicator 2. Rate of arrears in the relevant portfolio of working capital financing or guarantees 12 months after the start of the program compared with the rate in private banks.	unit	14.7	11.5	Program monitoring information gathered by SiGa and the Office of the Superintendent of Financial Services.	The relative rate of arrears in the SiGa-PYMES portfolio at the time of program preparation is 3.15 times higher than the rate of arrears of private banks. Considering the importance of public banks in times of crisis, the current situation and the historical evolution of the relative arrears of public banks with respect to private banks must be taken into account to approximate the relative rate of arrears to be expected in a crisis situation. The relative rate of arrears of public banks to private banks at the time of the most recent measurement was 1.54. In turn, the value corresponding to the 75th percentile of the distribution of this arrears, which includes periods like those subsequent to the 1998 Asian financial crisis, the 2002 crisis, and the 2008 crisis, is 5.63 (expansion factor: 3.66). In turn, the value corresponding to the 90th percentile of the distribution of this arrears is 7.18 (expansion factor: 4.7). It is considered that without the program, the relevant expansion factor would be that corresponding to the 90th percentile, but that given the program (and the support for companies and the payment chain), the relative arrears with the program corresponds to the expansion factor of the 75th percentile (factors of 4.7 and 3.66, respectively).

Indicators	Unit of measure	Baseline 2020	Final target	Means of verification	Comments
Specific objective 2: Promote the economic recovery of MSMEs through access to production-oriented finance					
Indicator 1. Rate of arrears in the relevant portfolio of working capital financing or guarantees 24 months after the start of the program compared with the rate in private banks.	unit	6.8	4.9	Program monitoring information gathered by SiGa and the Office of the Superintendent of Financial Services.	The relative rate of arrears in the SiGa-PYMES portfolio at the time of program preparation is 3.15 times higher than the rate of arrears of private banks. Considering the importance of public banks in times of crisis, the current situation and the historical evolution of the relative arrears of public banks with respect to private banks must be taken into account to approximate the relative rate of arrears to be expected in a crisis situation. The relative rate of arrears of public banks to private banks at the time of the most recent measurement was 1.54. In turn, taking the relative values observed between months 18 and 30 after recent periods of crisis (1998, 2002, 2008), an expansion factor of 2.4 is approximated, which when applied to the relative arrears value at the time of the most recent measurement available, yields a result of 4.9. In the situation without the program, it is assumed that the relative arrears would be in line with the 50th percentage of the distribution (expansion factor: 2.15).
Indicator 2: Total amount of the relevant portfolio of production-oriented finance achieved as a result of program support.	US$ millions	45.6	125.6	Program monitoring and supervision information gathered by SiGa.	Loans guaranteed by SiGa as of 2019 reached US$45.6 million. This is considered as the relevant portfolio because the program is expected to serve the same set of sectors that are included in the operation, given its multisector nature. The target corresponds to a conservative scenario with respect to the volume of loans guaranteed by SiGa (the majority of which is expected to be from the SiGa Emergencia line) that are leveraged using program resources.

OUTPUTS

Outputs	Unit of measure	Baseline 2020	Year 1	Year 2	Final target	Means of verification	Comments
Subcomponent 1: Support for improvement of short-term financial capacity (Total cost = US$60 million)							
Output 1: Amount provided to finance guarantees granted on loans for MSMEs.	US$ millions	0	30	30	60	Program monitoring and supervision information collected by SiGa.	Corresponds to the amount of the operation devoted to the capitalization of the guarantee fund.
Subcomponent 2: Support for access to production-oriented finance for economic recovery (Total cost = US$20 million)							
Output 2: Amount provided to finance guaranteed granted on loans for MSMEs.	US$ millions	0	10	10	20	Program monitoring and supervision information collected by SiGa.	Corresponds to the amount of the operation devoted to the capitalization of the guarantee fund.

Country: Uruguay **Sector:** CMF **Project number:** UR-L1171 **Year:** 2020
Cofinancing: N/A. **Co-execution:** N/A.

FIDUCIARY AGREEMENTS AND REQUIREMENTS

Executing agency: Corporación Nacional Financiera Administradora de Fondos de Inversión S.A. (CONAFIN-AFISA)

Project name: Global Credit Program for Safeguarding the Productive Fabric and Employment

I. THE EXECUTING AGENCY'S FIDUCIARY CONTEXT

1. Use of country systems in the project[1]

Budget	■	Reports	■	Information system	■	National competitive bidding	☐
Treasury	■	Internal audit	☐	Shopping	☐	Advanced national competitive bidding	☐
Accounting	■	External control	■	Individual consultants	☐	Consulting firm	☐

Laws/regulations applicable by the executing agency: Decree 773/2008 creating the National Guarantee System, Law 16,696 Charter of the Central Bank of Uruguay and the laws amending it, Law 17,703 the Trust Act.

2. Fiduciary capacity of the executing agency

The fiduciary capacity was evaluated using the ICAP (simplified and virtual), concluding that financial management and project coordination is adequate for the management of the operation. As a global credit program, no procurement is envisaged. Therefore, no analysis of procurement capacity was carried out. CONAFIN-AFISA is owned by the National Development Corporation (CND), which is the executing agency of loan 3578/OC-UR, and well as borrower of said loan and loan 4824/OC-UR.

3. Fiduciary risks and mitigation actions

Fiduciary risk: High ☐; Medium ☐; Low ■

Risk	Risk level (Medium/High)	Mitigation plan
No medium or high fiduciary risks were identified.		

[1] Any system or subsystem that is subsequently approved may be applicable to the operation, in accordance with the terms of validation by the Bank.

