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The World Bank

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Report No: PGD277

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT FOR A

PROPOSED LOAN

IN THE AMOUNT OF US$500 MILLION

TO THE

REPUBLIC OF COLOMBIA

FOR THE

COMPETITIVENESS AND RECOVERY – DEVELOPMENT POLICY LOAN

August 26, 2021

Finance, Competitiveness And Innovation Global Practice
Latin America And Caribbean Region

Republic of Colombia

GOVERNMENT FISCAL YEAR

January 1 – December 31

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of July 29, 2021)

COP 3,902.18 = US$ 1.00

ABBREVIATIONS AND ACRONYMS

AEO	Authorized Economic Operator	IMF	International Monetary Fund
AFD	French Development Agency (*Agence Française de Développement*)	INVIMA	Food and Drug Surveillance (*Instituto Nacional de Vigilancia de Medicamentos y Alimentos*)
ArCO	Articulation for Competitiveness methodology	ISA	International Standards on Auditing
ASA	Advisory Services and Analyticals	KfW	German Development Bank
CAF	Development Bank of Latin America (*Corporación Andina de Fomento*)	LAC	Latin America and the Caribbean
CAPEX	Capital Expenditure	LPI	Logistic Performance Index
CAR	Capital Adequacy Ratio	MIGA	Multilateral Investment Guarantee Agency
CCE	Colombia Efficient Procurement Agency (*Colombia Compra Eficiente)*	MSMEs	Micro, Small and Medium Enterprises
CIT	Corporate Income Tax	MSMs	Micro and Small Enterprises
CNBT	National Council for Tax Benefits	MTEF	Medium-Term Expenditure Framework
CONPES	National Council on Economic and Social Policy (*Consejo Nacional de Politica Económica y Social*)	NCRE	Non-Conventional Renewable Energy
COP	Colombian Peso	NDC	Nationally Determined Contribution
CPC	Private Council for Competitiveness (*Consejo Privado de Competitividad*)	NDF	Non-Delivery Forwards
CPEM	Presidential Advisor for the Equality of Women	NPL	Non-Performing Loans
CPF	Country Partnership Framework	OCAD	Órgano Colegiado de Administración y Decisión
CPI	Consumer Price Index	OCCP	Colombian Observatory of Public Procurement
CPSD	Colombia Country Private Sector Diagnostic	OECD	Organization for Economic Co-operation and Development

DAFP	Public Administration Department (*Departamento Administrativo de la Función Pública*)
DANE	National Statistics Institute (*Departamento Nacional de Estadística*)
DIAN	Tax authority (*Dirección de Impuestos y Aduanas Nacionales*)
DNP	National Planning Department (*Departamento Nacional de Planeación*)
DPF	Development Policy Financing
EIB	European Investment Bank
EMBIG	Emerging Markets Bonds Index
EMICRON	Small businesses survey
FAE	Savings and Stabilization Fund (*Fondo de Ahorro y Estabilización*)
FCL	Flexible Credit Line
FCR	Regional Compensation Fund
FCTel	Science, Technology, and Innovation Fund
FDI	Foreign Direct Investment
FDR	Regional Development Fund
FINDETER	Territorial Development Finance Bank *(Financiera de Desarrollo Territorial)*
FNA	*Fondo Nacional del Ahorro*
FNG	National Guarantee Fund (Fondo Nacional de Garantías)
FOME	Emergency Mitigation Fund (*Fondo de Mitigación de Emergencia*)
FONPET	Pensions Saving Fund *(Fondo Nacional de Pensiones de las Entidades Territoriales)*
FOREX	Foreign Exchange
GBP	Green Bond Principles
PAEF	Wage subsidy program (*Programa de Apoyo al Empleo Formal*)
PDP	Productive Development Policy
PER	Public Expenditure Review
PFM	Public Financial Management
PND	National Development Plan (*Plan Nacional de Desarrollo*)
R&D	Research and Development
RIA	Regulatory Impact Assessment
RNFPS	Rest of the Non-Financial Public Sector
SAS	Simplified Join Stock Companies
SBD	Standard Biding Documents
SCD	Systematic Country Diagnostic
SCM	Standard Cost Model
SDR	Special Drawing Rights
SENA	National Technical and Vocational Training Service Agency (*Servicio Nacional de Aprendizaje*)
SFC	Colombia's Superintendence of Finance
SFC	Superintendence of Finance (*Superintendencia Financiera de Colombia*)
SGR	*General System of Royalties (Sistema General de Regalías*)
SIC	Superintendence of Industry and Commerce (*Superintendencia de Industria y Comercio*)
SISBEN	Identification System of Potential Beneficiaries of Social Programs *(Sistema de Identificación de Potenciales Beneficiarios de Programas Sociales)*
SME	Small and Medium Enterprises
SNCI	National Competitiveness and Innovation System

GCFF	Global Concessional Financing Facility	SPD	Standard Procurement Documents
GDP	Gross Domestic Product	STEM	Science, technology, engineering, and mathematics
GEIH	Colombian Household Survey *(Gran Encuesta Integrada de Hogares)*	STI	Science, Technology, and Innovation
GEM	Global Entrepreneurship Monitor	SUIT	Single Registry for Administrative Procedures
GHG	Greenhouse Gases	TAB	Trading Across Borders
GMF	Tax on Financial Movements	TEA	Total early-stage Entrepreneurial Activity
GNP	Gross National Product	TES	Colombian Treasury Bonds
GoC	Government of Colombia	TIDIS	Tax Refund Bonds *(Títulos de Devolución de Impuestos)*
GPG	Global Public Goods	UN	United Nations
GRID	Green, Resilient and Inclusive Development	URF	Financial Regulation Unit
GVC	Global Value Chain	UVR	Unit Value Ratio
IADB/IDB	Inter-American Development Bank	UVT	Tax Value Unit
IBRD	International Bank for Reconstruction and Development	VAT	Value Added Tax
ICA	Turn-over tax on businesses (*Impuesto de Industria y Comercio*)	VET	Virtual Environment for Training
ICETEX	Colombian Educational Credit Institute *(Instituto Colombiano de Crédito Educativo y Estudios Técnicos)*	VUE	Single Business Window
ICT	Information and Communication Technologies	WB	World Bank
IFC	International Finance Corporation	WBG	World Bank Group
IFRS	International Financial Reporting Standards	WTO	World Trade Organization

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REPUBLIC OF COLOMBIA

COMPETITIVENESS AND RECOVERY - DEVELOPMENT POLICY LOAN

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SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Project ID	Programmatic
P175801	No

Proposed Development Objective(s)

The development objective of the program supported by the proposed operation is to encourage a high-productivity and sustainable recovery from the COVID-19 crisis by (i) improving regulation for private sector-led recovery; (ii) promoting innovation and digital finance; and (iii) fostering entrepreneurship and internationalization.

Organizations

Borrower:	REPUBLIC OF COLOMBIA
Implementing Agency:	MINISTERIO DE HACIENDA Y CRÉDITO PÚBLICO, DEPARTAMENTO NACIONAL DE PLANEACIÓN

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Financing	**500.00**

DETAILS

International Bank for Reconstruction and Development (IBRD)	500.00

INSTITUTIONAL DATA

Climate Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks

Overall Risk Rating

Substantial

Results

Indicator Name	Baseline	Target
Results Indicator #1: Reduction in regulatory burden measured as total savings in compliance costs[1].	COP 0 [2020]	COP 179,468 million [2022]
Results Indicator #2: Number of green bond issuances that comply with the Green Bond taxonomy and guidelines.	0 [2019]	4 [2022]
Results Indicator #3: Average number of bids per public bidding process in all the sectors where standard documents are mandatory.	3 [2019]	7.5 [2022]
Results Indicator #4: Yearly investment by MSMEs in STI projects leveraging on tax incentives.	COP 168.000 million [2020]	COP 285.000 million [2022]
Results Indicator #5: Total value of projects presented by the private sector that are approved for SGR co-financing and are associated with environmental, sustainable development and renewable energy projects oriented to energy transition and reduction of carbon emissions.	COP 4,845 million [2019]	COP 21,232 million [2022]
Results Indicator #6: Volume of financing through crowdfunding platforms.	COP 8,000 million [2020]	COP 40,000 million [2022]
Results Indicator #7: Percentage of adults who make payments or purchases online.	20 percent [2020]	40 percent [2022]
Results Indicator #8: Number of dynamic enterprises participating in acceleration programs offered by iNNpulsa[2].	508 [2020]	3,000[3] [2022]
Results Indicator #9: Number of women-led enterprises supported through technical assistance and/or co-financing programs offered by iNNpulsa and SENA.	2,230 [2020]	10,178 [2022]
Results Indicator #10: The GVC-related trade value covered by the AEO Program[4].	12 percent [2019]	14 percent [2022]

[1] The Public Administration Department (*Departamento Administrativo de la Función Pública*, DAFP) developed a methodology to measure compliance costs savings related to regulatory and administrative simplification policies and programs. The methodology is similar to a Standard Cost Model (SCM), a tool commonly used in the world to measure and monetize regulatory burdens. In the case of Colombia, compliance cost savings from government policies and programs come from reducing the time to complete an administrative procedure (*trámite*); eliminating the need to physically be present to deliver documents or pay fees; eliminating associated costs for transportation or shipment of documents; reducing fees; and eliminating other costs related to compliance with regulatory requirements.

[2] The Government of Colombia defines dynamic enterprises as those that increase their sales or employment by at least 9 percent per year or their profitability by at least 5 percent per year (National Development Plan 2018-2022).

[3] Indicator and target established in the National Development Plan 2018-2022.

[4] Trade value of AEO certified firms that both import and export over the total trade value of firms that both import and export.

IBRD PROGRAM DOCUMENT FOR A PROPOSED COMPETITIVENESS AND RECOVERY LOAN - DPF - TO THE REPUBLIC OF COLOMBIA

1. INTRODUCTION AND COUNTRY CONTEXT

1. **The proposed stand-alone Competitiveness and Recovery Development Policy Loan operation, for US$500 million, supports the Government of Colombia's policies to strengthen productivity and accelerate economic growth**. The development objective of the program supported by the proposed operation is to encourage a high-productivity and sustainable recovery from the COVID-19 crisis by (i) improving regulation for private sector-led recovery; (ii) promoting innovation and digital finance; and (iii) fostering entrepreneurship and internationalization. Through three corresponding pillars, the program will support the Government's efforts to address market failures, remove distortions, and improve the quality of firms, with the aim of lifting Colombia's productivity growth path in the medium term. These priorities are in line with the Government's strategy for economic recovery in the aftermath of COVID-19 for the short and medium term.

2. **After two decades of consistent economic growth and reduction in poverty, the COVID-19 crisis hit the economy hard, with effects that will take time to absorb.** Colombia's solid economic growth since the early 2000s had led to significant social improvements. Extreme poverty fell from 17.7 percent in 2002 to 7.2 percent in 2018. Moderate poverty also decreased, dropping from 49.7 percent to 27.0 percent over the same time frame. Notwithstanding the mitigating impact of the government's emergency response, the COVID-19 crisis wiped out all gains in poverty reduction realized over the past decade: the incidence of poverty increased from 35.7 percent in 2019 to 42.5 percent in 2020. Despite the emergency social transfers put in place in response to the crisis, the incidence of poverty increased from 35.7 percent in 2019 to 42.5 percent in 2020. Real GDP contracted 6.8 percent in 2020 against a pre-crisis projection of 3.6 percent growth. As a result of weak revenue collection, and higher spending to respond to the health crisis and support the economy, the overall deficit of the general government increased to 7.2 percent of GDP, from a projected 2.6 percent before the pandemic broke out; and the general government debt-to-GDP ratio reached 66.9 percent of GDP in 2020.[5]

3. **The Government established a 3-axes economic reactivation plan for the short and medium term**, including the following short and medium to longer term measures:

(i) The first axis includes two policy documents approved by CONPES[6] to respond to the crisis. The first[7] compiles the initial response between March and July 2020. The second[8] comprises the medium-term strategy (See Box 1).

(ii) The second axis focuses on the prioritized and accelerated implementation of commitments

[5] In this document, general government debt is reported as gross, non-consolidated debt (see discussion in fiscal section).

[6] CONPES is the National Council for Economic and Social Policy, the main advisory body of the national government.

[7] Documento CONPES 3999 *Estrategia de respuesta inicial ante los efectos de la pandemia del COVID-19 sobre la salud pública, los hogares, el aparato productivo y las finanzas públicas*. August 5, 2020. Bogota, Colombia. *https://colaboracion.dnp.gov.co/CDT/Conpes/Econ%C3%B3micos/3999.pdf*

[8] Documento CONPES 4023 Política para la reactivación y el crecimiento sostenible e incluyente: Nuevo compromiso por el futuro de Colombia. February 11, 2021. Bogota, Colombia. *https://colaboracion.dnp.gov.co/CDT/Conpes/Econ%C3%B3micos/4023.pdf*

contained in the National Development Plan (PND 2018-2022).

(iii) The third axis focuses on the implementation of recommendations by the employment and internationalization taskforces of national and international experts (*Misión de Empleo* and *Misión de Internacionalización*).

4. **The success of the Government's recovery strategy crucially hinges on tackling structural bottlenecks that have been exacerbated by the current crisis.** Productivity growth in Colombia has been practically nil over the last decades as a consequence of a poor business environment, feeble market competition, limited openness of the economy and weak propensity to innovate. Colombia ranks 123rd and 110th, respectively, in the burden of government regulation and domestic competition areas of the Global Competitiveness Index. The financial sector is highly concentrated, while the capital market is shallow and illiquid, limiting private sector investment and growth. Colombia's investment in R&D amounts to 0.28 percent of GDP in 2019, compared to 0.62 percent in the LAC region and is the lowest among Organization for Economic Co-operation and Development (OECD) countries (2.38 percent). Colombia also lags in digitalization and Information and Communication Technologies (ICT) adoption, with the lowest download speed in the OECD (8.8 Mbps vs. 53.9 Mbps), limiting digital financial inclusion, which is particularly important in the post-pandemic era. Finally, Colombia remains relatively closed to international trade, with exports concentrated in commodities, and limited integration in global value chains.

5. **The proposed operation aims to support the authorities' strategy for a broad-based, inclusive, and sustainable recovery by addressing structural issues hindering productivity.**

- *The first pillar seeks to enhance the productivity of the Colombian economy by improving the regulatory environment for private sector activity*. A first set of measures aims at reducing the time and cost allocated to comply with administrative procedures or government transactions as well as associated carbon footprint, and at establishing whole-of-government better regulation to the production and review of technical regulations. Second, a clearer regulatory framework for green finance will help power a broad-based, climate-friendly and environmentally sustainable recovery, with an expected increase of green bond issuances. Finally, the introduction of standard bidding documents for public procurement in an increasing number of sectors, coupled with the enhanced technological capability of the competition authority to detect collusive behavior, will help level the playing field and open up opportunities for more Colombian businesses.
- *The second pillar supports innovation and the development of digital finance, whose shortcomings have become evident in the wake of the COVID-19 crisis and hinder productivity*. First, investment in science, technology, and innovation (STI) will receive a boost from the expanded use of tax incentives by smaller firms. Moreover, the allocation of a greater share of resources from the General Royalties System to STI, unprecedented for green projects, will foster innovation with positive spillovers for an environmentally sustained recovery. Next, a set of actions aims at encouraging digital finance and improving competition in Colombia's highly concentrated financial sector. One aims at increasing the market for crowdfunding, while the other at increasing digital financial inclusion.
- *The third pillar fosters high-growth entrepreneurship and builds on the work of the ongoing Internationalization taskforce, aiming to improve business entry, operation and growth and increasing the international integration of the Colombian economy*. First, improving the Colombian entrepreneurial ecosystem through strengthened institutional capacity, a more favorable regulatory

and business environment, and greater access to key enablers,[9] is expected to favor high-growth entrepreneurship and inner-firm productivity. Notably, this measure is expected to generate a fivefold increase in the number of dynamic enterprises benefitting from acceleration and entrepreneurship programs by 2022, with particular focus on innovative, green and climate mitigating initiatives. Second, providing differentiated technical and financial support to women entrepreneurs through the creation and consolidation of the autonomous trust fund--*Fondo Mujer Emprende*-- is expected to benefit 10,178 female-led enterprises by 2022. The last measure is expected to ease the burden of controls at the border, thus reducing the cost that Colombian firms face to participate in global value chains.

6. **The operation is aligned with the approach set out in the paper *From COVID-19 Crisis Response to Resilient Recovery - Saving Lives and Livelihoods while Supporting Green, Resilient and Inclusive Development (GRID)* prepared by the World Bank Group for the April 9, 2021 Development Committee Meeting and with the *World Bank Group COVID-19 Crisis Response Approach Paper – Saving Lives, Scaling-Up Impact and Getting Back on Track* discussed by the Board on June 25, 2020**. Actions in all three pillars of the DPF are consistent with Pillar 3 of the Approach Paper, 'Ensuring Sustainable Business Growth and Job Creation', with measures aimed at making the enterprise sector more productive, innovative and internationally oriented in order to achieve a more sustainable recovery. A number of actions tackle long-standing institutional bottlenecks and are in line with Pillar 4 of the Approach Paper, 'Strengthening Policies, Institutions and Investments for Rebuilding Better', notably with reforms of the regulatory system, public procurement, the innovation ecosystem, and digitalization of financial services. Crisis response offers a unique opportunity to rebuild stronger, greener, and more equitable economies and institutions while leveraging the private sector. In this spirit, several policy reforms supported by the operation are in line with the GRID approach, notably with actions that support a <u>green</u> (digital government procedures, green finance, green and climate mitigating entrepreneurial initiatives), <u>resilient</u> (deepening of financial markets and trade facilitation) and <u>inclusive</u> (female entrepreneurship, more innovation and access to finance for MSMEs and competition in public procurement) recovery.

