



***PARAGUAY***

***2024 -***

***June***

***Component: Expenditure Policy***

***Modules: SM I – Spending Policies***

*PARAGUAY*

| PROJECT SUMMARY           |                                   |
|---------------------------|-----------------------------------|
| COUNTRY:                  | Paraguay                          |
| LEAD DEPARTMENT:          | FAD                               |
| REGION:                   | WHD                               |
| PROGRAM ID:               | [To be filled out by Secretariat] |
| PLANNED DATES:            | FY25-FY27                         |
| FUNDING PROGRAM TITLE:    | [to be added by Secretariat]      |
| PROJECT MANAGERS:         |                                   |
| SM I – SPENDING POLICIES: | Nick Carrol, Nick (FADEP)         |
| ESTIMATED BUDGET          | \$164,799                         |
| BUDGET FOR ENDORSEMENT:   | \$98,378                          |

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*PARAGUAY***ACRONYMS**

|     |                                 |
|-----|---------------------------------|
| CD  | Capacity Development            |
| FAD | IMF's Fiscal Affairs Department |
| PCI | Policy Coordination Instrument  |

*PARAGUAY***I. PROJECT PURPOSE**

**At the 2023 Annual Meetings authorities requested support in FY25 on their upcoming reforms to social, security, civil servant pension funds and public sector compensation.** This has been confirmed in follow-up discussions with a particular focus on developing pension fund reform options and modelling ahead of reform proposals being tabled in parliament in the second half of 2024.

**Strengthening the viability of pension funds was identified in the Second Review of the Policy Coordination Instrument (PCI) as a significant reform.** This Capacity Development will provide advice to the authorities on assessing the financial sustainability of social security (Instituto de Previsión Social (IPS)) and other pension fund parameters; identifying alternative reform options and their potential savings / costs; and developing recommendations for measures to improve the pension system. Complementary to this, there will also be support on assessing public compensation reform options.

**The estimated budget for this two-year project is \$164,799 but endorsement is requested for \$98,378 in FY25.** Endorsement for future plans will be requested at a later date as funding for the program is secured and reform plans gain traction.

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## II. BACKGROUND

### Macro-fiscal situation

In June 2023, the Paraguayan central government fiscal deficit, the current primary expenditure, and the net incurrence of floating debt limits were close to the targets set in the IMF PCI program. However, at the end of the year the fiscal position might turn out to be weaker as the new government intends to register and regularize outstanding claims from private contractors accrued during the pandemic. Afterwards, the fiscal deficit is expected to gradually converge to the 1.5 percent of GDP deficit ceiling of the fiscal rule by 2026. The pension system of public employees (“Caja Fiscal”) was identified in the IMF Staff Report of the Second Review under the PCI as an important fiscal vulnerability, and ensuring the sustainability of social security and public compensation is a priority.

### Country engagement and alignment to reform priorities

This capacity development (CD) will support an improved understanding of the fiscal impacts of the design of social security and other pension parameters and identify reform options to improve sustainability, efficiency and adequacy of that spending. It will therefore align with the priorities for the better management of the pension system of public employees identified in IMF Staff Reports.

## III. PROJECT MODULES - DESCRIPTION

This proposal will provide CD support to Paraguay in the area of spending policies. The IMF’s Fiscal Affairs Department (FAD) will provide CD to support improvements within the strategic objectives presented in Table 1:

**Table 1. Summary of Objectives covered by the Proposal**

| Component | Module                   | Objective                                            |
|-----------|--------------------------|------------------------------------------------------|
| Spending  | SM I / Spending Policies | Strengthen Expenditure Policy Formulation and Design |

### A. SM I – Spending Policy

#### Scope

The main priority for this program is support for the authorities in improving the sustainability of pensions and social security. Strengthening the viability of the pension system was identified in the Second Review of the PCI as a significant issue. Field-Based CD in this area will provide advice to the authorities on: (i) assessing the financial sustainability of social security and pension parameters, (ii) identifying alternative reform options and their potential savings / costs, and (iii) developing recommendations for measures to improve the efficiency, adequacy and sustainability of the pension and social security (including health) systems.