II. Considerations for the Special Provisions of the Contract

Conditions precedent to the first disbursement: There are no conditions of a fiduciary nature.
Exchange rate: For the rendering of accounts, the applicable exchange rate will be the rate in effect on the day when the respective guarantee is established for the financial intermediary.
Audited program financial statements: The executing agency will submit audited annual financial statements for the program in accordance with the terms of reference agreed upon with the Bank, within 120 days following the close of the executing agency's fiscal year. The final financial statements for the program will be delivered within 120 days after the date of the last loan disbursement. The project audit will be conducted by the Office of the Auditor General or a Bank-eligible independent audit firm, under the procedures established in the current audit guidelines.
Prohibited practices: In the agreements between the executing agency and its financial intermediaries, and the other contracts financed with Bank resources, the due clauses regarding the Bank's prohibited practices will be included.

III. Agreements and Requirements for Procurement Execution

Exceptions to policies and guidelines:

• No exceptions anticipated.

Retroactive financing and/or advanced procurement	• The Bank may retroactively finance eligible expenditures made by the borrower prior to the loan approval date for the granting of guarantees to financial intermediaries associated with loans granted to MSMEs under the program for up to the amount of US$16 million (20% of loan amount), provided that requirements substantially similar to those established in the loan contract and the credit regulations were met. These expenditures will have been made on or after 6 April 2020, the date on which the SiGa Board of Directors formally approved the new SiGa Emergencia line of guarantees to serve MSMEs affected by the health emergency caused by COVID-19. Although this date is prior to the date the project officially entered the pipeline (document GN-2259-1), due to the exceptional circumstances the crisis is expected to have on the deterioration of the MSME portfolio, and considering the large growth in demand for loan guarantees under the SiGa Emergencia line of guarantees since its creation, exceptional authorization of retroactive financing as of this date is justified.
Supplementary procurement support	• N/A.
Alternative procurement arrangements	• N/A.

Projects with financial intermediaries	• As this loan is for global credit programs and other operations in which resources are provided to financial intermediaries that will in turn issue guarantees, it will be stipulated that the Bank's prohibited practices clauses are to be included in the agreements between the executing agency and its financial intermediaries. Alternatively, if the effective inclusion of these clauses in the aforementioned contracts is not possible or practical in view of the program's circumstances, the project team may examine other mechanisms to adopt acceptable controls and duly bind the relevant third parties to the Sanctions Procedures. The design of these mechanisms will be coordinated with the Office for Institutional Integrity (OII), with the support of the Legal Department, and they will be set forth in the Credit Regulations.
Procurement agents	• N/A.
Direct contracting	• N/A.

Operating expenses will be financed: ☐ N/A.	**Domestic preference:** ☐ N/A.

General supervision methods for project procurement: N/A.	
Supervision method: N/A.	**For:** N/A.

Country thresholds: www.iadb.org/procurement

IV. Agreements and Requirements for Financial Management

Programming and budget	• CONAFIN-AFISA manages the funds it administers on the basis of periodic programming based on the scope of the funds it administers and on a demand analysis thereof. The CND will periodically transfer the resources budgeted by CONAFIN-AFISA to address its financial needs.
Cash and disbursement management	• Disbursements will be made in the form of advances of funds and reimbursements. • Disbursements will be made upon submission of electronic disbursement requests in the system defined by the Bank for such purposes. • Bank account: CND will receive the Bank's disbursements in a designated account at the Central Bank of Uruguay (BCU). • Financial plan: Advances will be made for a period of up to 6 months, depending on the estimated demand by the executing agency. • Percentage for rendering of accounts: 80% of the balance of advances pending justification. • Project cash flow: Funds are disbursed to the borrower (CND) in the designated account at the BCU, from where they will be transferred to an exclusive account of CONAFIN-AFISA, opened at Banco de la República (BROU), if they are advances, or to the account indicated by CND and CONAFIN-AFISA if they are reimbursements of payments.

Accounting, information systems, and reporting	• Specific accounting standards: Regulatory framework of the Central Bank of Uruguay – based on the International Financial Reporting Standards (IFRS). • Reports for rendering of accounts: Statement of cash and disbursements made and Statement of cumulative investments, prepared based on information in the CONAFIN-AFISA information system. • Accounting method and currency: Accounts will be kept on an accrual basis, but the program's financial reports will be prepared on a cash basis, in U.S. dollars.
External control	• With the agreement of the Bank, the executing agency will select and contract the services of an eligible auditor, in accordance with the terms of reference agreed upon with the Bank. Alternatively, the project audit may be conducted by the Office of the Auditor General.
Financial supervision of the project	• Financial supervision will be conducted by means of working meetings and reviewing reports and audited financial statements.

V. RELEVANT INFORMATION FOR THE OPERATION

Policies and guidelines applicable to the operation

Financial management	**Procurement**
• Document GN-2811 [OP-273-12]	• Document GN-2349-15 • Document GN-2350-15

Records and files

CONAFIN-AFISA has digital and physical files, as well as procedures and instructions allowing appropriate records and files to be kept.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-__/20

Uruguay. Loan ____/OC-UR to the Corporación Nacional para el Desarrollo. Global Credit Program for Safeguarding the Productive Fabric and Employment

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Corporación Nacional para el Desarrollo, as borrower, and with the Eastern Republic of Uruguay, as guarantor, for the purpose of granting the former a financing aimed at cooperating in the execution of the Global Credit Program for Safeguarding the Productive Fabric and Employment. Such financing will be for the amount of up to US$80,000,000 from the resources of the Bank's Ordinary Capital, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on ___ ____________ 2020)

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