7. **The overall risk of the operation is assessed as substantial.** Macroeconomic risks and political and governance risks are the most consequential for the achievement of the development objectives. Macroeconomic risks are substantial given the severe economic impact of COVID-19 globally, as well as uncertainty as to how quickly domestic economic activity can fully resume. If downside risks materialize, the urgency of short-term needs could cause a change in priorities of the Government that could impact the implementation of this DPF. To mitigate macroeconomic risks, the Government is working closely with international financial institutions to secure fiscal buffers and formulate a balanced reactivation plan for the economy. Political and governance risks are also substantial. Reforms supported in the DPF have the overall effect of increasing competition across the economy, thus denting existing vested interests, who may attempt to derail implementation. The high level of political ownership of the reform agenda can moderate the influence of vested interests. Furthermore, swift implementation of the DPF program itself can mitigate both the macroeconomic and political/governance risk since it would have countercyclical effects on the economy, as well as give voice to the winners from the reforms (minority shareholders, small firms, innovators, new exporters, new telecoms operators, etc.), who would become

[9] Including finance, skills (managerial, digital and for innovation), and knowledge and technology transfer.

a political force in support of the reforms. Other risks are assessed as moderate or low.

2. MACROECONOMIC POLICY FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

8. **The outbreak of the COVID-19 pandemic caused GDP to contract 6.8 percent in 2020 halting the recuperation from the 2014-16 oil price shock.** During 2017–2019 adequate macroeconomic policies (a fully-fledged inflation targeting regime, a flexible exchange rate, and a rule-based fiscal policy) ensured gradual external and fiscal adjustments from the 2014–16 oil price shock (Table 1). The strict lockdown and mobility restrictions that the government adopted to slow down the diffusion of COVID-19, the economic repercussions of the pandemic throughout lower global demand and oil prices, and the ensuing uncertainty about the depth and duration of the crisis disrupted both supply and domestic demand. After economic activity nearly collapsed in March and April of 2020 (as strict mobility restrictions brought manufacturing, construction, and commerce almost to a halt),[10] beginning in May 2020, economic activity resumed and has been increasing steadily since then. Inflation remained subdued despite the large monetary stimulus (see next paragraph), averaging 2.5 percent in 2020.

9. **The authorities put in place a range of monetary and fiscal stimulus measures to support lives, livelihoods, and the economy since the COVID-19 crisis struck.** The Central Bank progressively cut the monetary policy rate to a historical low of 1.75 percent, provided over COP 20 trillion of liquidity injection, lowered reserve requirement ratios, purchased public and private securities, and activated U.S. Dollar swap lines.[11] To ensure adequate fiscal support, the suspension clause of the fiscal rule was activated for 2020 and 2021,[12] and the Government put together a support package for households and firms, raising transfers to vulnerable groups through existing and new programs (*Ingreso Solidario* and VAT devolutions), deferring tax collection for firms, and providing wage subsidy and liquidity support for businesses.[13] In August 2020, the government announced a 163 trillion pesos investment plan (about 16 percent of GDP) to be implemented jointly with the private sector over the next ten years (the "New

[10] These three sectors contributed to about 36 percent of GDP in 2019, and in 2020Q1 contracted (q/q), 21.6 percent (manufacturing), 24.6 percent (construction), and 33.6 percent (commerce).

[11] The Central Bank reduced the policy interest rate seven times, bringing it from 4.25 before March 2020 to 1.75 percent in September 2020. It lowered the reserve requirements for current and savings accounts and other liabilities from 11 to 8 percent; and for certificates of deposit of less than 18 months from 4.5 to 3.5 percent. The amount of the corresponding liquidity injection is estimated to have been COP 9.8 trillion. To support liquidity in short-term funding markets, the Central Bank purchased COP 8.7 trillion of securities issued by credit institutions. It also purchased government bonds worth up to COP 2.8 trillion. Furthermore, to support the exchange market and promote liquidity in US dollars, swaps contracts up to US$400 million have been executed, equivalent to 12 percent of the banks' short-term foreign currency debt balance. Between March and end-November 2020, non-delivery forwards (NDFs), worth US$ 8.8 billion, have been auctioned or renewed.

[12] Colombia's fiscal rule mandated a reduction of 0.8 percentage points of GDP in the Central Government's fiscal deficit between 2019 and 2022, which would have brought the structural deficit of the Central Government to 1 percent of GDP in 2022. Flexibility parameters built into the fiscal rule allow the Fiscal Rule Consultative Committee to consider oil price and business cycle (including COVID-19 related) fluctuations in setting the fiscal path. In May 2020, the flexibility built into the fiscal rule allowed resetting the 2020 deficit ceiling to 6.1 percent of GDP (up from 2.2 percent established in the 2019 medium-term fiscal framework). On June 15, 2020, taking stock of the further deterioration in economic conditions, the Consultative Committee on the Fiscal Rule endorsed the Government's request to suspend the fiscal rule, which would provide further flexibility to sustain economic activity. The suspension clause of the fiscal rule does not set a ceiling to the fiscal deficit during the suspension period, nor it sets a maximum duration of the suspension period.

[13] *Ingreso Solidario* and the subsidy for wages were later extended to August and March 2021 respectively.

commitment for the future of Colombia"), and in December 2020, it announced a 2.9 trillion pesos economic reactivation plan to mitigate the increase in poverty and economic vulnerability and to support sustainable and green growth and the digitalization of the economy.

10. **Amid the decline of oil exports, lower expatriation of profits to foreign direct investors and strong remittances brought the current account deficit down to 3.4 percent of GDP in 2020, from 4.5 percent of GDP in 2019.** The decline in export volume and prices (especially oil) caused a decline in exports (20.9 percent) that exceeded the decline in imports (18.6 percent). At the same time, lower profitability of foreign invested firms operating in Colombia compressed the primary balance of payments to foreign investors, and remittances remained robust in nominal terms (especially, those from the U.S. and Spain). During the year, inflows of Foreign Direct Investment (especially to the financial and oil sectors) financed about 85 percent of the current account deficit while strong inflows of portfolio investment (a total of US$7.5 billion, of which public debt operations accounted for US$6.1 billion) allowed to finance the remaining current account deficit and to accumulate external assets, including international reserves. At end-year, international reserves reached US$59 billion, the equivalent of 265.6 percent of short-term external debt outstanding at end-December 2020.

11. **The Central Government's deficit widened to 7.8 percent of GDP in 2020 (from 2.5 percent in 2019), as spending increased for crisis response and tax receipts declined due to disruptions in economic activity and lower oil revenue.** Spending increased by 4.3 percent of GDP, as a result of the decline in nominal GDP (1.1 percentage point), greater spending on goods and services related to the COVID-19 response (0.5 percent of GDP), and measures to support the economy and the most vulnerable, and increased transfers to territorial and local governments (2.7 percent of GDP). The decline in private consumption and the exemption for strategic health imports and selected food industries and services weighed on VAT (down 0.4 percent of GDP relative to 2019), whereas the temporary delay in tax payments and withholding drove down income taxes (0.3 percent of GDP).[14] The decline in oil prices is estimated to have reduced dividends from Ecopetrol by about 0.4 percent of GDP.

12. **After an initial sharp market reaction in 2020Q1, financing conditions remained favorable for the rest of the year and the Central Government was able to over-finance the 2020 budget.** Markets reacted strongly when the pandemic broke out in March 2020: the exchange rate depreciated 14 percent in March 2020 relative to February 2020, the risk premium increased 170 basis points, the stock market fell 27 percent, and there was a brief episode of non-resident portfolio outflows. Including thanks to ample injections of liquidity abroad, market conditions later stabilized, and most indicators went back to levels very close to those at the beginning of the year.[15] In this context, the government successfully tapped financial markets. On June 1, 2020, it issued US$2.5 billion in global bonds (including a new 31-year maturity bond) at the lowest historical coupon rate in the long part of the yield curve in U.S. dollars. Also, on June 17, 2020, Colombia issued COP 255 billion in treasury bonds (TES) in unit value ratio (UVR), with a demand that was 4.5 times the amount issued, and in September 2020, it raised 4.8 trillion pesos

[14] Because income taxes are assessed on the previous year's earnings, the slowdown in activity did not affect income taxes much in 2020.

[15] By end-2020, the EMBIG spreads went back to 206 (that is, 36 bps above January 2020 levels). The exchange rate appreciated 13.2 percent relative to the most depreciated value, in March 2020, which makes a 7.1 percent depreciation relative to the average in January 2020. The stock market has slowly recovered from its lowest point on March 18, 2020 and recuperated about 60.4 percent of the loss incurred between its highest point in late February 2020 and its trough on March 18, 2020. At the end of June 2021, it is 19 percent below its highest point in late February 2020.

with a domestic issuance of a 30-year bond. During the year, the Central Government was able to raise financing equivalent to 13.7 percent of GDP.[16] As debt amortization and payment of obligations emerging from judicial rulings amounted to about 1.1 and 1.5 percent of GDP respectively, the 2020 financing allowed to carry over to 2021 about 1.1 percent of GDP of resources.[17]

13. **Pushed by the Central Government's deficit, the General Government's gross debt increased to 66.9 percent of GDP at end-2020.**[18] As in previous years, the rest of the general government posted an aggregate surplus of 0.6 percent of GDP in 2020: the social security system posted a surplus of 0.5 percent of GDP (owing to exceptional yields on portfolio investments), territorial governments had a surplus of 0.3 percent of GDP, whereas funds suffered a deficit of 0.2 percent of GDP. The Central Government debt increased to 64.8 percent of GDP at end-2020, while the debt of the general government increased to 2.1 percent of GDP. Whereas cross-holding of debt between institutions of the general government is close to zero, about 2.7 percent of GDP of the Central Government consists of IOUs towards territorial government, another 1.4 percent of GDP correspond to lending from Funds, and 4 percent of GDP is held by the non-financial public sector.[19] This is about 14.9 percent of GDP higher than in a counterfactual scenario without COVID-19, of which lower nominal GDP growth contributed about 6.6 percent of GDP, while the depreciation of the peso explains roughly another 1.1 percent of GDP.

14. **After a very strong performance in 2021Q1, activity was affected by strikes in opposition to the government's fiscal reform package**. In the first quarter of 2021, GDP expanded 2.9 percent (q/q on a seasonally adjusted basis), reaching 99.3 percent of the 2019Q4 level, above all expectations. On the supply side, the sectors that most contributed to the increase were wholesale and retail trade, transportation, construction (mainly in the component of civil works), and manufacturing. On the demand side, gross fixed capital formation and private consumption were the components that most pushed GDP up. On April 15, 2021, the government submitted to Congress a fiscal reform package intended to increase revenues by 2 percent of GDP, expand social protection by 0.6 percent of GDP (by transforming the program *Ingreso Solidario* into a Guaranteed Minimum Income program, and by expanding the coverage and amount of the program to compensate poor households for VAT), and reduce the deficit by 1.4 percent of GDP. After opposition in Congress and heavy protests around the country, the government withdrew the proposal and started working on a new draft. Protest and blockades continued well into May 2021 and the first half of June 2021, although with decreasing intensity. As a result, unemployment, business and consumer confidence, and manufacturing activity deteriorated in May 2021. Also, annual CPI inflation increased to 3.3 percent in May 2021 (above the middle point of the inflation targeting band) owing to shortages and interruptions in distribution chains caused by road blockages. Nevertheless, economic activity has been gradually recovering since the second week of May 2021, as shown by the energy consumption indicator, which in June 2021 was above

[16] Financing included the use of savings accumulated in existing funds and deposits channeled to the FOME (1.3 percent of GDP), domestic borrowing (4.4 percent of GDP, including the issuance of the solidarity bond for 1 percent of GDP), external borrowing (1.7 percent of GDP), borrowing from multilateral organizations and bilateral donors (2.1 percent of GDP), and by withdrawing US$ 5.4 billion (about 2.1 percent of GDP) from its Flexible Credit Line with the IMF.
[17] The stock of government's deposit increased from 2.1 percent of GDP at end-2019 to 3.3 percent of GDP and end-2020.
[18] This is total, non-consolidated debt. The consolidated debt of the general government amounted to 58.4 percent of GDP.
[19] Because the holding of Central Government's debt by the rest of the non-financial public sector (RNFPS, mostly public corporations and funds) depends on its capacity to generate surpluses, the non-consolidated debt reflects the total debt to the private sector that could emerge if the rest of the RNFPS did not have the financial capacity to hold Central Government's debt, or if this sector was privatized.

the June 2019 level.

15. **Markets reacted to the strikes and withdrawal of the fiscal reform package.** After a 4 percent depreciation since protests began, the Colombian Peso appreciated and went back to almost the same level as before the protests, but the EMBIG spread increased 13 basis points (reaching 250 basis points at end-May), one of the largest increases among LAC Countries over the same period. S&P downgraded Colombia from BB+ to BBB- (on concerns about difficulties in reaching consensus on a reform package that can steadily and credibly reduce the deficit and debt). On July 1, 2021, Fitch also downgraded Colombia's credit rating below investment grade owing to the expected deterioration in public finances, as well as the reduced confidence around the government's capacity to credibly decrease the debt trajectory.

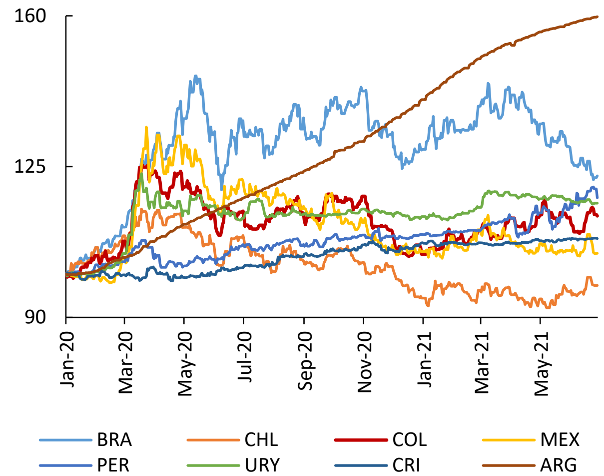
16. **On July 20, 2021, the government submitted to Congress a fiscal reform bill law backed by the Corporate Income Tax (CIT) revenue, spending savings, and the fight against tax evasion.** On revenues, the bill proposes to (i) increase the CIT rate to 35 percent, cancelling the planned decrease in CIT, (ii) implement a surcharge of 3 percentage points to the CIT of the financial sector until 2025, (iii) offer a new opportunity to "whiten" undeclared assets through a "regularization" tax, (iv) include complementary measures to combat tax evasion, (v) maintain 50 percent of the payment of the turnover tax (ICA) as CIT credit (which reverses a previous commitment to allow full crediting of the ICA). On spending, the bill proposes to (i) extend *Ingreso Solidario* program until December 2022 and expand its scope from 3 million to 4 million families starting in April 2022, (ii) subsidize employers hiring young adults between 18 and 28 years up to 25 percent of the minimum wage, in 2021 and 2022, (iii) broaden the wage subsidy program (PAEF *Programa de Apoyo al Empleo Formal*) until December 2021, (v) set a free tuition in tertiary education for low income students (695,000 students) in public institutions, and (iv) establish austerity measures. In addition, the bill introduces a debt anchor to set the Central Government fiscal rule and moves towards an independent fiscal council. The reform is estimated to have a fiscal cost of about 1 and 0.4 percent of GDP in 2021 and 2022, respectively, while contributing to reduce the deficit by 1 percent of GDP on a permanent basis starting in 2023. However, the net contribution is negative through 2022. The new fiscal package does not propose structural changes to address the challenges of the Colombian fiscal accounts, so the deficit reduction from 2023 onwards implied by this bill will not be enough to meet the deficit limits set by the new fiscal rule. Therefore, the government will have to present an additional fiscal reform in the following years to effectively bring the debt back to a downward path and consolidate public finances.

17. **The current account deficit in 2021Q1 widened to 4.8 percent of quarterly GDP, compared to 4.0 percent in 2020Q4 on account of an increase in primary income payments (distribution of profits, reinvestment of earnings, and interest payments).** The trade deficit slightly decreased in U.S. dollar terms, from US$4.0 billion in 2020Q4 to US$3.9 in 2021Q1, driven by an improvement in the balance on services, as exports (especially travels) increased more than imports. The secondary income account continued to rise and reached a historic record, supported by strong remittances. The increase in primary income payments (US$538 million above 2020Q4) was the main driver of the deficit expansion. In particular, distribution of profits of firms with direct investment (in the oil sector—owing to higher oil prices) rose US$130 million; reinvestment of earnings rose US$330 million, and interest payments on short-term debt rose US$224 million. Yet, most of these flows remain below 2019Q4 levels. As a percentage of GDP, the increase in the deficit (0.8 pp) was explained by the increase in dollars amount of the current account deficit (0.7 pp), and the reduction in nominal GDP in dollars (0.1 pp). The current

account deficit was primarily financed by divestment of foreign assets.