Building capacity in the areas of social security, pensions and public compensation is a priority to ensure improved policy capability and integration with decision-making. This proposal therefore

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also includes two additional capacity building activities. The purpose of these two activities is to provide timely, targeted advice and training to support the authorities in their reform.

- The interactive learning (in-person workshop) in FY26 will provide training on the social security and pension mission output, with a particular focus on modelling the costs and savings or alternative reform options.
- A final activity is included for FY26 is an HQ-based desk review of the public compensation proposal, which would assess the fiscal implications associated with the proposal, options to manage the fiscal issues and recommendations on short and medium-term priorities.

### Program Objectives

**The main program objective within the spending module is to rationalize public expenditure in the short term.** The immediate priority is to support authorities' efforts to undertake civil service pension reforms (excluding military and security workforces). Two supplementary activities are to provide HQ-based review of a public compensation reform and interactive training in FY26. CD activities will focus on:

- Assessing the financial sustainability of social security and pensions, identifying parametric reform options that can improve the sustainability of the funds, and modelling the savings associated with the reform options (FY2025).
- Completion of a desk review of the policies managing government compensation and employment, including key design elements and areas for reform (after the civil service reform and structure of the state laws have been passed) (FY2026).
- A follow-up activity on the social security and pension parameters will provide interactive training on the civil service pension reform options and modelling (FY2026).

### Expected Results (outcomes)

**CD support under this program should achieve the following:**

- An assessment of the costs of the current social security and pensions systems, their sustainability and options for reform.
- A modelling of the long-run savings/ costs of reform options for social security and pensions.
- Increased capacity of the authorities to independently undertake high-quality policy analysis of reform options to improve the financial sustainability and fairness of the civil service pensions.
- Tailored advice on civil service remuneration and pension policy.

## IV. ORGANIZATIONAL ARRANGEMENTS

### A. Country Engagement

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This spending area is a new area with new engagement with Paraguay. It is building on mature frameworks and analytical pension and public compensation spending policy tools that have been used elsewhere for Capacity Development and applied to the specific challenges in Paraguay.

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### B. Delivery Modalities

**CD will comprise of a mix of remote and in-person activities.** Virtual deliveries will be used to provide efficiencies to in-person support, including pre-engagement meetings and post-follow-up meetings. The following CD activities will be delivered as a package:

- **Headquarters-led (HQ) missions and staff visits** to provide strategic recommendations, conduct regular follow-ups, assess progress, ensure short-term expert (STX) work is aligned to plans, coordinate with other CD providers, and adjust reform implementation plans.
- **Workshops**, during the HQ missions, staff visits, or STX visits, to share experiences, provide stakeholders with a view of progress achieved and challenges faced, and discuss with the managers and staff their views on the reforms and particular technical subjects.

The project makes provision for appropriate HQ backstopping and project management. Funding for FY25 is assumed to be available from May 2024. Activities and budgets for FY25, FY26, and F27 will be developed in light of progress.

### C. Coordination / Cooperation

Collaboration with other capacity development providers will be promoted with a view of enhancing the relationship among the various partners working in Paraguay.

| Coordination                                                                      |                                                                              |                                                                                                         |                                       |
|-----------------------------------------------------------------------------------|------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------|---------------------------------------|
| Partner                                                                           | Type of coordination                                                         | Area of coordination                                                                                    | Frequency                             |
| IMF's area department country team, IMF's Monetary and Capital Markets department | Supporting program benchmarks, and CD Design and delivery, and joint support | Social Security (IPS) and Civil servant pension fund parametric reform and management                   | Quarterly                             |
| Cooperation                                                                       |                                                                              |                                                                                                         |                                       |
| Partner                                                                           | Type of coordination                                                         | Area of coordination                                                                                    | Frequency                             |
| Inter-American Development Bank and World Bank                                    | Coordination meetings and exchange of work plans to align work plans         | Social Security, Civil servant pension and public compensation reform option development and modelling. | Before and after CD delivery (Annual) |

