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ILO NOTES ON THE CRISIS

PARAGUAY
PUBLIC INVESTMENT AS A COUNTER-CYCLICAL TOOL TO FACE THE CRISIS

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In the face of the economic crisis, Paraguayan authorities have raised allocation of resources and execution of public investments. If all resources allocated to public investment in the 2009 budget were totally executed, the estimated impact created would amount to 16,000 additional jobs throughout the year. This estimate does not include execution of additional funds from international financial cooperation organizations or bi-national power plants, utilization of which requires approval by Parliament.

To this should be added the effect of a number of measures designed to increase the use of labour rather than machinery in public investments, via improved access to public contracts for micro and small enterprises and introduction of a routine road-maintenance system. Beyond the current economic crisis, these efforts mean significant improvements in the economic policy of the nation, even though their short-term effect on employment may be modest or difficult to measure. In this context, introduction of a system to measure the impact of public investment on employment becomes especially important.

1. Introduction

Public investment is part of an economic policy agenda favouring employment in the long-term as well as in the situational response to the economic crisis. This paper illustrates in the case of Paraguay some measures and opportunities in the present situation, together with some short- and long-term challenges, limitations, and tensions.

From a long-term perspective it may be observed that public investment in developing countries is generally executed with more machinery and less labour than would be socially desirable. On account of this, ILO is providing advice to Governments, aiming to increase participation by micro enterprises and creation of employment via improvements to project design, tender procedures, and the regulatory framework related to public tenders.[2] In turn, during economic crises such as the present one, appreciation of public investment rises as a key item of counter-cyclical packages designed to offset partially the lower economic activity in the private sector.

2. Programme description I: Permanent policies

For some years now, the Paraguayan authorities have been working on applying a labour-intensive approach to public investment in national policies.[3] Since President Fernando Lugo took office in August 2008 these efforts

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2 For further information, see http://www.ilo.org/public/spanish/employment/recon/eiip/about/lbt.htm.
3 See Aguilera and Cartier (2006) and Yeng, Sosa and Cartier (2007).

have intensified, pursuing a more significant role for employment in economic and social policies.[4] In this context, the following developments may be mentioned.

Improvements in public-contract procedures

It is common knowledge that contract procedures are an obstacle for micro and small enterprises –which tend to execute works in a more labour-intensive, less equipment-intensive way than larger corporations– to gain effective access to public contracts. In response to this problem, reforms have been made at various levels:

- Although the Law regulating public contracts in Paraguay has not been amended, Decree 1434/2009 was issued, giving preferential access to public contracts to micro, small, and medium-sized companies, defining this type of company and giving them a chance to submit a second proposal when the price of the first topped by up to 5% that of a larger company.[5]
- At the administrative level, a document was issued "Standard letter of invitation for direct-contracting processes", intended to simplify the requirements made to companies contracted by the State in this mode involving relatively low amounts, avoiding exaggerated demands that prevent smaller organizations from participating.

Introduction of a routine road-maintenance system with micro enterprises

In several countries of Latin America, road construction and maintenance has been the main field of application of the labour-intensive approach to public investment. In Paraguay, a routine road-maintenance system is being introduced with micro enterprises.[6] Routine maintenance is distinct from periodical or corrective maintenance in that it is performed more frequently, while no major damage has yet been done to the roads, and mainly consists in cleaning and minor repairs that can be performed with little machinery and the use of local labour, which helps to maintain roads in good shape for a longer time.

To introduce the routine maintenance programme, micro enterprises will be created, promoted, and trained initially by the Ministry of Public Works and Communications (*Ministerio de Obras Públicas y Comunicaciones - MOPC*). A new Micro Enterprises Unit was created for this purpose at MOPC and initial pilot company experiences were conducted in 2008 working on dirt roads.

In the alternative mode, certain sections of paved roads were chosen in the central area of the country and MOPC proceeded to select and hire workers –both men and women– to make up routine-maintenance crews. Workers are paid a daily wage based on the minimum wage, for 40 hours a week, and provided with occupational accident insurance. However, they are not registered with Social Security (Instituto de Previsión Social). The work consists mainly in cleaning the public strip of road (weeding, unclogging drains, etc.). The MOPC is gradually converting successful crews into micro enterprises mode.

To date the number of persons working on routine road maintenance is relatively low –no more than 350 workers. The aim is for these companies to become sustainable over time and for the system gradually to extend to all roads of similar characteristics throughout the country.

Progress in the introduction of employment as an item of public investment management

One paradox in the socioeconomic policy of many countries is that job creation is a stated aim but no mechanisms or tools are available to assess and monitor the impact on employment. To overcome this weakness the Paraguayan Ministry of Finance is working with ILO on the introduction of a system for priority-setting, assessing and monitoring job-creation in public investment. Full introduction of the system will take place in the future, in the framework of launching a Public Investment System (*Sistema de Inversión Pública – SIP*), where one priority-setting indicator for infrastructure projects will be the number of jobs created and employment measurement will be component of the monitoring system.

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4 In addition, the main role of employment in national public policy is reflected in the Youth Employment Creation Panel (*Mesa de Creación de Empleo Juvenil),* under the leadership of the Ministry of Justice and Labour, the substantive strengthening of the National Employment Service in the purview of the same Ministry, together with the inclusion of employment aims in the 2008-2013 Economic-Social Strategic Plan.

5 http://www.dncp.gov.py/app/q_a_pls.jsp

6 See Salomon et al. (2009).

3. Programme description II: Response to the crisis

As in other countries, public investment as a mechanism for defending employment is playing a key role in the response of the Paraguayan authorities to the economic crisis. The main measures adopted include raising the amounts allocated to public investment during 2009 –a programme contemplating decentralized allocation of funds for executing public works through Municipalities and Governor's Offices– and rapid introduction of routine road-maintenance crews through direct hiring of workers.