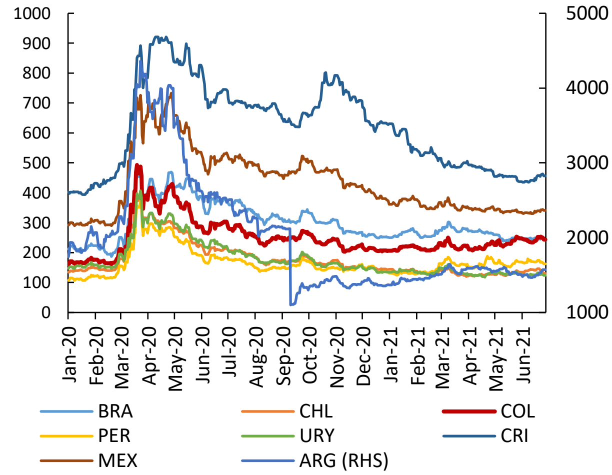
18. **The financial sector remains resilient to the deterioration in the portfolio of lending.** The NPL ratio increased to 5 percent (+0.7 pp y-o-y) in Dec-2020 driven by a deterioration in the quality of the consumer lending portfolio (+1.6 pp y-o-y) and is expected to reach 8 percent by end-2021, considering the expected expiration of the borrower relief measures by mid-2021 (90 percent of the credit portfolio has already “graduated” from these measures, or did not need them). Banks remain well capitalized, with the system’s CAR reaching 17.2 percent in Dec-2020 after dropping to 13.7 percent mid-year (the lowest since 2008), with no individual institution in single digits. Immediate financial stability risks are mitigated by the significant build-up of additional provisions, which reached 150 percent of NPLs by end-2020, and by the implementation of additional capital buffers following Basel III standards (to be gradually introduced over a four-year period starting January 2021). Although corporates’ financial conditions improved since the beginning of the pandemics, as of June 2021, around 26 percent of firms were experiencing difficulties in servicing their debt on time.

Figure 1. Exchange Rates
(Index 1/1/2020=100)



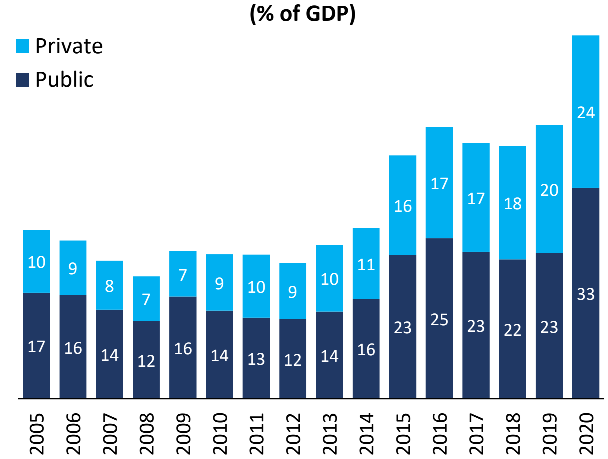
Source: Bloomberg.

Figure 2.EMBI Sovereign Spread
(Basis points)



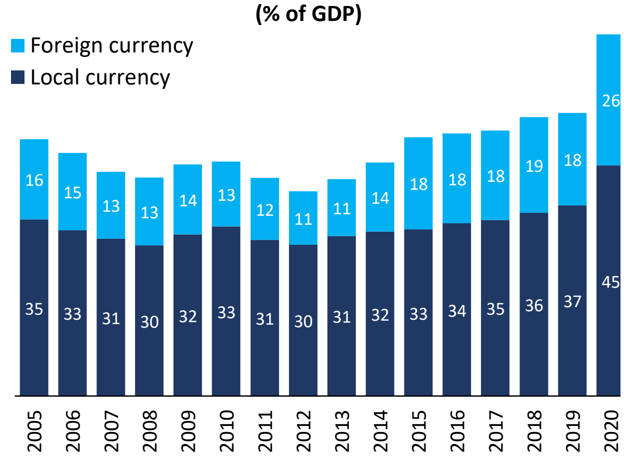
Source: Bloomberg.

Figure 3. External Debt
(% of GDP)



Source: Central Bank and World Bank staff calculations.

Figure 4. Gross Non-Financial Public Sector Debt
(% of GDP)



Source: Ministry of Finance and Public Credit and World Bank staff calculations.

Table 1. Colombia: Key Macroeconomic Indicators, 2017–2024

					Proj.	Proj.	Proj.	Proj.
	2017	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Real sector	Annual percentage change, unless otherwise indicated							
Real GDP	1.4	2.6	3.3	-6.8	5.9	4.1	4.0	3.7
Contributions:								
Private Consumption	1.4	2.2	2.7	-3.9	3.9	3.0	2.8	2.6
Government Consumption	0.5	1.1	0.8	0.6	0.6	0.2	0.3	0.3
Investment	0.4	0.2	0.7	-4.5	3.4	1.5	1.3	1.1
Exports	0.4	0.1	0.5	-2.8	1.0	0.8	0.4	0.4
Imports	-0.2	-1.2	-1.6	4.0	-2.9	-1.5	-0.8	-0.8
Exports	2.6	0.6	3.1	-18.3	7.4	6.2	2.8	3.1
Imports	1.0	5.8	7.3	-17.3	14.4	6.7	3.5	3.6
Unemployment rate (nat. def.)	8.6	9.7	9.5					
GDP deflator	5.1	4.6	4.0	1.4	3.2	3.5	3.8	3.9
CPI (average)	4.3	3.2	3.5	2.5	2.8	3.0	3.0	3.0
Fiscal accounts (Central Government)	Percent of GDP, unless otherwise indicated							
Revenues*	15.7	15.1	16.2	15.2	15.9	15.6	16.0	16.2
Expenditures	19.3	18.3	18.7	23.0	24.7	22.7	20.9	20.1
Fiscal balance (CG)	-3.6	-3.1	-2.5	-7.8	-8.7	-7.2	-4.9	-3.9
Fiscal accounts (General Government)	Percent of GDP, unless otherwise indicated							
Revenues	24.8	26.5	27.5	25.9	26.7	28.0	28.1	28.2
Expenditures	27.3	29.1	30.1	33.1	35.0	35.1	32.7	31.8
Fiscal balance	-2.5	-2.6	-2.6	-7.2	-8.3	-7.1	-4.6	-3.6
Gross public debt**	48.5	51.3	52.2	66.9	70.9	72.7	72.2	70.7
Selected monetary accounts	Annual percentage change, unless otherwise indicated							
Base money	5.0	10.4	12.3	17.9				
Credit to private sector	12.1	4.4	7.8	7.6				
Policy interest rate (end-of-period)	4.8	4.25	4.25	1.75				
External sector	Percent of GDP, unless otherwise indicated							
Current account balance	-3.4	-4.1	-4.5	-3.4	-4.2	-3.9	-3.7	-3.7
Exports GNFS	15.8	16.5	16.3	14.3	15.2	15.8	15.9	15.9
Imports GNFS	18.7	19.3	20.3	18.9	19.5	19.6	19.5	19.3
Foreign direct investment (net)	3.3	1.9	3.5	2.3	2.9	3.2	3.2	3.2
Gross reserves (US$ billion, eop)	47.6	48.4	53.2	59.0				
In months of next year's imports	9.1	9.0	12.4	12.3				
As % of short-term external debt	290	239	237	265				
External debt	40.0	39.7	42.9	55.4				
Terms of trade (% change)	9.3	5.8	0.1					
Exchange rate (COP/US$, average)	2,951	2,956	3,281	3,695				
Memo items								
Nominal GDP (US$ million, current)	311,883	333,569	323,616	271,438				
Nominal GDP (COP billion, current)	920,471	987,791	1,061,119	1,002,922	1,096,107	1,180,984	1,275,387	1,374,686
Oil production (hundred thousand barrels/day)	854	865	886	781	770	821	850	876
Oil price (Brent spot price, US$/barrel)	54	71	64	43	59	63	64	65

* In 2019 includes extraordinary Ecopetrol dividend. Since 2019 includes profits of Banco de la Republica.
**Gross pulic debt is unconsolidated debt and it includes Ecopetrol.
Source: Colombian autorities and WB staff estimates and projections.

Table 2. Colombia: Key Fiscal Indicators for the Central Government, 2017-2024 (% of GDP)

	2017	2018	2019	2020	Proj. 2021	Proj. 2022	Proj. 2023	Proj. 2024
Total revenues *	**15.7**	**15.1**	**16.2**	**15.2**	**15.9**	**15.6**	**16.0**	**16.2**
Tax revenues	13.8	13.7	14.0	13.0	13.5	14.0	14.9	15.0
Net income tax and profits	5.7	6.5	6.4	6.1	5.8	6.04	6.85	7.05
Value-added tax	5.5	5.7	5.8	5.4	5.8	5.9	5.9	5.9
International trade	0.4	0.4	0.4	0.3	0.4	0.5	0.5	0.5
Financial transactions tax	0.7	0.7	0.8	0.7	0.8	0.8	0.9	0.9
Stamp and other taxes	1.4	0.5	0.7	0.5	0.7	0.74	0.80	0.75
Non-tax revenues	0.6	0.1	0.1	0.2	0.2	0.2	0.2	0.2
Capital revenues *	1.1	1.2	1.9	1.9	2.1	1.3	0.9	0.8
o/w Ecopetrol dividends	0.1	0.3	1.1	0.7	0.1	0.4	0.5	0.5
Other	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1
Total expenditures	**19.3**	**18.2**	**18.7**	**23.0**	**24.7**	**22.7**	**20.9**	**20.1**
Current expenditures	16.0	15.6	15.6	19.4	20.5	19.0	17.9	17.5
Wages and salaries	2.2	2.3	2.1	2.4	2.3	2.1	2.1	2.1
Goods and services	0.6	0.7	0.7	1.2	1.4	0.9	0.8	0.7
Interest	2.9	2.8	2.9	2.8	3.4	3.5	3.4	3.4
Current transfers	10.2	10.2	10.1	13.6	13.3	12.5	11.6	11.3
Other	0.1	-0.3	-0.1	-0.5	0.0	0.0	0.0	0.0
Capital expenditures	3.3	2.6	3.0	3.5	4.2	3.7	3.0	2.6
Fixed capital formation	2.1	1.5	1.8	2.2	2.7	2.4	2.1	1.7
Capital transfers	1.2	1.1	1.2	1.3	1.4	1.2	0.9	0.9
Primary balance	-1.1	-0.3	0.4	-4.9	-5.3	-3.6	-1.4	-0.5
Overall fiscal balance *	**-3.7**	**-3.1**	**-2.5**	**-7.8**	**-8.7**	**-7.2**	**-4.9**	**-3.9**
Financing needs and end-year deposits	**8.3**	**8.0**	**8.4**	**13.7**	**12.2**	**10.8**	**8.1**	**7.5**
Overall fiscal balance	3.7	3.1	2.5	7.8	8.7	7.2	4.9	3.9
Amortizations	2.5	1.0	2.8	1.1	1.7	2.3	2.4	2.6
Arrears, judicial claims and other	0.2	0.6	1.2	1.5	0.8	0.5	0.0	0.0
Stock of deposits at the end of the year	2.0	3.4	1.9	3.3	1.0	0.8	0.8	1.0
Financing sources and previous year deposits	**8.3**	**8.0**	**8.4**	**13.7**	**12.2**	**10.8**	**8.1**	**7.5**
Domestic	5.1	5.0	4.1	3.4	4.9	6.5	5.0	4.5
Use of saving to capitalize FOME				1.3	1.1			
"Titulos de Solidaridad"				1.0				
External	1.7	1.2	1.2	5.9	3.3	3.4	2.3	2.3
Stock of deposits at the end of the previous year	1.6	1.8	3.2	2.1	3.0	0.9	0.8	0.7
Memo items								
Nominal GDP (COP billion, current)	920,471	985,931	1,061,730	1,002,922	1,096,107	1,180,984	1,275,387	1,374,686

*In 2021, this includes privatization receipts from the sale of participation in ISA.
Source: Ministry of Finance and WB staff estimates and projections.

Table 3. Balance of Payments financing requirements and sources, 2017-2024 (USD million)

	2017	2018	2019	2020	2021	2022	2023	2024
Financing requirements	**42,356**	**47,156**	**51,530**	**49,275**	**49,625**	**47,366**	**49,117**	**50,864**
Current account deficit	10,744	13,669	14,508	9,326	11,750	11,743	12,054	12,864
External debt amortization	31,067	32,301	33,689	35,621	37,071	34,422	35,780	36,700
Medium and long term	16,215	15,711	13,230	14,362	13,710	11,133	12,575	13,250
o/w Multilateral and Bilateral institutions				825	974	966	966	966
Short term	14,852	16,590	20,458	22,932	22,054	20,289	21,303	22,369
Gross reserve accumulation	545.11	1,187	3,333	4,328	805	1,200	1,283	1,300
Financing sources	**42,356**	**47,156**	**51,530**	**49,275**	**49,625**	**47,366**	**49,117**	**50,864**
FDI (net)	10,147	6,409	11,160	6,355	8,205	9,620	10,286	11,100
o/w inward (net)	13,837	11,535	14,313	8,100	10,667	12,505	13,371	14,430
External debt disbursements	33,638	40,551	39,714	51,055	39,131	33,550	36,201	38,062
Medium and long term	17,047	20,093	16,782	29,001	18,842	12,247	13,833	14,575
o/w Multilateral and Bilateral institutions	1,228	3,145	1,781	10,300	4,942	4,522	4,522	4,522
Short term	16,590	20,458	22,932	22,054	20,289	21,303	22,369	23,487
Other capital flows (net)	-1,429	196	656	-8,135	2,289	4,196	2,630	1,702
Memo items								
Remittances (net)	5,242	6,031	6,407	6,617	6,500	6,600	7,000	7,500

Source: Central Bank of Colombia and WB staff estimates and projections.

2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

19. **Under the baseline scenario, GDP is projected to increase 5.9 percent in 2021, and reach its end-2019 level in mid-2022.** Only as a base effect, activity in 2021Q1 was high enough to compensate for losses in 2021Q2 associated with the strikes and mobility restrictions imposed in April 2021 to slow down the third wave of infections. Our projection assumes a contraction in May 2021 (-8.0 percent m/m) and a slow recovery in the following months allowing economic activity for the year as a whole to grow close to end-2019 level. For 2021, the baseline projection further assumes that:

- Vaccination proceeds with few further delays and hiccups.[20]
- Occasional and localized restrictive mobility measures might be imposed during the rest of the year on an on-off basis, as additional milder waves of COVID-19 cases emerge after the easing of previous mobility restriction measures.
- Oil prices and oil demand, and external demand continue to recover, but at a moderate pace during 2021.

20. Under this scenario, after the drop in 2021Q2, manufacturing and commerce are expected to continue to grow robustly (on a quarterly basis), contributing jointly 3.8 percentage points to growth in 2021, while mining would continue to grow weakly. The increase in domestic demand would amount to 7.8 percent of 2020 GDP (of which 3.3 percentage points are explained by investments), as an accommodative monetary policy and an expansive fiscal stance[21] support private consumption and

[20] The vaccination plan started at a slow pace, but it has accelerated in June 2021 (up almost 80,000 doses from the May 2021 average), although with marked regional disparities. The plan of the authorities is to vaccinate about 72 percent of the population by year-end. Reaching that goal would imply maintaining the average number of doses per day reached in mid-June 2021 (247,000).

[21] The government is counting on the investment plan contained in the "*Nuevo Compromiso por el Futuro de Colombia*" for the reactivation of the economy. The plan foresees investments worth COP 140 trillion over the next 10 years, primarily concentrated in 2021 and 2022. The plan aims to increase employment through support to MSMEs, the acceleration of large projects of infrastructure, and incentives for creative and cultural industries.

investment growth. Imports of goods and services are expected to grow robustly, around 14.4 percent. With higher external demand and oil prices, exports of goods and services are projected to grow 7.4 percent over a year earlier. Over the medium-term, a recuperation of external demand, private consumption growth, the 4G road infrastructure projects,[22] the Bogota metro project,[23] and improvements in investment planning and spending capacity at the subnational level are expected to support economic recovery. As GDP ascends towards its potential, growth would slow down. For the medium term, the baseline projection assumes a permanent level effect of COVID-19 on the level of activity, and a mild effect on trend growth (3.3 percent instead of 3.5 pre-pandemic).

21. **The current account deficit is projected to increase in 2021 to 4.2 percent of GDP and stabilize at 3.7 percent of GDP in 2023 and 2024.** In 2021 the trade deficit is projected to decline relative to 2020 as exports recover on the back of strong global growth and higher commodities prices, while imports (that already bounced back) keep growing fueled by domestic demand. Redistribution of dividends to foreign direct investors is expected to rebound in 2021 (including to compensate for low distribution in 2020) and then stabilize. It is expected that net FDI inflows will continue to finance most of the current account deficit. Government external borrowing and FDI flows are projected to provide the bulk of external financing (Table 3). As the growth of external demand picks up and that of domestic demand slows, the current account deficit is expected to narrow to 3.9 percent of GDP in 2022 and stabilize at 3.7 percent of GDP in 2023 and 2024.

22. **Under the baseline, the output gap will remain open past 2022, allowing the Central Bank to maintain an accommodative monetary policy for some time**. Relative to the trend prior to the COVID-19 crisis, the output gap will remain as large as 8 percent of trend GDP in 2021 and about 7 percent in 2022. Assuming that inflation expectations remain anchored (although there are some risks from recent increases), this would allow the Central Bank to maintain a stance that is supportive of growth until 2022, while still keeping inflation anchored at around the 3 percent target.