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## V. RISK ASSESSMENT AND MITIGATION

| General or Module                                            | Description                                                | Risk Assessment | Mitigation Measures                              |
|--------------------------------------------------------------|------------------------------------------------------------|-----------------|--------------------------------------------------|
| <b>Political Support</b>                                     |                                                            |                 |                                                  |
| SM I                                                         | Pensions and wage bill can be contentious                  | Very High       | Discuss communication plans with authorities     |
| <b>Management and Technical Staff Support and Commitment</b> |                                                            |                 |                                                  |
| SM I                                                         | Pension modelling requires high level capacity and support | Medium          | Review technical capacity and support, as needed |

## VI. CD DELIVERY PLAN

Table 2. Summary of Indicative CD Delivery

| CD Modalities<br>(Remote or Field-based CD) | FY25 | FY26 | FY27 | FY28 | FY29 | Grand Total |
|---------------------------------------------|------|------|------|------|------|-------------|
| <b>SM I – Spending Policies</b>             |      |      |      |      |      |             |
| HQ led CD mission                           | 1    | 1    | -    | -    | -    | 2           |
| Interactive Learning (in-person workshop)   | -    | 1    | -    | -    | -    | 1           |
| Total                                       | 1    | 2    | -    | -    | -    | 3           |

Note:

- In-person delivery was chosen in most instances to support a new CD engagement on expenditure policy in a program country and because of the sensitivity of the CD messages on pensions being conveyed.
- Remote delivery was chosen in one instance because of the short duration of the activity and the cost of travel.
- Collectively the blend of CD delivery proposed over the duration of this project/program reflects the optimal balance of in-person, remote, and hybrid activities needed to achieve the project/program outcomes taking into account the needs of the country and the resources available.

Table 3. First year workplan

| Timing                          | CD Modality                               | CD Delivery | Proposed Topics of CD                                                                      |
|---------------------------------|-------------------------------------------|-------------|--------------------------------------------------------------------------------------------|
| <b>SM I – Spending Policies</b> |                                           |             |                                                                                            |
| FY25 – Q1                       | HQ-led CD Mission                         | HQ (FB)     | Reform options to improve the viability of social security and civil service pension funds |
| FY26 – Q1                       | Interactive learning (in-person workshop) | HQ (FB)     | Workshop on social security and pension reform analysis                                    |
| FY26 – Q2                       | HQ activity                               | HQ (HQ)     | HQ based support for civil service compensation reform                                     |

*PARAGUAY***VII. PROGRAM FINANCIALS**

|                                | <b>FY25</b> | <b>FY26</b> | <b>FY27</b> | <b>FY28</b> | <b>FY29</b> | <b>Total</b> |
|--------------------------------|-------------|-------------|-------------|-------------|-------------|--------------|
| SM I – Spending Policies       | \$91,942    | \$62,076    | -           | -           | -           | \$154,018    |
| <b>Subtotal</b>                | \$91,942    | \$62,076    | -           | -           | -           | \$154,018    |
| Trust fund management fee (7%) | \$6,436     | \$4,345     | -           | -           | -           | \$10,781     |
| <b>Total</b>                   | \$98,378    | \$66,421    | -           | -           | -           | \$164,799    |

The estimated budget for this three-year project is \$131,589, but endorsement is requested for \$98,378 through FY25. Endorsement for future plans will be requested at a later date as funding for the program is secured and reform plans gain traction.

**VIII. TARGETED LOGICAL FRAMEWORK****A. SM I – Spending Policies**

| <b>Objective</b>                                                                                  |                                                     |
|---------------------------------------------------------------------------------------------------|-----------------------------------------------------|
| <b>Strengthen Expenditure Policy Formulation and Design</b>                                       |                                                     |
| <b>Outcome(s)</b>                                                                                 | <b>Indicator(s)</b>                                 |
| Public pension system sustainability is enhanced while ensuring the adequacy of retirement income | Main pension parameters, including pension coverage |
| Public expenditure is fiscally sustainable and efficient                                          | Primary spending, in percent of GDP                 |