PROGRAM INFORMATION DOCUMENT (PID)
CONCEPT STAGE

March 13, 2014
Report No.: AB7554

Operation Name	Fiscal Space for Greater Opportunities Second Programmatic Development Policy Loan
Region	Latin America and Caribbean
Country	Guatemala
Sector	Central government administration sector (100%).
Operation ID	P133738
Lending Instrument	Development Policy Lending
Borrower(s)	Republic of Guatemala
Implementing Agency	Ministry of Public Finance Government of Guatemala 8va Avenida 20-65, Zona 1 Centro Civico, Nivel 15 Ciudad de Guatemala, Guatemala
Date PID Prepared	March 13, 2014
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I. Key Development Issues and Rationale for Bank Involvement

Guatemala is the largest economy in Central America and its economic performance has been relatively stable compared to the rest of the Latin America and the Caribbean (LAC) region, a result of prudent macroeconomic policies. Guatemala's GDP is about US$53 billion (2013) and its per-capita gross national income (GNI) is US$4,880 (2012). It has a multiethnic population of about 15 million. Between 2001 and 2013 annual GDP growth averaged 3.3 percent (the LAC average was 3.4 percent), and less volatile than the region. Democratic institutions have been consolidating following a 36-year civil war that ended in 1996. Despite progress, however, persistent economic and social challenges have affected the population's trust in the Government's capacity to eradicate poverty and boost shared prosperity.

Guatemala has made modest progress in poverty reduction since 2000. Guatemala reduced its poverty headcount rate between 2000 and 2006 from 56.2 percent to 51 percent according to national estimates. Extreme poverty decreased from 15.7 percent in 2000 to 15.2 percent in 2006. In the wake of the global financial crisis, poverty rates increased. The latest household survey indicates that the poverty rate increased from 51 percent in 2006 to 53.7 percent in 2011, although extreme poverty did decrease during this period from 15.2 in 2006 to 13.3 in 2011. Poverty is disproportionately concentrated in rural areas and amongst the indigenous population. Despite marginal increases in poverty, inequality improved slightly between 2006 and 2011, explained by modest reduction in extreme poverty and improvements in the middle class income.

Since 2000 shared prosperity worsened as Guatemala was the only country in LAC for which the income growth rate of the bottom 40 percent was negative (-1 percent) during 2000-2011; meanwhile, social indicators remain weak compared to other middle-income countries. The country has achieved some progress during the last decade on social indicators. Rates of primary school enrollment (general population and for girls) increased by 12 and 15 percentage points, respectively, during 2000-2010. In the same period, rates of childhood mortality declined from 49 to 32 per thousand. Yet, in addition to being modest, coverage to basic goods and services is often unequal, which limits the set of economic opportunities, particularly for the most vulnerable. This is evidenced by Guatemala's low Human Opportunity Index (which measures how equitable is the access to basic goods and services), which is among the lowest in LAC. Despite recent progress on reducing underweight in children, Guatemala's level of chronic malnutrition remains among the worst in the world, with about half of all the children suffering from malnutrition. The Government plans to undertake a new household survey in 2014 to overcome data limitations that currently limit the ability to evaluate recent progress in poverty reduction and shared prosperity.

The Government has committed itself to an ambitious agenda that aims to address key development challenges. These include improving social development, accelerating economic growth, ensuring productive and social infrastructure for development (especially in rural areas), and strengthening justice and democratic security. The Government has also placed strong emphasis on promoting transparency and accountability, and reducing crime and violence.

This programmatic DPL series of Fiscal Space for Greater Opportunities has been supporting this reform program, and the proposed Second DPL is fully consistent with the objectives of the World Bank Group's Strategy. This DPL builds on the progress achieved under the previous operation and complements it by focusing on a limited set of cross-sectorial policies intended to increase fiscal space and support a more efficient delivery of quality public services. In particular, it supports two pillars of the Guatemala Country Partnership Strategy (CPS) discussed by the Board in September 2012, namely: pillar one (create fiscal space and improve transparency in the budgeting process), and pillar two (improved results in the social sector). The proposed operation, in coordination with the efforts of other development partners, will provide fiscal resources to support the Government's poverty reduction and shared prosperity efforts. In addition, to enhance its policy dialogue, the World Bank Group is engaged in a series of analytical and advisory activities in support of envisaged reforms in this DPL, in the areas of economic governance, poverty and equity monitoring, and competitiveness.