23. **The Central Government's deficit is projected to increase to 8.7 percent of GDP in 2021, followed by a decline to 7.2 percent of GDP in 2022.[24]** The economic recovery would allow a gradual pickup of revenues (as percent of GDP) in 2021, which would also be buoyed by measures to improve competitiveness supported by this DPF. Also, the authorities expect to raise about 1.1 percent of GDP from the sale of the government's participation in public companies, which the government is recording as revenues.[25] The emergency spending for the health sector appropriated but not executed in 2020 will be spent in 2021, as spending for the vaccine materializes in 2021. As a result, spending on goods and services will increase slightly in 2021. Similarly, the expected extension of transfer programs (*Ingreso Solidario*) will cause only a small decline in the transfers-to-GDP ratio (the nominal increase in GDP would

[22] Supported by the World Bank Capital Markets Strengthening Facility – ASA (P167816).
[23] World Bank Project P165300.
[24] According to the "2021 Medium-Term Fiscal Framework" and consistent with the draft fiscal reform bill presented to Congress on July 20, 2021, the government expects the Central Government deficit to increase to 8.6 percent of GDP in 2021 and decrease to 7 percent of GDP in 2022.
[25] The "2021 Medium-Term Fiscal Framework" contains a more optimistic projection of 1.3 percent of GDP. The resources would primarily come from the sale of the government's participation in ISA (an electric company) to Ecopetrol. Ecopetrol would finance the acquisition through a recapitalization in which only private investors participate. As a result, the government's participation in Ecopetrol would slightly decline, but the government would still remain the controlling shareholder. As a result, the government would retain control of ISA indirectly, through Ecopetrol.

cause a decline of 1.3 percentage point relative to 2020). Investment spending (primarily in infrastructure) is expected to increase by about 0.5 percent of GDP as part of the government's reactivation plan. As a result, the fiscal stance would be expansionary in 2021.

24. **The government's 2021 financing needs amount to 11.2 percent of GDP.** In addition to the deficit, these include amortization (1.7 percent of GDP) and payment for judicial rulings (0.8 percent of GDP). Sources of financing include domestic private sector borrowing (4.9 percent of GDP, 2.7 percentage points of which were raised before end-June 2021), utilization of savings accumulated in the Emergency Mitigation Fund (FOME, from its name in Spanish, for 1.1 percent of GDP), private sector external borrowing for 1.6 percent of GDP (of which 1.5 percent of GDP—US$ 4.6 billion—was raised between January 2021 and April 2021), borrowing from multilateral organizations (1.7 percent of GDP—US$4.9 billion, of which the World Bank is expected to provide US$2.3 billion, the IADB US$1.9 billion, the Development Bank of Latin America (CAF, from its name in Spanish) US$500 million, and others US$180 million), and a drawdown of deposits (2.0 percent of GDP).

25. **The COVID-19 crisis had a negative impact on the debt trajectory of the General Government, but the overall debt sustainability analysis indicates that, in the baseline scenario, the general government debt remains sustainable, although at a high level.** In the baseline scenario, the general government's debt to GDP ratio will increase to 70.9 percent in 2021, peak in 2023, start declining in 2024 and fall to 66.6 percent of GDP by 2026 on the back of a favorable growth-interest rate differential (Figure 5). With 65 percent of the public debt denominated in local currency and a large part at fixed interest rates, depreciation and interest rate shocks would not have a significant impact on the debt trajectory over the short to medium term. Standard sensitivity analyses on the baseline scenario show that slower than expected economic growth by one standard deviation in the short run would increase public debt levels to a peak of 76.8 percent of GDP in 2023. However, a combined macro-financial shock would cause public debt to peak at 87.5 percent of GDP in 2023 and decline from 2024 onwards.[26]

26. **The external debt sustainability analysis suggests that, after the increase in Colombia's external debt in 2020, it will gradually begin to fall in the medium term in all scenarios**. Colombia's external debt rose to 56.9 percent of GDP in 2020, on account of adverse exchange rate effects and rising fiscal pressures. As these shocks gradually fade, external debt will decline from 2021 on, reaching 52 percent of GDP in 2025 (Figure 6). Debt service will increase in the medium term but will remain manageable. Furthermore, Colombia has an excellent track-record of meeting its financial obligations, and its refinancing risks are mitigated by a diversified foreign investor base. Stress tests indicate that under an exchange rate shock[27] or a combined macro-financial shock[28], external debt will still decline after reaching its peak (2022 under the exchange rate shock, or 2023 under the combined shock).

27. **Risks around the 2021 baseline narrowed (relative to the beginning of the year) and titled on the upside, whereas risks over the medium-term are tilted somewhat to the downside.** On the external front, upside risks to growth stem from:

- A stronger recovery of external demand, especially over the Summer.

[26] Standard shocks applied to interest rate, exchange rate and GDP growth rate simultaneously.
[27] One-time real depreciation of 30 percent occurs in 2022.
[28] Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

- Stability in interest rate in the US (although inflation has risen in the U.S. in recent months, the Federal Reserve has not responded aggressively so far).
- A greater increase in the commodities prices owing to the higher growth of the Chinese economy and its demand for basic products.

On the domestic front, the main sources of upside risks include:

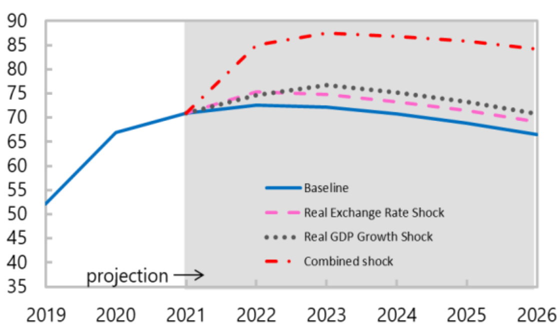
- A continuation of vaccination at June 2021 rate, as bottlenecks in vaccination are eliminated.
- Lower-than-expected effects of the national strike on economic activity, and a faster recovery in the second half of the year.
- An acceleration in the government's reactivation plan that allows increasing investment to levels higher than expected.

28. **For 2022 and onward, the main downside risks include the possibility that new strands of SARS-CoV-2 spread globally** (forcing new lockdowns, depressing demand, and requiring another round of massive vaccinations), and domestic difficulties in reaching consensus on a strong and convincing package of fiscal reforms that can reduce the deficit durably and ensure bringing down debt.

29. **The macroeconomic policy framework remains adequate for the purpose of the operation.** Colombia has solid fundamentals and macroeconomic policy institutions. Before the crisis, Colombia had built fiscal buffers that have helped respond to the COVID-19 crisis and leave space to mitigate to some extent the exogenous risks described above. Although the monetary policy rate has reached historically low levels, there is still some space for further cuts if need be, including because inflation and inflation expectations remain well anchored. On the external front, Colombia has ample reserves, and the International Monetary Fund (IMF) augmented the amount of Colombia's precautionary credit line. Although no other disbursements are foreseen, this credit line provides an important buffer for BOP financing. Finally, institutions and commitment to prudence remain strong. Specifically, the activation of the suspension clause of the fiscal rule was accompanied by an increase in the frequency of fiscal monitoring and assessment by the consultative committee on the fiscal rule (from an annual to a quarterly assessment).

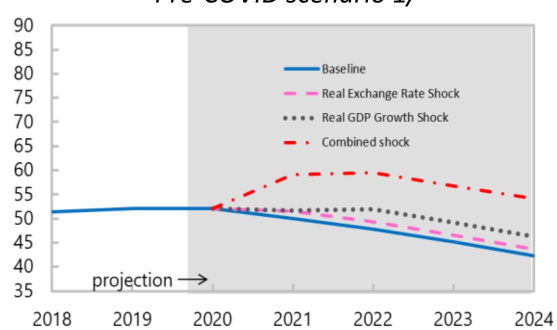
Figure 5. Debt Sustainability Analysis (General Government debt, percent of GDP)

Baseline scenario



Source: WB Staff projections.

Pre-COVID scenario 1/

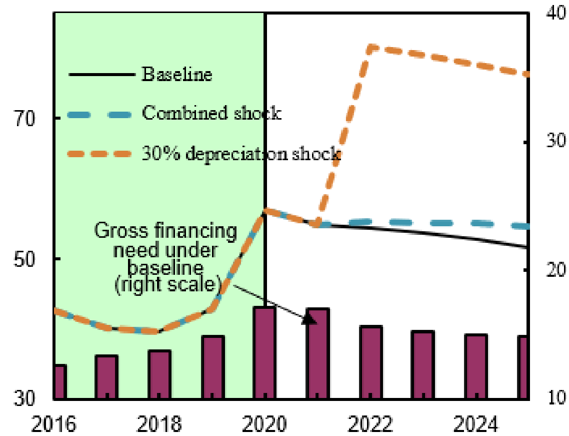


Source: WB Staff projections

Note: 1/ It uses macroeconomic projections made before March 2020.

Figure 6. External Debt Sustainability Analysis (External debt, percent of GDP)

Baseline scenario



Source: WB staff estimates.

2.3. IMF RELATIONS

30. **The IMF Board approved a US$17.2 billion Flexible Credit Line (FCL) for Colombia, concluded the 2021 Article IV consultation with Colombia on March 19, 2021, and the review of Colombia's performance under the FCL on April 28, 2021**. Colombia has had access to FCL arrangements since 2009, and it last renewed its FCL on May 1, 2020, for about US$10.8 billion, augmenting it to US$17.2 billion in September 2020. The authorities made a drawing of US$5.1 billion in December 2020 but intend to treat the rest of the credit line as a precautionary. IMF staff project that GDP will grow 5.1 percent in 2021, and another 3.6 percent in 2022, reaching pre-pandemic levels in the second half of 2022. They also project that the current account deficit will increase to 3.8 percent of GDP in 2021 and stabilize at 3.9 percent of GDP thereafter. Finally, they project that the Central Government's fiscal deficit will reach 9.5 percent of GDP in 2021 (this considers privatization receipts as a financing item) and will decline to 4.4 of GDP in 2022. At the conclusion of the review under the FCL, the IMF Board recognized that Colombia's very strong policy frameworks, anchored by a flexible exchange rate, credible inflation targeting-regime, effective financial sector supervision and regulation, and medium-term fiscal framework, continue to serve the country well and have allowed the authorities to deliver a coordinated and timely response to the COVID-19 pandemic. They also recognized that Colombia remains exposed to elevated external risks given the uncertainty about the path of the pandemic, and that the authorities continue to show their firm commitment to maintaining sound and prudent policies going forward. At the conclusion of the Article IV consultation, the IMF Board emphasized the need to sustain policy support in the near term both to protect the most vulnerable segments of the population, and to support economic activity, while safeguarding financial stability and fiscal sustainability. It stressed that, as the pandemic subsides, emergency measures should be gradually phased off. Finally, it agreed that return to fiscal rule would help anchor the fiscal framework and provide confidence over the medium term. In this respect, it indicated that striking right balance between flexibility and credibility will be important, and it encouraged considering measures to strengthen the fiscal framework and the fiscal rule. Finally, the IMF Board encouraged efforts to support employment, reducing informality, and raising productivity, and welcomed recent measures to formalize Venezuelan migrants. The IMF and World Bank maintain close collaboration.

3. GOVERNMENT PROGRAM

31. **The Government of Colombia has taken swift actions to control the spread of COVID-19, contain the socioeconomic crisis, and put in place a broad program to limit the impact of the pandemic and promote the gradual reactivation of the economy.** The initial emergency response strategy had four objectives:[29] (i) reduce the impact on public health by increasing detection and diagnostics, containing transmission through limited mobility, and strengthening the public health system; (ii) mitigate the impact on households by protecting employment and income and guaranteeing continuity of public services and utilities; (iii) mitigate the impact on firms, mainly by alleviating liquidity constraints, facilitating corporate reorganization and streamlining procedures, in addition to sector specific measures; and (iv) strengthen public finances with the creation of the Emergency Mitigation Fund (FOME) and supporting subnational governments by removing liquidity and budgetary constraints.

32. **The Government established a 3-axes economic reactivation plan for the short and medium term.** In addition to the three axes, the overall approach is complemented by sectoral policy documents in the areas of entrepreneurship;[30] electronic commerce;[31] STI;[32] and financial inclusion and education.[33] The three core axes are as follows:

(i) The first axis 1 consists of the two policy documents approved by CONPES to respond to the crisis. CONPES Document 3999[34] compiles the initial response actions taken by the Government between March 2020 and July 2020, and establishes the monitoring process going forward, in four areas: health, welfare protection of households, mitigation of effects on the productive apparatus, and public financing. CONPES Document 4023[35] comprises the medium-term strategy consisting of the "Policy for Reactivation and Sustainable and Inclusive Growth 2021-2026"[36] and the investment plan "New Commitment to the Future of Colombia[37] for the period 2020-2030" (See Box 1).

(ii) The second axis focuses on the prioritized and accelerated implementation of commitments contained in the PND 2018-2022 with respect to social inclusion, modernizing social policy, boosting the information and communication technologies (ICT) sector, supporting business development,

[29] The strategy was compiled in the CONPES Document 3999 "Initial response strategy to the effects of the COVID-19 pandemic on public health, households, the productive apparatus and public finances", DNP. August 5, 2020. *https://colaboracion.dnp.gov.co/CDT/Conpes/Econ%C3%B3micos/3999.pdf*

[30] Documento CONPES 4011 *Política Nacional de Emprendimiento*, November 30, 2020. *https://colaboracion.dnp.gov.co/CDT/Conpes/Econ%C3%B3micos/4011.pdf*

[31] Documento CONPES 4012 *Política Nacional de Comercio Electrónico*, November 30, 2020. *https://colaboracion.dnp.gov.co/CDT/Conpes/Econ%C3%B3micos/4012.pdf*

[32] *Política Nacional de Ciencia, Tecnología e Innovación 2021-2030.* In preparation to be approved by CONPES by December 2021.

[33] Documento CONPES 4005 *Política Nacional de Inclusión y Educación Financiera*. September 28, 2020. *https://colaboracion.dnp.gov.co/CDT/Conpes/Econ%C3%B3micos/4005.pdf*

[34] Documento CONPES 3999 *Estrategia de respuesta inicial ante los efectos de la pandemia del COVID-19 sobre la salud pública, los hogares, el aparato productivo y las finanzas públicas*. August 5, 2020. Bogota, Colombia. *https://colaboracion.dnp.gov.co/CDT/Conpes/Econ%C3%B3micos/3999.pdf*

[35] Documento CONPES 4023 Política para la reactivación y el crecimiento sostenible e incluyente: Nuevo compromiso por el futuro de Colombia. February 11, 2021. Bogota, Colombia. *https://colaboracion.dnp.gov.co/CDT/Conpes/Econ%C3%B3micos/4023.pdf*

[36] *Política para la reactivación y el crecimiento sostenible e incluyente*

[37] *Nuevo Compromiso por el Futuro de Colombia*. *https://compromisoporcolombia.gov.co/*

and advancing agribusiness.

(iii) The third axis aims to implement recommendations by the internationalization taskforce of national and international experts (*Misión de Internacionalización*) launched in August 2021 and by the employment taskforce of national and international experts (*Misión de Empleo*) to be concluded in October 2021.

33. **Colombia's development strategy recognizes the leading role of the private sector for increasing productivity and boosting reactivation**. One of the three pillars of the National Development Plan 2018-2022 aims at boosting productivity, increasing business formalization, and promoting dynamic entrepreneurship. It focuses on building a more favorable business environment to establish formal and competitive businesses, support the productive transformation of firms, simplify the interaction with the public sector, leverage international trade and attract productive investments.[38] The PND 2028-2022 also comprises two key cross-cutting themes: STI and digital transformation. The PND 2028-2022 builds on the "Productive Development Policy" (PDP) that sets out a 2016-2025 action plan to tackle structural factors hampering productivity growth. The PDP places the firm at the center of efforts to increase productivity, by encouraging the provision of enabling public goods, as well as promoting technological transformation, access to finance for innovation and entrepreneurship, and participation in global value chains. Furthermore, the government has joined forces with the private sector by signing 22 sectoral pacts with 86 production guilds to generate employment and economic growth. These pacts set specific commitments for both the government and the private sector, aimed at increasing the productivity and competitiveness of the sectors, and enhancing their capacity for innovation, production, employment, sales, and exports. The pacts also set ambitious targets for 2022: 1.1 million new jobs, US$14 billion in productivity increases, and US$10 billion in additional exports. Since August 2019, as a result of the pacts, 34 decrees, 30 resolutions and 37 instruments of public policy have been issued, and 10 special lines of credit have been created for a value of COP 564 billion.

[38] Additionally, this pillar focuses on fostering progress in the countryside and the tourism sector.