Increased amounts for public investment

In the 2009 budget –prepared before the Paraguayan economy was drawn into the context of world crisis– the funds for public investment allocated to the agencies of the Central Administration amounted to 1,967,731 million guaraníes (US$ 394 million),[7] less than the amount budgeted for fiscal year 2008. Reacting to the crisis, the authorities obtained additional loans from international financial cooperation agencies –mainly the World Bank and the IDB– which will increase allocations for public investment in 2009 and following years by a total of about US$ 100 million.

However, the country's historical experience shows that actual execution of public investment in 2008 and preceding years averages just over 50% of the budget; hence the main short-term challenge lies in full execution of available resources rather than allocation of additional funds. As a result, the Ministry of Public Works and Communications and the Ministry of Finance announced special efforts to speed-up execution, without introducing legal amendments to the regulatory framework within which such funds are executed.

Execution of public investment from January to June 2009 showed some outcome of this action, US$ 103.7 million in public investment having been executed, or 34% more than in the same period of 2008. If this result is extended over the entire year, the effect of such increased execution –with no additional project or raising the intensity of investment in employment– approximately 6,500 jobs would be created throughout the year. If the entire 2009 budget were totally executed, the additional creation of employment by comparison with 2008 would be 16,000 jobs, equivalent to almost 10% of the total unemployed at the end of 2008.[8] Introduction of routine road maintenance with local labour is simultaneously being speeded-up (see section 2 above).

Execution of works through Municipalities and Governor's Offices

Decentralized public investment has advantages by comparison to centralized investment through Ministries in the Central Government. Some of these advantages are especially important in a context of crisis. First, decentralized decision-making usually arouses firmer commitment by the local population vis-à-vis the works and their proper use and maintenance. Secondly, smaller works are usually undertaken and contracts usually involve lower figures, in turn implying less need for heavy machinery and more job creation in relation to the sum invested. Thirdly, decentralized contracts are more likely to be executed by local enterprises with local workers, with the resulting reactivation of the local economy.

In the face of the crisis, the Central Government proposed labour-intensive projects for investment in municipal infrastructure through two decentralized public-investment programmes, in addition to decentralized investments already under execution with Municipal or Governor Office funds. First, agreements were executed by the Yaciretá and Itaipú bi-national power plants, the Ministry of Finance, and the Governor Offices of six Departments in the country (Concepción, San Pedro, Caaguazú, Caazapá, Misiones, and Ñeembucú) covering allocation of a total US$ 6 million (US$ 1 million per Department). Under the agreements, the programme will develop projects requiring mass labour, such as cobbling, paving, construction of bridges, sewers, containment walls, slaughterhouses, urban buildings, and similar works, including repairs involving major demand for labour. Secondly, among the additional loans obtained by the Ministry of Finance from the World Bank, US$ 34 million are been allocated to decentralized public investment in each of the 17 Departments of Paraguay, at the rate of US$ 2 million per Department. If these two decentralized programmes are executed in the space of one year, approximately 4,800 annual jobs would be created.[9]

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7 Based on an exchange rate of 1 US$ = 5,000 guaraníes.

8 Estimate calculated using of 30% of the total amount invested in labour expenditure.

9 The initial duration of agreements with bi-national organizations is 9 months; however, possible extension is expected. For decentralized public investment, expenditure on labour is calculated at 40% of the total amount invested.

Given that approval by Parliament is very recent, execution of these two programmes has not yet started. In the case of works to be financed with funds from the bi-national power plants, the agreement wording already stipulates the division of work among Governor Offices, the Ministry of Finance, and the bi-national plants. In addition, criteria are given for allocating resources to specific projects, associated to poverty, unemployment, and underemployment circumstances. However, project execution will face significant challenges arising from institutional weaknesses, beginning with project formulation and estimating the amounts to be allocated to labour and associated job creation. In addition, the need for speedy execution in the context of the crisis causes tension with parallel measures that may be taken to strengthen institutions, as the outcomes of such measures are rarely instantaneous.

4. Assessment

In a context of economic crisis, the responses of the authorities for increasing job creation through public investment are correct and in line with recommendations of both ILO and other international agencies with regard to counter-cyclical economic policy.

In turn, the increase in public investment as a tool to create jobs in the face of the crisis does entail a lag typical of the cycle for project formulation and approval, together with subsequent contract and execution. The same applies to new activities where the State previously had no activity, e.g. routine road maintenance; it is very difficult in the short term to reach a major scale by comparison with the number of unemployed or underemployed persons. Hence, in the short term, the most important variable is not the amount of additional funds allocated but speedy execution of the funds already available.

Despite the fact that the Paraguayan authorities are strengthening their capabilities for managing public investment and adding job-creation efforts, many of the improvements will not be fully operational in time to be numbered among responses to the present economic crisis. This limitation also affects measurement of the effect of steps taken, which in the best of cases could be performed with some accuracy *ex-post*, once the investments have been executed.

5. Conclusions

The information summarized in this brief paper illustrates the scope as well as the limitations of job creation through public investment. Undoubtedly, public investment can be a powerful tool to create jobs and dynamize the economy in times of economic crisis. The Paraguayan authorities have shown by their actions their political will to make the most of this tool.

It is also clear that positive impact increases to the extent that there is more ability to execute decentralized investment, to measure impact on employment, which involves priority-setting, monitoring, and assessment, and to speed up investment execution in a context of critical economic circumstances. From all of these angles, the Paraguayan case provides examples of achievements as well as challenges still pending, which could be useful to other developing countries.

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