II. Proposed Objective(s)

The Program Development Objective of the DPL series is to support the Guatemalan Government in creating fiscal space and expanding opportunities for the most vulnerable segments of society.

III. Preliminary Description

The proposed operation is the second in a series of two single-tranche operations, the first of which was approved by the World Bank Group Executive Board of Directors in September 2012. This DPL series is informed by the lessons learned in previous World Bank

operations and supports three policy objectives: (i) strengthening tax administration and tax policy; (ii) enhancing budget management and increasing the results orientation of public spending; and (iii) improving the coordination and management of social policy. Measures focused on mobilizing revenues, raising the efficiency of spending, and improving the coordination of social policies support the Government's goal of reducing poverty and promoting shared prosperity. Enhanced transparency of public resources contributes to the Government's goal to foster growth by improving the country's image with foreign investors.

IV. Poverty and Social Impacts and Environment Aspects

Poverty and Social Impacts

Government actions supported in this DPL are expected to have positive poverty and social impacts. The analysis carried out on the potential impacts of the reforms supported under DPL1 showed a positive or neutral impact for each of the reforms. Progress has been made in the implementation of key reforms that affect poor and vulnerable populations in the area of social protection, such as the creation of Zero Hunger Offices and the creation of the Single Beneficiary Registry which will help ensure that households receive all benefits for which they are eligible. The introduction of new inter-ministerial coordination mechanisms are also expected to improve welfare of vulnerable groups.

The tax system is expected to become more progressive as a result of the tax reform, and the impact of the tax reforms is expected to fall mainly on the upper decile of the income distribution and is unlikely to have a direct impact on the poor and vulnerable. The analysis carried out on the impact of the tax reform under DPL1 confirmed that the direct impact of the changes in the tax code will likely be felt only among the top income decile. The tax reform also aims to increase the share of direct taxes, which has the potential of making the tax system more progressive. Furthermore, additional fiscal space, a central objective of this DPL series, will give the Government the resources to deliver a more ambitious social contact and expand economic opportunities for all citizens.

Tax information sharing and the procurement reform are not expected to directly impact poverty or the distribution of incomes. However, indirect effects could occur, for example, based on an overall increased transparency which could generate an improved business environment and therefore more employment through enhanced competitiveness.

Measures related to social protection programs are expected to generate significant, positive impacts for the poor. The size of this impact depends on the quality of targeting of these programs. The development of tools to improve the monitoring and evaluation of social programs, including advances in Results-Based Management and the Single Beneficiary Registry are important milestones in the promotion of shared prosperity in Guatemala. Analysis conducted under DPL1 using the latest household survey (ENCOVI 2011) as well as the latest National Maternal and Infant Health Survey (ENSMI 2008-09) noted the potential positive impacts of improving Results-Based Management. In this regard, evidence from other countries emphasizes the positive impacts of RBM as a tool to reduce poverty and promote shared prosperity, including: (i) an informed budget that enhances the transparency and accountability

of public resources; and (ii) an enhanced monitoring and evaluation system, in particular with regards to social programs.

Improving the coordination of social policy is also expected to promote shared prosperity in Guatemala. Pillar 3 of the proposed DPL aims supports government efforts to tackle infant malnutrition and maternal mortality in geographic areas with high malnutrition rates and improve the monitoring and evaluation framework and the unique registry of beneficiaries. A better targeted social program is expected to be more progressive as it will help ensure that the resources will be channeled to those in most need and expected to benefit the most from public social expenditures. Indeed, the use of the recently completed Poverty Maps (2006, total; 2011, rural) could help substantially to increase the effectiveness of targeting mechanisms. Similarly, focusing the budget on results according to social needs greatly improves its progressive nature.

Environmental Aspects

The measures supported under the proposed DPL are not likely to have significant effects on the environment, forests or other natural resources. The increase in the taxes on motor vehicles (prior action 1) is unlikely to have a negative significant impact on emissions and air pollution since the taxes are paid as a lump sum annually and are not on a per use basis thereby providing limited incentives to have an effect on the use of vehicles. Policy actions in the areas of tax administration, public expenditure and social policy are not likely to have either significant positive or negative environmental impacts.

V. Tentative Financing

Source:	($million)
Borrower	0
International Development Association	340
Total	340

VI. Contact Point

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