Box 1. Colombia's Policy for Reactivation and Sustainable and Inclusive Growth

The "Policy for Reactivation and Sustainable and Inclusive Growth: New Commitment to the Future of Colombia", approved by CONPES in February 2021, seeks to develop capacities in households, the productive sector and the government for accelerated, resilient, and sustainable economic reactivation and growth. To achieve this objective, the policy is structured in five pillars:

1. ***Mitigation of the increase in poverty and economic vulnerability***, by improving the targeting (Sisbén IV, rural registry) of social programs for the reduction of monetary and multidimensional poverty; promoting access to adequate housing; and mitigating the risk of higher incidence of poverty and vulnerability for the population in rural areas by promoting subscriptions to the Social Protection Floor enacted in August 2020.
2. ***Mitigation of the human capital loss***, by (i) strengthening childcare and education with a focus on positive discipline and play-based learning, promotion of science, technology, engineering and mathematics (STEM) education, improving connectivity, nutrition and food safety; (ii) limiting school dropout and pursuing education catch-up through close monitoring and active search, improvement of ICT tools usage, infrastructure adjustment, loosening financial constraints for higher education; (iii) strengthening links between higher education and the productive sector, and improving the VET system; (iv) creating incentives for the prevention of chronic non-communicable diseases and promotion of healthy habits, and (v) implementing a strategy for the acquisition, storage, distribution and administration of a safe and effective vaccine against COVID-19.
3. ***Towards greater and more sustainable growth***, by (i) implementing recommendations by the Employment Taskforce; (ii) facilitating access to finance by promoting the development of factoring and crowdfunding, while improving the regulatory framework to promote capital market development; (iii) promoting global integration by reducing costs and streamlining procedures for importing and exporting, as well as implementing recommendations by the Internationalization Taskforce; (iv) increasing the implementation of quality and biosafety standards; (v) strengthening agricultural extension and innovation programs; (vi) promoting investment in transport infrastructure projects; (vii) fostering the energy transition through the implementation of energy efficiency programs and enabling the use of non-conventional sources of renewable energy in non-interconnected zones; (viii) increasing innovation and technology adoption in the productive sector by implementing applied research programs among firms, clusters, universities, and research centers; expanding technical assistance programs for productive and digital transformation processes and adoption of 4.0 technologies; facilitating the use by private sector of infrastructure and physical spaces (networks of tech centers, open labs, research universities) to carry out tests, prototypes, etc.; increasing public and private investment in STI activities, prioritizing resources from the General Royalties Fund; and (ix) fostering the bioeconomy and the circular economy.
4. ***Boosting institutional capacities and citizen trust***, by strengthening the State-Citizen relationship with the improvement of the perception of transparency in public decision-making and facilitating public consultation and collaboration in the reactivation process and COVID-19 measures; strengthening subnational interventions both financially and institutionally, and guaranteeing articulation across government levels; and improving citizen security and disrupting crime, increasing judicial effectiveness and citizens' perception of justice; and promoting digital transformation programs of justice administration.
5. ***Acceleration of digital enablers***, by (i) strengthening and increasing internet connectivity in the territories, through the implementation of a national digital single window for procedures related to the deployment of telecom infrastructure and exploring innovative and non-traditional alternative technologies to deploy telecom infrastructure in rural and remote areas; (ii) accelerating the development of GovTech services and solutions through public procurement for innovation; and (iii) developing a National Data Infrastructure Plan to sustainably strengthen the data ecosystem and enabling the adoption of Fourth Industrial Revolution technologies.

The policy actions set objectives for the short- and the long-run. Short-run actions aim at tackling temporary issues in 2021-2022, assuming a scenario in which COVID-19 is not yet fully controlled and mobility restrictions are still in place. Longer-term actions address structural issues that have deepened with the pandemic in 2023-2026, under the assumption that the pandemic has been controlled, with businesses operating normally and unrestricted mobility.

The policy actions are complemented by the investment plan "**New Commitment to the Future of Colombia"**, implemented jointly with the private sector. It comprises new and ongoing investments, between 2020-2031, for COP 163 trillion (around 16 percent of GDP). The plan aims mostly at generating employment (80 percent), promoting green and clean growth (12 percent) and reducing poverty and vulnerability (10 percent). About 42 percent of investments are mainly focused on housing construction, education, agriculture, oil, infrastructure, and artistic activities (between 2020-2022). The remaining 53 percent will focus mainly on transport infrastructure (between 2023-2031). By 2030, it is expected that the plan will increase economic growth by 2.86 percent, and it will generate 758 thousand new jobs.

Source: Documento CONPES 4023 *Política para la reactivación, la repotenciación y el crecimiento sostenible e incluyente: Nuevo compromiso por el futuro de Colombia*. February 11, 2021. DNP, Bogota, Colombia.

4. PROPOSED OPERATION

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

34. **The proposed DPF directly supports key components of the Government's COVID-19 reactivation strategy.** The operation is designed to encourage a high-productivity and sustainable recovery by (i) fostering private sector through better regulation, broadened access to green capital markets, and increased competition and transparency in public procurement [Pillar I]; (ii) boosting investment in STI, including with an environmental sustainability focus, and increasing the use of digital platforms to raise capital through crowdfunding and effect payments [Pillar II]; (iii) promoting enterprise creation, operation and growth and at the same time international integration through high-growth entrepreneurship oriented support and trade facilitation [Pillar III]. Moreover, the proposed DPF is directly related to pillars 3 (*Reactivation of the productive apparatus towards greater and more sustainable growth*) and 4 (*Digital Transformation*) of the Government's "*Reactivation and Sustainable and Inclusive Growth Policy"* (Box 1 above) as well as to the goals of the PND 2028-2022's *Productivity, Formalization and Entrepreneurship* pillar.

35. **Several measures supported by this operation contribute to structural reforms in areas where the World Bank has been actively engaged with the Government of Colombia**. In Pillar I, actions on regulatory reform are the result of policy dialogue through World Bank and International Finance Corporation (IFC) projects, and actions on access to finance and green finance build on the World Bank's engagement in the Capital Markets Taskforce. In Pillar II, actions on innovation stem from a long-standing dialogue on productivity and innovation policy. In Pillar III, actions to boost trade build on the ongoing engagement of the World Bank in the Internationalization Taskforce. Actions on entrepreneurship also build on policy dialogue through World Bank and IFC projects.

36. **The DPF is in line with the World Bank Group's climate change commitments, incorporating climate change considerations in various aspects of the program design that promote an environmentally sustainable recovery from the COVID-19 shock.** Colombia is exposed to several natural hazards such as flooding, water scarcity, extreme heat, and precipitation events. Projected rising temperatures and changing precipitation patterns are expected to lead to more frequent and intense natural disasters that are affecting the country's hydropower and agriculture, among others. Noting that Colombia's economy is highly dependent on its rich endowment of natural wealth and that current economic patterns make inefficient use of resources and are unsustainable, a need to translate into a cleaner economic model to transform the economy and address the challenge of climate change remains critical in the context of Colombia's recovery efforts. The DPF takes these challenges and related opportunities into account and, with a view to promoting an environmentally sustainable recovery, incorporates measures on green finance and entrepreneurship and innovation that aim at mitigating climate action or promote the use of clean and non-conventional renewable energies and battle deforestation. Also, supported digital payments facilitate relief support and increase resilience from natural disasters.

37. **Lessons learned in the implementation of previous development policy operations have been reflected in the design of this operation**. The experience of the Fiscal Sustainability and Growth Resilience DPF series (FY12/13) and the Enhancing Fiscal Capacity to Promote Shared Prosperity DPF

(FY14) suggests that: (i) the World Bank's ability to provide cross-sectoral support through a DPF is an effective tool to address the client's cross-cutting challenges; (ii) DPFs can serve as a vehicle for deepening the policy dialogue on fundamental issues, even beyond the scope of the program supported by the operation; and (iii) the World Bank's role as a provider of technical knowledge can further add to the value of a DPF. Additionally, the World Bank has developed a comprehensive and progressive approach to help Colombia face the impact of the pandemic from which the proposed operation draws important lessons learned. Namely, the experience of the COVID-19 Crisis Response DPF and the Resilient and Sustainable Infrastructure for Recovery DPF Series have emphasized the value of responding quickly to Government needs with flexibility and creativity while focusing on impact in close collaboration with counterparts. These lessons are reflected in the proposed operation, which: (i) supports a crosscutting but interlinked set of reforms to reignite sustainable growth in the wake of the COVID-19 crisis; (ii) is based on strong policy dialogue and technical assistance; and (iii) is founded on the knowledge generated by the World Bank Group, based on international experience, to help client countries respond to the crisis. The proposed operation has been developed in close collaboration with the Colombian Government, reflecting a key lesson learned from other DPFs on the importance of country ownership and commitment to achieve the program's objectives.

4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

38. **The development objective of the program supported by the proposed operation is to encourage a high-productivity and sustainable recovery from the COVID-19 crisis by (i) improving regulation for a private sector-led recovery; (ii) promoting innovation and digital finance; and (iii) fostering entrepreneurship and internationalization.** Through three corresponding pillars, the program is supporting the Government's efforts to address market failures, remove distortions, and improve the quality of firms, with the aim of lifting Colombia's productivity growth path in the medium term.

39. **The proposed program includes reforms that address structural bottlenecks to productivity growth, both external to firms and pertaining to firms' own capabilities.** Productivity growth can be decomposed into three components.[39] The first component refers to the between-firms productivity gains from reallocation of factors of production; the second refers to the within-firms productivity gains from individual firms becoming more productive; and the third component refers to gains from entry of high-productivity firms and exit of low-productivity firms. Policy interventions that resolve market failures, remove distortions, and improve the quality of firms can promote gains in these three components. Through its three complementary pillars, the program aims to promote a steady recovery by addressing structural issues in the operating environment, as well as limitations in firms' own capabilities that hinder the three components of productivity growth.

Pillar I: Improving the regulatory environment for private sector-led recovery

40. **Robust and environmentally sustainable reactivation of the economy involves tackling structural constraints to the private sector activity arising from regulation.** Improving regulation to ease the development and growth of enterprises is at the core of the current PND as part of one of its three

[39] Cusolito, Ana Paula; Maloney, William F. (2018) Productivity Revisited: Shifting Paradigms in Analysis and Policy. Washington, DC: World Bank. © World Bank. *https://openknowledge.worldbank.org/handle/10986/30588* License: CC BY 3.0 IGO.

main pillars (*Pacto por el emprendimiento y la productividad)*. Moreover, the national reactivation strategy from the COVID-19 crisis includes policies to improve competitiveness through a better regulatory environment, aiming to achieve higher and more sustainable growth. These initiatives recognize that productivity growth in Colombia has been practically nil over the last decades as a consequence of factors that are both external and internal to firms. External factors include the regulatory environment, access to finance, and market competition, areas in which Colombia performs poorly. Despite recent efforts to streamline and simplify procedures and regulations (e.g., "*Colombia Simple"*, "*Estado Ágil"*), Colombia ranks 57th among 141 countries in the overall Global Competitiveness Index, and fares particularly poorly in the burden of government regulation (123rd) and domestic competition (110th). Colombian capital markets benefit from a robust regulatory framework, risk-based financial supervision, an integrated infrastructure, and an institutional framework conducive to regional integration. However, the private debt market for green bonds is concentrated in a few blue-chip issuers, leaving the vast majority of firms starved for long-term and climate-friendly financing. Regulation for the green bonds market is required to facilitate the private sector access to new financing instruments and to ensure businesses' environmental sustainability. In addition, the regulatory framework for public procurement does not foster competition as the lack of standardized procedures in this area limits transparency. These structural limitations, if not addressed, are likely to make Colombia's economic recovery less robust and less sustainable.

41. Against this backdrop, Pillar I supports reforms to (i) reduce the cost of doing business by adopting better regulation policies and reducing its carbon footprint; (ii) facilitate access to green finance; and (iii) level the playing field in public procurement.

Prior Action #1. *The Republic of Colombia has taken measures aimed at reducing the cost of doing business by: (a) mandating the simplification, automatization and digitalization of administrative procedures and information obligations on businesses; and (b) institutionalizing the steps required for improving the quality and predictability of technical regulations that directly impact production and marketing costs, as evidenced, respectively, by Law No. 2052, published in the Official Gazette on August 25, 2020, and Decree No. 1468, published in the Official Gazette on November 12, 2020.*

42. **Rationale**. The Colombian regulatory framework continues to be cumbersome.[40] According to the World Bank's Enterprise Surveys in 2017, senior management in Colombia spend 19.5 percent of their time dealing with government regulation, compared with 12.6 percent in the LAC region and 8.2 percent globally. Due to the social distancing imposed by the pandemic, as well as observed and anticipated climate change impacts that are disturbing business continuity of Colombian firms in the face of natural disasters, it has become imperative for governments to digitize and offer online solutions for the private sector to comply with regulatory administrative requirements and improve climate change resilience of Colombian firms[41]. In Colombia, there are more than 2,600 administrative procedures that are part of

[40] Colombia's efforts to alleviate the regulatory burden have yielded important results: the issuance of regulatory production has dramatically decreased since 2017, going from 8,064 regulations to 5,513 regulations issued in 2019 (DNP, 2020). However, these efforts have not been reflected in the share of non-substantial regulations being issued, which continue to be more than half of all regulations at the national level (from 62 percent in 2017 to 55 percent in 2019). Non-substantial regulations refer to regulations of an administrative or procedural nature (e.g., clarifications, authorizations and designations), while substantial regulations consider those with general effects.

[41] The most recent El Niño phenomenon left losses in the productive sectors of the order of COP 3.1 trillion, equivalent to 0.6

the Single Registry for Administrative Procedures (SUIT*, Sistema Unico de Informacion de Trámites*).[42] As of December 2020, only about 26 percent of those administrative procedures can be conducted online, 42 percent partially online and 32 percent require physically interaction. At the subnational level, numbers are even worse. More than 91 percent of the 68,000 existing subnational administrative procedures require physical presence. In addition to solving these issues related to regulatory administrative burdens, following the example of many OECD and developing countries, Colombia requires a whole-of-government system that improves the quality of business regulations.[43] Efforts should be directed towards (i) the creation of a legal mandate, (ii) dedicated institutions to coordinate and support policy implementation, and (iii) the adoption of good regulatory practices that improve predictability, transparency, participation and use of evidence-base approaches in the design and review of regulation.[44]

43. **Substance of the prior action**. The Law 2052/2020, also referred to as the Administrative Simplification Law (*Ley de Racionalización de Trámites*), aims to reduce the time and cost that the private sector and citizens allocate to complying with administrative procedures or government transactions (*trámites*). Among its provisions, the Law creates the necessary conditions and requirements for government agencies to simplify, automate and digitize administrative procedures. This Law is aligned to the *Estado Simple, Colombia Ágil* Strategy. Box 2 explains the substance of the Administrative Simplification Law. In addition to Law 2052/2020 and in accordance with the recommendations of the technical assistance provided by the WBG over the last two years, the Ministry of Commerce, Industry and Tourism enacted the Decree 1468 in November 2020. The objective of the decree is to establish a whole-of-government better regulation[45] control mechanisms applied to the production and review of technical regulations.[46] These controls mechanisms include the implementation of forward planning, ex-ante RIA, public consultation, and ex-post review of existing regulation. Overall, these measures applied to technical regulations can reduce the costs of production and marketing of goods controlled by this

percent of the GDP of 2015 as a consequence of the reduction in the water supply and the increase in the price of electricity (DNP, 2018). On the other hand, the La Niña phenomenon and its increasingly strong rainy seasons have also dramatically affected the productive sector. Only last year, the only road communicating the department of Choco (one of the most underdeveloped) with the main and closest economic center (Medellin, one of the largest Colombian cities) was closed for 19 days due to landslides caused by extreme and prolonged heavy rain. For instance, in late 2020, Colombia suffered simultaneously from the economic, social and human impact of the La Niña phenomenon, the cyclone Eta and the hurricane Iota. In 2017, the "Mocoa landslide" left the city uncommunicated and some areas completely vanished.

[42] *https://www.funcionpublica.gov.co/web/sie/tramites-del-estado-inscritos-en-el-suit*

[43] An OECD report on regulatory policy in Colombia made recommendations for better regulation, including the implementation of ex-post evaluations. OECD (2013), Regulatory Policy in Colombia: Going beyond Administrative Simplification, OECD Reviews of Regulatory Reform, OECD Publishing, Paris, *https://doi.org/10.1787/9789264201941-en*

[44] Good regulatory practices include tools such as forward planning, ex-ante regulatory impact analysis (RIA), public consultation, ex-post review of existing regulation and administrative simplification.

[45] According to the European Union, Better Regulation "means designing EU policies and laws so that they achieve their objectives at minimum cost. Better regulation is not about regulating or deregulating. It is a way of working to ensure that political decisions are prepared in an open, transparent manner, informed by the best available evidence [The Commission has a policy on data, information and knowledge management which helps support policymaking by maximizing the use of data (SWD, 2016). In this context, the EU Open Data Portal is important as a source and repository of open data] and backed by the comprehensive involvement of stakeholders". European Commission (2017), 'Better Regulation' Guidelines, 2017, p. 4, Luxembourg, Publications Office of the EU, *https://ec.europa.eu/info/sites/info/files/better-regulation-guidelines-better-regulation-commission.pdf*.

[46] The Ministry of Commerce, Industry and Tourism defines technical regulation as a document that establishes the characteristics of a product or the methods and procedures related to it, including the related administrative procedures that are mandatory. Technical regulation also includes prescriptions regarding product terminology, symbols, packaging, labelling, process, or production methods.

type of regulation.[47] Importantly, these regulations are notified to the World Trade Organization (WTO) because they constitute non-tariff trade barriers. Hence, this measure complements the trade facilitation objectives of Pillar III. The main regulatory governance improvements introduced by Decree 1468/2020 are described in Box 3.

Box 2. The Administrative Simplification Law

In order to reduce the time and cost to comply with administrative procedures, Law 2052 of 2020 requires, among other things: periodic reviews for simplification purposes; automatization, digitization and online delivery of administrative procedures; simplification efforts on administrative procedures that are part of a broader chain of government transactions; promotion of alternative compliance approaches, such as simple notifications, automatic authorizations and adoption of indefinite licenses and registration, balanced with better supervision and oversight; and more transparency and access to information by strengthening the Single Registry of Administrative Procedures (SUIT).

Source: Law 2052 of 2020, Official Gazette No. 51,417.

Box 3. Regulatory Impact Analysis according to Decree 1468 of 2020

Decree 1468 of 2020 improves the procedures and mechanisms to plan, design and review technical regulations that directly impact production and marketing costs. It does so by adopting good regulatory practices along the regulatory cycle, including: (i) forward regulatory plans, which announce in advance upcoming regulatory changes; (ii) ex ante RIA and public consultation, which introduce evidence-based and participatory approaches to the design of regulations; and (iii) ex post impact evaluations to assess periodically whether regulations achieved their intended results and are still relevant. The combination of these tools brings more predictability, transparency, evidence, and trust to the regulatory process.

Source: Decree 1468/2020.

44. **Expected results**. The better regulation policies and directives established by Law 2052/2020 and Decree 1468/2020 are expected to reduce the cost of doing business in Colombia. This result will come from less burdensome and time-consuming administrative procedures, which will allow businesses to allocate more resources and time to productive activities and less to conducting government transactions. Results are also expected to come from improved new and existing technical regulation affecting production and marketing costs. Lastly, by facilitating the uptake of digital transactions, this prior action will also reduce the vulnerability of Colombian firms through ensuring business continuity in the event of climate change-induced natural disasters.[48] This reform implies a significant reduction in travel and physical courier costs. Expected results will be measured by a reduction in the regulatory burden, measured as total savings in compliance costs[49], from 0 in 2020 to COP 179,468 million in 2022.

[47] As of January 2021, there were 98 technical regulations in place imposed by the Ministry of Agriculture and Rural Development, the Ministry of Environment and Sustainable Development, the Ministry of Commerce, Industry and Tourism, the Ministry of Health and Social Protection, the Ministry of Mining and Energy, the Ministry of Housing, City and Territory, the Superintendence of Industry and Commerce, and the General Secretariat of the Andean Community.

[48] As mentioned earlier (see footnote 41), recent natural disasters have had costly impacts in the country, disrupting businesses and cities disconnected from other cities and across neighborhoods within cities. This was the case in the state of Choco in 2020 and the city of Mocoa in 2017, to name the most drastic recent episodes.

[49] DAFP developed a methodology to measure compliance costs savings related to regulatory and administrative simplification policies and programs. The methodology is similar to a Standard Cost Model (SCM), a tool commonly used in the world to measure

Prior Action #2. *The SFC has adopted measures to ensure transparency and integrity of the market for green finance by developing the taxonomy of Green Bonds in securities issuances as well as instructions on the minimum information that the prospectus for issuance of these bonds should contemplate, as evidenced by SFC External Circular No. 028/2020 dated September 7, 2020 and published in the SFC's website.*

45. **Rationale**. Increasing access to greener capital markets can play a key role in powering a broad-based and climate-friendly recovery of the Colombian economy from the COVID-19 shock. The green bond market in Colombia has experienced exponential growth, reaching issuances for COP 2.36 trillion between 2016 and 2019, primarily led by the banking sector and with growing diversity in terms of geography and projects financed.[50]

46. **Substance of the prior action**. External Circular 028/2020 and the accompanying Good Practice Guide for the Issuance of Green Bonds institutes a clear regulatory framework for the issuance of green bonds, thus increasing access to green finance. To ensure transparency and integrity of the market for green finance, the External Circular specifies the minimum information that the prospectuses for issuance of these bonds must contemplate. These are aligned with the Green Bond Principles developed by the International Capital Market Association, which issuers of green bonds in the primary domestic market have to comply with concerning: use of funds; project evaluation and selection; fund management; publication of annual reports on the use of funds and their respective impacts; and use of external audit. The principles also set clear minimum requirements to facilitate knowledge by new investors and make the authorization and supervision processes more expeditious and cost-efficient. With this action, Colombia becomes the first country in Latin America to have an exclusive regulatory framework for green bonds, laying a solid basis for the further development of the local green bond market and supporting its national and international climate change policy objectives, including its recently submitted revised Nationally Determined Contribution (NDC) in which the country commits to reduce greenhouse gas emissions by 51 percent in 2030 compared to a baseline scenario, which, among others, is expected to be achieved through the use of innovative green/climate finance.[51]

47. **Expected results**. The introduction of a regulatory framework for green bonds to finance private investment will contribute to Colombia's climate change policy objectives and commitments by facilitating the relationship between issuers and investors, as well as strengthening the protection,

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and monetize regulatory burdens. In the case of Colombia, compliance cost savings from government policies and programs come from reducing the time to complete an administrative procedure (*trámite*); eliminating the need to physically be present to deliver documents or pay fees; eliminating associated costs for transportation or shipment of documents; reducing fees; and eliminating other costs related to compliance with regulatory requirements.

[50] Green bonds refer to debt instruments whose proceeds have to be used for projects that contribute to the fulfillment of goals around mitigation and/or adaptation to climate change, the conservation of biodiversity and/or the control of air, water and soil pollution, among others. The authorization mechanism and other regulations for the issuance of green bonds are similar to ordinary bonds and, therefore, the public offering must be authorized by the Financial Superintendence of Colombia and registered in the National Registry of Securities and Issuers (NRSI). However, in the case of green bonds, to ensure transparency and integrity of the market, it is essential for the issuer to comply with additional obligations to be detailed in the prospectus and complementary documents of the issuance. With joint IBRD/IFC technical assistance, the Financial Superintendence is implementing a strategy that aims to integrate climate-related risks (and opportunities) in the relevant financial regulatory and supervisory framework. The Financial Superintendence is also leading efforts to develop a nationally agreed classification framework of activities that contribute to climate change mitigation and adaptation specifically (i.e., green taxonomy).

[51] External Circular 028/2020 and the accompanying Good Practice Guide for the Issuance of Green Bonds have been developed with WBG technical assistance.

transparency, trust, and integrity of the local market. Increasing the uptake of green bonds will lead to an increase in low-carbon and climate-resilient investment since the use of the resources raised from green bonds must be aimed at financing or refinancing all or part of eligible green activities or projects. The supported action is expected to increase green bond issuance from none in 2019 to 4 by 2022.[52]

Prior Action #3. *The Republic of Colombia has taken measures to facilitate an increase in competition and transparency in public procurement by mandating the National Agency of Public Contracting Colombia Compra Eficiente to adopt mandatory standard bidding documents in the contractual activity of all entities subject to the General Contracting Statute of the Public Administration, as evidenced by Law No. 2022, published in the Official Gazette on July 22, 2020.*

48. **Rationale**. Public procurement is an important tool to stimulate investment and employment. During 2021-2023, 30.2 percent of total government expenditure is estimated to be channeled through public procurement, making effective and transparent procurement processes a powerful engine for the economic recovery following the COVID-19 shock.[53] Lack of consistency between government entities and within the same entity negatively affects transparency and increases the time and costs that suppliers face when participating in government procurement. Standardization of procurement processes, in particular the use of standard bidding documents (SBD),[54] increases transparency and reduces the risk that tenders are tailor-made to favor certain suppliers, while bringing value for money through increased competition. Beginning in early 2019 with public transport works - a sector where, historically, competition has been hindered by tailored conditions for specific bidders[55] - the government has been rolling out the mandatory use of standardized open tender documents.[56] According to an analysis of tenders under the new regime in the infrastructure civil works sector between April 2019 and August 2019, the number of bids increased both at the national and regional level.[57] Enhanced inter-institutional cooperation, notably with the competition authority (*Superintendencia de Industria y*

[52] The number of issuances of green bonds as selected indicator relates to the fact that what is important to be measured is that more bond issuances adhere to the taxonomy (as more issuances use it the more successful this measure). Note that the volume of the issuances will not capture this.

[53] In 2017 public procurement expenditure in Colombia stood at 34 percent of total government expenditure and 9.93 percent of GDP, well above the LAC average of 17.4 percent and 6 percent, respectively. OECD (2020), Government at a Glance: Latin America and the Caribbean 2020, OECD Publishing, Paris, https://doi.org/10.1787/13130fbb-en.

[54] The concept "standard" implies a document or a process that cannot be changed, except in previously defined variable aspects (such as the identification of an entity or the quantity to be contracted).

[55] Bajpai, Rajni; Myers, C. Bernard (2020) Enhancing Government Effectiveness and Transparency: The Fight Against Corruption (English). Washington, D.C.: World Bank Group. *http://documents.worldbank.org/curated/en/235541600116631094/Enhancing-Government-Effectiveness-and-Transparency-The-Fight-Against-Corruption*

[56] The deployment of SBD is being done by type of procurement. So far SBD have been prepared and approved for infrastructure contracts (Civil works and supervision), water and sanitation (Civil works) and a contract for multipurpose cadaster services is under preparation.

[57] At the national level, 61 percent of tenders received more than 20 bids while 20 percent received between 11 and 20 bids, and only 19 percent received fewer than 10. At the regional level, results were more muted but still impactful: 20 percent of tenders received more than 20 bids, and 48 percent received between 2 and 10 bids, while 32 percent received only one. The same analysis showed that the standard documents were used in their original or a modified version in more than 90 percent of tenders across national and regional cases. *Cámara Colombiana de la Infraestructura* (2019) "Observatorio de Contratación. Resultados del 1 de abril al 31 de agosto de 2019". Bogotá, Colombia. *http://www.infraestructura.org.co/16congreso/presentaciones/observatorio-contratacion.pdf*. For more information (in Spanish): Campos Borja, Luis Miguel, et al. "Pliegos tipo como instrumento para la transparencia en la contratación estatal en Colombia." (2019).

Comercio, SIC), is critical to further increase the efficiency and transparency of procurement processes by tackling bid-rigging cartels (Box 4).

Box 4. Detection of bid-rigging cartels by the Superintendence of Industry and Commerce

Bid rigging cartels occur when bidders agree to eliminate competition through, among others, the submission of non-competitive or non-conforming bids, abstention or withdrawal from a bid, bidding only in certain areas or to certain public buyers (market sharing) or bid rotation. The OECD estimates that the elimination of bid rigging could help reduce procurement prices by 20 percent or more. In Colombia, between January 1, 2017 and November 30, 2020, SIC sanctioned 20 cases for bid rigging for a total value of COP 275,688 million. This implies an average of 5 bid-rigging cases per year for SIC as compared to an average of 8 cases of all cartel offenses per year across jurisdictions captured by the OECD.

Detecting bid rigging requires assessing the presence of factors such as: numbers of bidders, same bidders involved in repeated procurements, standardized products/services, relationships between bidders, opportunities for bidders to communicate with each other, among others. Access to information on past bids or tenders enables monitoring of markets, as well as identification of suspicious patterns, while bidding data need to be reliable and directly accessible, including through software to screen tender data.

The tool for screening procurement data introduced by the Superintendence of Industry and Commerce (SIC) will allow access to data held by public bodies and increase detection of bid-rigging schemes. The tool is currently in beta stage and will be formally launched and be fully operational in 2021. Among others, the tool will screen data on similar procurement procedures, bidders, agencies that continually enter into agreements with the same bidders and relationships between representatives of different bidders. SIC investigators will then be able to process the data more efficiently and identify patterns that could indicate the presence of bid rigging, which will strengthen detection and dismantling of bid rigging cartels.

Data aggregating software is necessary to uncover suspicious patterns that could otherwise not be observed. Implementation of the screening tool will have tangible effects on competition. The tool will increase the probability of detecting restrictive practices and, in turn, deter bidders from engaging in anticompetitive conduct. SIC will submit a formal communication to all public bodies, at the national and subnational level, to inform them of the launch of the tool to foster inter-institutional cooperation in bid rigging investigations.

Use of technological tools to increase the quality of public expenditure is not new in Colombia. Decree 403 of March 16, 2020 allows the General Comptroller (*Contraloría General de la República, CGR*) to rely on intelligent information management, understood as the efficient use of all available technological capabilities (artificial intelligence, data analytics and data mining, predictive and prospective analysis, among others), for the early determination of bad practice events, with significant probability of occurrence, persistence or mutation, and that involve risks of loss of public assets.

49. **Substance of the prior action.** The introduction of standard bidding documents increases the transparency of procurement procedures. Law 2022/2020 mandates adoption by CCE of standard bidding documents in the contractual activity of all entities subject to the General Contracting Statute of the Public Administration. The Law's main objective is to ensure transparency in contracting for public works and improve the plurality of participants in bidding processes. It includes the following main features: (i) SBD will contain the enabling requirements, selection criteria (economic, technical, and other factors) and other requirements that, after justification, represent good contractual practices for the adequate development of the principles that govern public procurement; (ii) with the aim of promoting decentralization, local employment, development, services and local industry, in the adoption of the SBD, the characteristics of the regions, the amount of the activity, the promotion of the local economy and the nature and specialty of the contract will be considered; training to assure these results must be carried by the CCE for the municipalities; (iii) the CCE will establish an implementation schedule and define, in coordination with the corresponding technical or specialized entities, the procedure to gradually implement the SBD and will create the procedure to receive and review comments from

interested parties; (iv) the SBD will comprise public works, supervision services, supervision studies, design services and engineering consultancy for civil works.

50. **Expected results**. In 2020, the Government prepared and approved the SBD for infrastructure and water and sanitation. For 2021, its target is to prepare and approve the SBD for five sectors: Cadastral services, social infrastructure, education infrastructure, hospitals infrastructure, and sports and recreative infrastructure. Different possible indicators were considered during the preparation of this operation, but it is difficult to have comparable data in dimensions as fiscal savings. It is expected that the mandatory use of SBD, established in Law 2022 of 2020, will have a direct impact in fostering competition by increasing the number of bids that will be received with a positive effect on prices. It is expected that the average number of bids per public bidding process in all the sectors where standard documents are mandatory will increase from 3 in 2019 to 7.5 in 2022, equivalent to a 150 percent increase.[58] Considering the particular characteristics of the different methods of public procurement processes, it is expected to observe dispersion in the impact across such methods. For instance, a greater impact is expected in public tenders (*licitación*) than in lower and minimal amount (*menor y minima cuantía*).

Pillar II: Promoting innovation and digital finance

51. **The COVID-19 reactivation strategy presents an opportunity to leapfrog in innovation and the digital economy agenda, leading to more inclusive and productive growth**. Intangible assets such as technology, computer software, databases, licenses, and trademarks can explain productivity differences across firms (CompNet, 2020). In Colombia investment in R&D is quite low, amounting to 0.28 percent of GDP in 2019,[59] compared to 0.62 percent in the LAC region.[60] Likewise, in the same year, gross expenditure on R&D (as percentage of GDP) was the lowest among OECD countries (0.28 percent vs. 2.38 percent). Colombia lags in digitalization and ICT adoption, ranking 100th among 141 in mobile-broadband subscriptions per 100 population, an indicator of the Global Competitiveness Index 2019. Despite 98 percent of firms (with ten or more employees) having access to broadband in 2018, the quality of the connection was low[61], and its usage was unsophisticated relative to the OECD. Colombia is among the LAC region countries with the lowest level of businesses able to receive electronic payments, hindering e-commerce and business growth opportunities. More that 80 percent of small businesses do not have the equipment needed to receive or make electronic payments, despite the existence of more than 60 payments gateways in the country with technology for digital payments. Although during the pandemic

[58] To illustrate the positive effect of the use SBD on competition, the observatory of CCE has reported that in a sample of processes (1,000 activities) in 2020 SBD were used in 76.6 percent of cases resulting in 26 bids on average, compared to 4, in cases where SBD were not used. This shows the early impact of the reform. CCE will develop methodologies to evaluate the impact of the use of the SBD in other dimensions.

[59] In Colombia, firms contribute with 40 percent of total investment in STI (0.74 percent of GDP) and 43 percent of total investment in R&D (0.28 percent of GDP).

[60] The investment in R&D within LAC varies considerably by countries, so this aggregate corresponds mostly to the investment in a few countries: Brazil (1.26 percent of GDP), Argentina (0.49 percent of GDP), Uruguay (0.42 percent of GDP), Costa Rica (0.39), Chile (0.35 percent of GDP), Mexico (0.31 percent of GDP). RICTY (2020) El Estado de la Ciencia. Principales Indicadores de Ciencia y Tecnología Iberoamericanos / Interamericanos 2020.

http://www.ricyt.org/wp-content/uploads/2021/02/ElEstadoDeLaCiencia_2020.pdf

[61] Colombia has the lowest download speed in the OECD (8.8 Mbps vs. 53.9 Mbps), also below the Latin America average (11.3 Mbps), according to latest Worldwide Broadband Speed League Report (2020) of cable.co.uk and M-Lab.

digitalization has been one of the essential adaptation mechanisms for firms, increasing their survival, the percentage of firms using internet for sales, making orders or payments decreased between May 2020 and April 2021, according to the Business Pulse Survey.[62] Moreover, regulatory barriers have limited competition of new players in the digital payment system and the provision of digital financing services (e.g., crowdfunding). This, in consequence, has limited the financing access for MSMEs, most of whom do not have access to formal financing. In this context, this pillar aims at supporting the Government of Colombia promoting investment in innovation and in laying the path for the digital economy through the development of digital finance.

Prior Action #4. *The Republic of Colombia has taken measures to promote investment in innovation by regulating the use by MSMEs of tax credits for up to 50 percent for investment in research, technological development and innovation, as evidenced by Decree No. 1011, published in the Official Gazette on July 14, 2020.*

52. **Rationale.** The Government of Colombia has long recognized the role of innovation to boost productivity and the need for public policy interventions to address the market failures and barriers that lead to suboptimal levels of investment in research, development and innovation.[63] In the PND 2028-2022, Colombia has set out the ambitious target of doubling total and private investment in STI activities as share of GDP by 2022. It aims to increase total investment from 0.67 to 1.5 percent of GDP and private investment from 0.17 to 0.33 percent of GDP. Tax incentives have been generally effective to increase R&D spending, with a positive impact on productivity, job creation and export activity. Smaller firms are more responsive to tax incentives than larger firms,[64] but they tend to participate less in such programs, due to the fact that generally these incentives are based on income tax and smaller firms do not generate enough income to be taxable. Previous to the supported reform,[65] tax benefits for investment in STI[66] consisted mainly in deductions of 100 percent of the total amount invested in STI.[67] The allocation of tax benefits has increased from COP 347 billion in 2014 to COP 995 billion in 2019. Since 2016, the allocations have met the maximum amount available for deductions[68] established annually by the National Council

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[62] In May 2020, the percentages of firms using internet for sales, making orders and payments were 59, 56, and 85 percent, respectively. In April 2021, these percentages decreased to 41, 42, 72 percent. Source: Business Pulse Survey, DANE.

[63] See PND 2018-2022, PND 2014-2018, PND 2010-2014.

[64] Appelt, S., M. Bajgar, C. Criscuolo, and F. Galindo-Rueda. 2016. "R&D Tax Incentives: Evidence on Design, Incidence and Impacts." OECD Science, Technology and Industry Policy Paper 32, OECD Publishing, Paris.

[65] Colombia has been implementing fiscal benefits to promote private investment in STI since the early 1990s. Law 6/1992, Law 383/1997, Law 633/2000, law 1286/2009, Law 1450/2011, Law 1607/2012, Law 1739/2014, Law 1819/2016, Law 1955/2019.

[66] As per the new regulation (Law 1955/2019), the tax benefits for STI include: tax credits for MSMEs, deductions for donations to ICETEX and STI institutional funds and investments in research, technological development and innovation or linking of high-level human capital; discount for investments and donations made in research, technological development or innovation or hiring of high-level human capital.

[67] The existing regulation between 2011 and 2016 allowed for a 175 percent deduction of tax income. This percentage was reduced to 100 percent in 2016 (Law 1819/2016).

[68] Since 2012 (Law 1450/2011), the National Council for Tax Benefit (CNBT), defines the annual maximum total amount of tax deductions, reducing the uncertainty of the fiscal cost. At first, these caps were not actually binding. For the years 2012 and 2013, a maximum deduction amount or quota of COP 1 trillion was established by the CNBT, of which only 34 percent and 16 percent were used respectively. In 2014, the total maximum amount available for deductions was COP 500 billion and only COP 347 billion were allocated (69 percent). For 2020, the CNBT established a total deductions quota of COP 1.5 trillion.

for Tax Benefit (CNBT)[69] to minimize the uncertainty of the fiscal cost.[70] Between 2016 and 2019, the number of beneficiary firms increased from 163 to 191, a very small share of the business sector. With the intention of increasing participation of MSMEs, the CNBT established minimum quotas by firm size that resulted in mild effects.[71]

53. **Substance of the prior action.** The Government of Colombia, through Law 1955 of May 2019,[72] introduced tax credits of up to 50 percent of the investments by MSMEs in research, technological development and innovation projects, as certified by the CNBT, or of the salaries of personnel with doctorate degrees newly hired by MSMEs. These tax credits do not generate a balance in favor susceptible to refund, except when MSMEs earn tax credits in excess of one thousand tax value units (UVTs[73]). This measure allows MSMEs to use the new tax credit to offset national taxes (e.g., VAT) or to convert them into tax refund titles (*Títulos de Devolución de Impuestos*, TIDIS) to be traded in the secondary market or to pay taxes within the next calendar year. Decree 1011 of July 14, 2020,[74] established the procedure for the application of these tax credits and for obtaining the TIDIS. Following a procedure led by the CNBT and the Ministry of STI[75], firms can proceed to register the certificate on their tax filing form to offset national taxes totally or partially or may request TIDIS if meeting the aforementioned criteria. Furthermore, as per the Typology Guide of STI Projects[76], MSMEs would get additional points in the evaluation process if the project being submitted has a component related to

[69] The CNBT was created in 2009 and restructured in 2011 to include, in addition to the Director of Colciencias (STI agency, currently replaced by the Ministry of STI) and three STI experts (reduced to two experts), (i) the participation of the Ministry of Finance and Public Credit or the Director of the tax authority (DIAN), (ii) the Ministry of Commerce, and (iii) the Director of DNP.

[70] In 2017, CONPES Document 3892 mandates DIAN to present to the CNBT, by December 2022, a report of the effective use of the total maximum amount approved since 2018.

[71] Despite decreasing concentration of benefits over time, 5 firms received 31 percent of the tax benefits in 2019, with large, medium, and small companies obtaining 89 percent, 10 percent, and 1 percent, respectively. Interestingly, smaller firms tend to focus more on innovation than larger firms: 56 percent of small firms invest in innovation, 28 in scientific research and 15 percent in technological development, compared to 51, 9 and 41 percent of large firms respectively.

[72] Law of the National Development Plan 2018-2022. In this matter, it adds Article 256-1 to the Colombian Tax Statute (Decree 624/1989), Book I, Title I, Chapter X.

[73] Tax value unit (*Unidad de Valor Tributario*, UVT) is a reference unit that represents a value in pesos, which is updated annually by the DIAN according to the inflation of the year. For 2020, the tax authority (DIAN) established the value of UVT to equal $COP 35,607. Article 868 of the Colombian Tax Statute establishes the UVT, as the value measure that allows adjusting the values contained in the provisions related to taxes and obligations administered by the DIAN, which will be readjusted annually in the variation of the consumer price index for middle income as certified by the DANE.

[74] Decree 1011/2020 adds a chapter to the Sole Regulatory Decree in Tax Matters (*Decreto Único Reglamentario en Materia Tributaria*).

[75] The CNBT will issue the tax credit certificates by March 30th every year proving that MSMEs made investments in research, technological development and innovation or paid the remuneration of personnel with a doctorate degree, in accordance with the criteria and conditions previously established. On behalf of the CNBT, the Ministry of Science, Technology and Education will send the certificates to the tax authority (DIAN) by the last working day of May every year.

[76] Documento de tipología de proyectos de carácter científico, tecnológico o de innovación (page 79), versión 6. Ministry of Science, Technology and Innovation. *https://minciencias.gov.co/sites/default/files/upload/paginas/documento_de_tipologia_de_proyecto_version_6.pdf*

clean technologies therefore contributing to climate change mitigation.[77,78]

54. **Expected results.** The ability to convert tax credits into tradeable titles allows MSMEs to access existing tax benefits for STI. The measure also contributes to easing liquidity constraints faced by MSMEs, which may be especially relevant following the COVID-19 shock. It is expected that the number of MSMEs investing in STI projects leveraging tax credits will increase by 50 percent, going from 222 to 333 firms. Likewise, the yearly amount MSMEs invest in STI projects leveraging tax incentives is expected to increase by 70 percent, reaching COP 285 billion in 2022.[79] The current 2020 baseline amount of COP 168 billion invested in STI by MSMEs benefiting from the tax credit program is equivalent to 6.7 times *Colombia Productiva's* budget for that same year (25,000 million).

Prior Action #5. *The Republic of Colombia has taken measures to promote investment in green innovation by increasing the allocation of science, technology and innovation resources from the General Royalties System for projects related to the environment and sustainable development or to non-conventional renewable energies oriented to energy transition and reduction of carbon emissions, as evidenced by Articles 9-11, 22(5), 50(b) and Chapters IV and V of Title IV of Law No. 2056, published in the Official Gazette on September 30, 2020, and Decree No. 1821, published in the Official Gazette on December 31, 2020.*

55. **Rationale**. Environmentally related government R&D budget in Colombia accounted for 15.6 percent of total government R&D in 2019, notably above the OECD average (3.02 percent). Nevertheless, the low share of gross governmental expenditure in R&D has hindered the capacity to generate environmentally related innovations. In 2016, Colombia developed 0.39 environment-related inventions per capita, compared to 21.2 in the OECD. Since 2012, 10 percent of the of the investment component of the General System of Royalties (*Sistema General de Regalías*, SGR[80]) has been allocated to the STI Fund (*Fondo de Ciencia, Tecnología e Innovación*, FCTeI) [81] by Constitutional mandate, resulting in an

[77] Clean technologies are defined as: renewable energies and energy efficiency (including solar, hydro, wind, geothermal, tidal, biogas, biomass, fuel cells and others), green buildings (retrofitting for energy and water efficiency, clean transportation - alternative fuels, light rail, hybrid and electric vehicles, carpooling or carpooling systems), water management (water regeneration, wastewater treatment systems, water purification, management of rains and floods), waste management (recycling, composting, urban solid waste management, treatment and management of contaminated sites and degraded areas, sustainable packaging, use/recovery), land management (organic agriculture, habitat conservation and restoration, urban forestry and parks, reforestation, reforestation and soil stabilization, avoid deforestation, sustainable livestock), green business (biotechnology or bioproducts).

[78] Additionally, the tax benefits program has prioritized targets SDG 2.4 (sustainable food production systems and implement resilient agricultural practices) and 13 (Take urgent action to combat climate change and its impacts), among others.

[79] A previous impact evaluation of the tax incentives program, as designed by 2011, showed that participating firms increased firm productivity by 4 to 16 percent, job creation by 8 percent, and export activity by 5 percent. The Government of Colombia has commissioned a new impact evaluation of the current design and results are expected by 2022, on which baseline data and targets are based.

[80] The SGR was established in 2011, through Legislative Act 05, and started operating on January 1, 2012. With this constitutional reform to the royalty regime, it was sought that the income from the exploitation of non-renewable natural resources would contribute to regional development, competitiveness, and equity, to the reduction of poverty, to macroeconomic stability and to savings, among others. In this way, all the country's departments began to benefit from the royalties and not just the producers. The SGR is made up of five funds: the Science, Technology, and Innovation Fund (FCTeI), the Regional Development Fund (FDR); the Regional Compensation Fund (FCR); the Savings and Stabilization Fund (FAE) and the Territorial Pension Savings Fund (Fonpet).

[81] The objective of the FCTeI is to increase the scientific, technological, innovation and competitive capacity of the regions through co-financing of eligible projects. Contributions are accepted both in kind and/or in cash.

effective allocation of 9.45 percent of the total SGR funds, before discounts.[82] To improve poor execution,[83] in 2017, a new operating scheme allows allocations through public, open and competitive calls for projects.[84] Private bidders are allowed to participate as long as they are part of the National STI System and project execution is by the same project proponents. Under this new scheme, it is projected that almost COP 4 trillion will be approved in 2020-2022, compared to a total of COP 3.7 trillion over 2012-2019. The new scheme reduces the project cycle from 21 to 12 months and allows more flexibility. In 2019, the Ministry of STI organized 7 calls, and in 2020, it launched 2 express calls to address COVID-19 pandemic needs. Allocation of resources continues to be fragmented into small projects (average size of COP 7 billion) and only 34 out of 579 approved projects have had an investment greater than COP 20 billion. Despite seeking to promote regional integration, only 12 percent of FCTeI resources and 22 percent of projects have been implemented at the regional level.

56. **Substance of the prior action.** The Government of Colombia increased the allocation of royalties towards STI and unprecedentedly allocated funds for environmental research and innovation. Through Legislative Act 05 of 2019[85], Law 2056 of September 2020[86], and Decree 1821 of December 2020[87], the percentage of allocation of resources to STI was raised effectively from 9.5 percent to 10 percent, considering that the allocation is now estimated out of the total SGR funds before any deductions, while previous to this reform, the allocation was estimated after deducting 5.5 percent from the total SGR funds, as described above. This change represents an increase of COP $ 84,851 million (US$24 million) in the 2021-2022 STI allocation, a significant amount in terms of Colombia's budget allocations (equivalent to 14 times iNNpulsa's budget for 2021). With the aim of increasing execution and efficiency of the allocations, as of 2022, resources will be approved through public, open, and competitive calls at the national level, without departmental a priori distributions.[88] In addition, unprecedently, out of the 10 percent allocated to STI, at least 2 percent ought to be allocated to research or investment in STI projects related to or with impact on the environment, sustainable development or non-conventional renewable

[82] This is calculated after discounting out of total SGR funds the allocations to control the exploration and exploitation of mineral deposits and the knowledge and geological cartography of the subsoil (2 percent); to the Monitoring, Control and Evaluation System (1 percent); to the operation of the SGR (2 percent); and to municipalities of Rio Grande de la Magdalena and Canal del Dique (0.5 percent).Legislative Act No. 005 of 2011, which modified articles 360 and 361 of the Political Constitution of Colombia.

[83] As described in the Public Expenditure Review in STI carried out by the World Bank Group (2018), since the FCTeI began operations in January 2012 and until October 2018, it allocated COP 4.9 trillion. Out of this allocation, it approved STI projects for COP 2.7 trillion (55 percent) and had to transfer COP 1.4 trillion (28 percent) to OCAD Paz.

[84] Legislative Act 004, Law 1923 of 2018 and Decree 1467 of 2018. In the previous scheme, proposals were presented through the governorates (*gobernaciones*).

[85] Modifies the Article 361 of the Political Constitution of Colombia and dictates other provisions on the Royalties and Compensation Regime.

[86] It reforms Law 1530 of 2012.

[87] This constitutes the Sole Regulatory Decree for the General Royalties System (*Decreto Único Reglamentario del Sistema General de Regalías*), enacted to develop the new scheme introduced by Legislative Act 05 of 2019 and Law 2056 of 2020. This framework replaces and complements the set of regulatory provisions contemplated in the Sole Regulatory Decree of the National Planning Sector. In doing so, the Government provides legal certainty and facilitates consultation with citizens and institutions, avoiding the dispersion of regulations of the SGR, in accordance with a stronger regulatory governance and following recommendations by the OECD. In regard to the FCTeI, Decree 1821/2021 establishes the detailed regulatory framework, procedures, and technical evaluation criteria of the calls for STI projects, based on the lessons learned in 2019 and 2020 when this type of calls was introduced. It defines provisions for project execution and supervision, and the organization and functioning of the Collegiate Administration and Decision Body (OCAD) for STI. Additionally, it develops the regulatory framework for environmental innovation calls for projects with the participation of the Ministry of Environment and Sustainable Development.

[88] For the year 2021 the distribution of the entire allocation for STI will be made by department, under the allocation criteria for regional investment for the year 2021 and investment projects will be approved through public, open, and competitive calls.

energies to contribute to the energy transition and reduction of carbon emissions.[89] This percentage is expected to be higher since preliminary data on allocations made during 2021 show that some departments allocated more than 2 percent to environmental innovation (e.g., Amazonas). Also through this measure, 1 percent of total SGR funds, 20 percent of the highest collection generated with respect to the biennial royalty budget, and at least 2 percentage points of the 15 percent of total funds for the poorest municipalities are allocated to projects related to or with an impact on the environment and sustainable development, particularly for conservation and the fight against deforestation, to be invested in accordance with a national strategy for the protection of strategic environmental areas by municipalities. It is expected that a share of those funds will be invested in projects related to environmental innovation.

57. **Expected results.** The increase in royalty allocation to STI and the improvement in the implementation of the FCTeI is expected to increase STI investments of projects presented by the private sector that are associated with environmental, sustainable development and renewable energy projects by 338 percent (4.4 times), reaching COP 21,232 million, thereby facilitating climate-resilient and low-carbon investments.[90] The share of projects presented by the private sector out of all projects approved to be co-financed by the SGR under this category is expected to increase from 6 percent in 2020 to 15 percent in 2022, doubling the result achieved in the previous biennium. As of July 2021, COP 991 billion have been approved during the 2021 calls, tripling the investment resources that the Ministry of STI had allocated for this year.

***Prior Action #6.** The Republic of Colombia has enabled the development of digital finance by increasing the limits of financing through crowdfunding platforms, as evidenced by Article 12 of Decree No. 1235, published in the Official Gazette on September 14, 2020.*

58. **Rationale**. The different modalities of crowdfunding provide opportunities to access capital markets for a broad spectrum of Colombian firms including MSMEs. In recent years, the Ministry of Finance and Public Credit has promoted policies that encourage SMEs to access financing through capital markets (e.g., Decree 817/2020 allowed simplified stock companies[91] to access the capital market through the issuance of debt securities in the hybrid issuance regime —*Segundo Mercado—)*. Despite progress, the number of SMEs issuances and new issuers has not been as high as expected, mainly owing to their small size falling short of investments amounts required by institutional investors, as well as the high relative costs associated with issuing conventional securities. Additionally, micro firms are even smaller and therefore cannot consider traditional capital markets as a source of financing. It should be noted that more than 60 percent of MSMEs do not have access to financing, which is explained by self-

[89] The Ministry of Environment and Sustainable Development will work with the Ministry of Science, Technology and Innovation and DNP in the plan of call for projects, including the definition of guidelines and criteria to evaluate prospective projects.

[90] Investment in Non-Conventional Renewable Energy (NCRE) projects will reduce GHG emissions and allow for the improvement of air quality in the long-term. Also, investment in NCRE will promote power projects different from hydroelectric and thermal, such as solar photovoltaic, wind, and biomass projects, which have the capacity to produce energy in the place where it is generated and more constantly, increasing energy access to remote places and improving resilience of affected population given the dependence of hydroelectric on natural phenomena that affect energy supply, such as El Niño, and produce precipitation deficiencies and reduces the levels of reservoirs. Likewise, increased investment on reforestation projects and Reducing Emissions from Deforestation and Forest Degradation (REDD+) projects will help mitigate GHG emissions and promote biodiversity (fauna and flora) conservation and protection of natural resources, thereby contributing to both climate change mitigation and adaptation efforts.

[91] *Sociedades por acciones simplificadas,* SAS by its acronym in Spanish.

exclusion from the formal financial system, and a preference for non-financial formal sources. In particular, the self-exclusion factor is attributed in part to complicated procedures, high costs, lengthy credit decision periods and the belief that applications will be rejected, according to ANIF's SME 2019 survey (*Gran Encuesta Pyme*). Currently, the financial issuance regime for MSMEs is divided in two distanced segments. The first, established by the crowdfunding regulation, sets a maximum issuance of COP 9,000 million. The second, established by the hybrid issuance regime, at a minimum, requires issuances of at least COP 50,000 million, so that a market gap is created for firms with financing needs between these two ranges.

59. **Substance of the prior action.** Decree 1235 of September 14, 2020, seeks to address financing needs of firms that are currently neither eligible for crowdfunding nor for the SME hybrid debt issuance regime (*Segundo Mercado*).[92] The decree significantly modifies the maximum amount that a firm can raise through a crowdfunding platform (from COP 9,000 million to COP 50,000 million). So, it closes the gap between the previous maximum amount allowed by the crowdfunding regulation (COP 9,000 million) and the minimum allowed in the hybrid issuance regime (COP 50,000 million).

60. **Expected results.** The action aims to ensure that crowdfunding can become a relevant source of financing for MSMEs that do not reach the threshold required for capital markets debt issuance. The decree expands the potential use of crowdfunding as an important source of financing that would additionally support MSMEs in the post-COVID-19 economic recovery. It is expected that the volume of financing through crowdfunding platforms in Colombia will increase from COP 8,000 million in 2020, to 40,000 million in 2022.

Prior Action #7. *The Republic of Colombia has improved the regulatory framework for digital transactions by establishing requirements to increase the efficiency and transparency of the low-value payment system, as evidenced by Decree No. 1692, published in the Official Gazette on December 18, 2020.*

61. **Rationale.** In recent years Colombia has introduced several legal reforms to increase financial inclusion and promote electronic payments, including the regulation of electronic invoicing through Decree 358 of 2020. Currently, more than 96 percent of payments under US$50 are made in cash primarily because more than 80 percent of small businesses do not have the necessary equipment to receive payments by other means or to make electronic payments to their suppliers. Among Latin American countries, Colombia has one of the lowest levels of businesses able to receive electronic payments, although more than 60 payment gateways in the country have the technology for digitized payments. Additionally, fiscal barriers, such as 4x1,000 (COP) tax[93] and withholdings, create disincentives for businesses to accept electronic payments. Since 2016, the number of FinTech start-ups in payments and remittances has grown one and a half times. However, these new players in the payment system

[92] In an effort to encourage financial innovation, Decree 1234 of September 14, 2020 establishes a regulatory framework enabling financial institutions and FinTech start-ups to operate and test innovative financial products or services in a controlled space that limits the consequences of potential failures and thus maintains the soundness of the overall financial system. Following best international practices, the regulatory initiative defines the principles, requirements and stages of operation of the sandbox space, sets the duties of the participants, and establishes agile transition mechanisms to the licensing process of a regulated financial entity.

[93] The 4x1000 tax or Tax on Financial Movements (*Gravamen a los Movimientos Financieros*, GMF) refers to a national tax of COP 4 for every COP 1,000 transacted. This tax is collected by FIs and then paid to the Government, with some exceptions.

were not considered in the regulatory framework before the supported reform limiting their growth potential, which, in turn, limits competition in the industry.

62. **Substance of the prior action.** Decree 1692 of December 2020 establishes a comprehensive framework to promote a more robust digital fast payment transactions environment for low value payments with clear rules for the different actors, including peer-to-peer, peer-to-business, and business-to-business. In particular, for system administrators, it establishes rules against the abuse of a dominant position, good corporate governance practices and the prohibition of participating as acquirers within the low-value payment system, although they are allowed to provide payment services to acquirers and issuers. Also, it allows any stock company to be an acquirer provided that a series of capital requirements are met but without requiring them to establish themselves as credit institutions. The decree also establishes that low value payment systems, issuers, acquirers and receiving entities and their payment service providers cannot agree exclusivity in the provision of their services or arbitrarily block the processing and processing of payment orders or transfer of funds from other participants of the same payment system. The regulation seeks to improve interoperability, access, and security in digital transactions. It will attract more participants with higher standards, which in turn will increase competition in the industry and reduce the high use of cash in the country and increase financial inclusion[94]. Furthermore, digital payments facilitate the Government's duty of reaching out to the population in need as well as the use of public cash transfers by beneficiaries. For instance, the availability of mobile digital payments apps was key for the effective response relief of Hurricane Iota's victims last year. This was evidenced by the increase in the number of new accounts of mobile digital payments apps used by the Government to make Ingreso Solidario transfers (Movii, Ahorro a la Mano, Nequi and Daviplata)[95].

63. **Expected results.** The action creates a strong incentive to switch from cash to digital payments among the lower income segments. It will double the percentage of adults making payments or purchases online from 20 percent in 2020 to 40 percent in 2022. Furthermore, this measure may have some positive effects on climate change through reduction in carbon emissions and increase in resilience to climate-related disasters. As mentioned above, the availability of digital payments has been crucial for the Government's relief efforts by facilitating support transfers to victims of Hurricane Iota and La Niña phenomenon in 2020.

Pillar III: Fostering entrepreneurship and internationalization

64. **The Government's reactivation strategy offers an opportunity to remove barriers to high-growth entrepreneurship and internationalization, setting the economy onto a path of higher productivity and innovation**. The government entrepreneurship agenda set in the National Entrepreneurship Policy CONPES (and reflected in the national reactivation strategy and the National Development Plan 2018-2022) is oriented to generate enabling conditions in the entrepreneurial ecosystem to favor the creation, sustainability and growth of ventures that contribute to the generation of wealth, increase productivity and business internationalization. Firm level characteristics that are likely to affect productivity include internal capabilities (e.g., managerial, technical, digital), which may

[94] The fiscal barriers such as the 4x1000 continue to be in place.
[95] About 760,000 beneficiaries of *Ingreso Solidario* opened such accounts for the first time. (Banca de las Oportunidades, 2020).

constrain the propensity and ability to invest and innovate. Non-tariff measures[96], the highly dispersed structure of tariffs (particularly in agriculture), and competitiveness issues at border[97] aggravate the business productivity issues, hindering internationalization opportunities. Despite having 17 trade agreements currently in place[98], Colombia remains relatively closed to international trade.[99] According to the WDR 2020[100], Colombia falls into the group of countries that specialize in commodities Global Value Chains (GVCs), with the low level of GVC participation preventing the country from taking full advantage of the development opportunities offered by the expansion of GVCs.[101] This lack of diversification puts Colombia in a vulnerable position in the face of external shocks; the latest 71 percent fall in oil prices impacted negatively the state's public finances, posing an additional challenge to the financing of the reactivation policy. Recognizing the role of internationalization in boosting productivity and innovation, the Government of Colombia launched an Internationalization Taskforce, with the support of the World Bank. The objective of the taskforce is to make concrete recommendations to increase higher value-added exports, GVCs integration, attraction of investment flows, and international knowledge transfer. This pillar exploits the synergies between actions to foster business entry, operation and growth, and the implementation of initial recommendations made by the Internationalization Taskforce.

Prior Action #8. *The Republic of Colombia has enacted the Entrepreneurship Law to support high-growth entrepreneurship by unifying public resources and programs to support the development of the entrepreneurship ecosystem within iNNpulsa Colombia, formalizing the initiative for the creation of centers for entrepreneurship and innovation (CEmprende), facilitating financial access for high-growth enterprises, and mandating the introduction of complementary measures to strengthen entrepreneurs' export capabilities and promote MSMEs and entrepreneurship development (particularly of innovative, green and climate mitigating initiatives), as evidenced by Articles 1, 2, 5-7-9, 12, 13, 25, 30-38, 42-44, 46-48, 50-52, 55, 57, 58 and 74-83 of Law No. 2069, published in the Official Gazette on December 31, 2020.*

65. **Rationale.** Entrepreneurial activity in Colombia is high but it does not translate into sustainable business activity**.** In Colombia, 31.1 percent of the adult population is either starting or running a new business (Total early-stage Entrepreneurial Activity, TEA), while only 5.5 percent are established business

[96] In 2019 they covered almost 80 percent of tariff items.

[97] An export operation takes an average of 112 hours due to border compliance compared to 13 hours in OECD countries, and the cost to export a container (USD 630) exceeds the average for Latin America (USD 507).

[98] *https://procolombia.co/en/news/colombias-free-trade-agreements-65-countries-17-agreements-and-15-billion-buyers*

[99] Exports of goods and services represented 38.1 percent of GDP in 2019, just 3.3 percentage points higher than that registered in 1990 (CPC, 2020). Exports in goods are concentrated in commodities, with mineral fuels, lubricants and related materials representing 43 percent of total goods exports in 2020, and barely 2 percent corresponding to manufactures with high technological content.

[100] World Bank. 2020. World Development Report 2020: Trading for Development in the Age of Global Value Chains. Washington, DC: World Bank. © World Bank. https://openknowledge.worldbank.org/handle/10986/32437 License: CC BY 3.0 IGO.

[101] World Bank. 2020. World Development Report 2020: Trading for Development in the Age of Global Value Chains. Washington, DC: World Bank. doi:10.1596/978-1-4648-1457-0.

owners or managers.[102] Also, Colombian firms tend to stay small.[103] The poor dynamics of Colombian firms limit investments, innovation, and, consequently, productivity spurs. Some of the reasons behind the slow firm dynamics are the high regulatory burden (see Prior Action 1), lack of entrepreneurial, digital and innovation skills, and limited financial access (Prior Actions 6 and 7). Despite these challenges and government efforts[104], the public offer to support entrepreneurship suffers from atomization, duplication, and lack of articulation. It is spread out across 79 institutions with 497 policy instruments, and 247 instruments reporting budgets of less than COP 1,000 million.[105] The entrepreneurship and innovation agency iNNpulsa estimated that the national investment budget for entrepreneurship amounted in 2020 to COP 13.1 trillion, administered by 34 institutions across different sectors. In response, the Entrepreneurship Policy instructs the National Planning Department (DNP) and the Ministry of Commerce, through iNNpulsa, to coordinate the adjustment and articulation of the national government's offer to support entrepreneurship, including roles, competencies, and responsible actors. In July 2020, the Executive Committee of the National Competitiveness and Innovation System (SNCI) approved the creation of the Technical Entrepreneurship Committee[106] to strengthen and consolidate the entrepreneurial ecosystem, recommend actions to solve bottlenecks in the implementation of the entrepreneurship policy, and serve as the articulator of national policy with regional initiatives in entrepreneurship.

66. **Substance of the prior action.** The Entrepreneurship Law aims at improving the Colombian entrepreneurial ecosystem through strengthened institutional capacity, a more favorable regulatory and business environment, and greater access to key enablers including knowledge and technology transfer, skills (managerial, digital and innovation) and finance. Key measures include:

- *Consolidation of iNNpulsa as the national implementing agency for entrepreneurship, business innovation, and business development programs at the national level*. All national entities in the executive branch with competencies and functions in this area will transfer them to iNNpulsa. This

[102] Although it is common for the percentage of startups to be larger than that of established business, in Colombia this relation is one of the highest among the sample of 50 countries. In fact, new business creation has been constant over the last decade, while the growth rate of established businesses has been declining. Global Entrepreneurship Report (2019/2020). Authors: Bosma, N., Hill, S., Ionescu-Somers, A., Kelley, D., Levie, J., Tarnawa, A., and the Global Entrepreneurship Research Association (GERA). ***https://www.gemconsortium.org/report/gem-2019-2020-global-report***

[103] Eslava et al (2018) find that independent of size at creation, Colombian firms grow at a lower rate than US firms. Around 6 to 10 years of creation, on average, firms in Colombia have increased jobs by 10 percent, compared to 40 percent in the US. At 11 to 15 years of creation, these rates increased to 30 percent in Colombia and 80 percent in the US, and at 21 to 25 years of creation, the gap was significantly widened as average firms' employment rate in Colombia is 70 percent while it is 160 percent in the US.

[104] Fostering entrepreneurship has been one of Colombia's priorities in the last 20 years, becoming the backbone of the current National Development Plan as one of the three main pillars (*Pacto por el emprendimiento y la productividad)*. More recently, the CONPES approved the National Entrepreneurship Policy oriented to generate enabling conditions in the entrepreneurial ecosystem to favor the creation, sustainability and growth of ventures that contribute to the generation of wealth, increase productivity and business internationalization. Supporting and promoting entrepreneurship is one the main components of the national reactivation strategy from the COVID-19 crisis.

[105] Based on Articulation for Competitiveness methodology (ArCo). This methodology was developed by DNP based on the efficiency, governance and functionality analysis proposed by the Public Expenditure Reviews carried out by the World Bank in 2015 at the national level and in 2018 at the subnational level.

[106] The committee consists of public and private sectors, the presidency of iNNpulsa Colombia and the technical secretariat of DNP.

measure will increase the efficiency and effectiveness of interventions with better defined objectives and targeting, improved monitoring systems, and strategic planning and budgeting.[107]

- *Creation of centers for entrepreneurship CEmprende under iNNpulsa*, where technical and academic institutions, private companies, chambers of commerce, non-profit organizations, and national unions will interact to develop entrepreneurial activities and innovation. These centers will provide incubating and accelerating services, access to labs, financing, among other services.[108] The centers will focus on these areas: renewable energies, sustainable development, health, gender, AgriTech, EdTech, SporTech, and Fintech[109].
- *Promotion and support of green businesses.* The reform mandates the creation of programs that identify, promote, and support the creation and growth of businesses aimed to protect and preserve the environment, especially in rural areas and regions with the highest rates of poverty in the country, generally associated with greater environmental degradation.
- *Allowing the National Guarantee Fund (FNG, Fondo Nacional de Garantías) to expand its portfolio of guarantees, from operations of financial institutions, to debt securities, equity securities and* collective *investment funds (crowdfunding).* This will expand access to funding opportunities for high-growth ventures, complementing other initiatives within the recovery strategy from the COVID-19 crisis, aiming to increase access to finance related to bond emissions (Prior Action 2), crowdfunding (Prior Action 6), and digital payments (Prior Action 7).
- *Other complementary measures to promote MSMEs and entrepreneurship growth*. The Law improves the ease of doing business by mandating differentiated tariffs for health and safety registrations, strengthening the Single Business Window (complementing Prior Action 1). Also, it grants preferential conditions[110] for MSMEs in public procurement to increase MSMEs' access to markets, with particular focus on women-led and environmental and social enterprises (complementing Prior Actions 3 and 9). The law also introduces regulatory sandboxes to facilitate the development of business intensive in technology, innovation, sustainable use of natural capital and/or aimed at mitigating climate action. Finally, it mandates the Ministry of Commerce to lead interventions to strengthen export capabilities of entrepreneurs to facilitate their integration into the global markets. Additional key aspects of the law are summarized in Box 5.

[107] The measure excludes budget funds managed by the National Training Service (SENA), *Colombia Productiva* and *Fondo Mujer Emprende*, although the latter will be administered by iNNpulsa.

[108] Most importantly, these centers will provide interaction opportunities between entrepreneurs, researchers and support institutions which is considerably low in Colombia (DNP (2020) Documento CONPES 4011 Política Nacional de Emprendimiento. Bogota, Colombia). This type of interventions has proven effective to dynamize and develop productive ecosystems and improve SMEs performance. See Maas & Jones (2017) Entrepreneurship Centres: global perspectives on their contributions to higher education institutions. Palgrave. Editors; and Cirera, Xavier; Frias, Jaime; Hill, Justin; Li, Yanchao. 2020. A Practitioner's Guide to Innovation Policy: Instruments to Build Firm Capabilities and Accelerate Technological Catch-Up in Developing Countries. World Bank, Washington, DC.

[109] *https://innpulsacolombia.com/cemprende/preguntas-frecuentes*

[110] Specific criteria to be defined through regulatory decrees and resolutions

Box 5. Key measures of the Entrepreneurship Law (Law 2069 of 2020)

Improving the business and regulatory environment to facilitate the establishment and operation of companies:

- Interoperability, for all required procedures to create and operate businesses, of the Comprehensive Social Security System (*Sistema de Seguridad Social Integral*), the Family Subsidy System, and the tax authority (DIAN) with the Transactional Affiliation System *Mi Seguridad Social* and this in turn with the Single Business Window (VUE).
- INVIMA to establish differentiated service rates with lower rates for MSMEs and exemptions to microenterprises and small agricultural producers.
- Reduction of limit required to call board meetings from 25 percent of the firm's shared capital to 10 percent to increase protection of minority investors, complying with international best practice (see PA #4) and increasing the Doing Business *Extent of shareholder rights index* from 4 to 5 (6 being the maximum).

Promoting MSME development by facilitating access to public procurement and expanding their markets:

- Preferential conditions for MSMEs in processes of Minimum Amount and virtual store of the State.
- Adjustment and inclusion of new tie-breaking criteria in favor of MSMEs, women-led companies and companies incorporated as of public benefit and interest (*Sociedades de Beneficio de Interés Colectivo*, BIC). Specific criteria to be defined through regulatory decrees and resolutions.
- Creation of the Public Procurement Information System.

Facilitating access to finance for entrepreneurs:

- Modification of the corporate purpose of the FNG to expand its product portfolio and offer guarantees to other sources of financing.
- Financial inclusion of microenterprises through microcredits.
- Tax incentive to promote donations to the ecosystem through iNNpulsa.

Strengthening the institutional framework for the development of the entrepreneurial ecosystem:

- Unification of public sources of financing for entrepreneurship and business development into iNNpulsa.
- Articulation of entrepreneurship and MSMEs institutions within the SNCI.
- Formulation of activities implemented by iNNpulsa, including those to promote productivity and business development.
- Creates ICETEX fund to benefit entrepreneurs who have obtained educational credits with them.

Entrepreneurship education and skills development:

- Entrepreneurship training in basic, secondary, and middle education.
- Teacher training programs on entrepreneurship and business development for basic and intermediate levels.
- SENA programs to promote an entrepreneurial mindset in financial, legal and market access issues.
- Inclusion of entrepreneurship and innovation projects as a degree option in higher education.
- Creation of free advisory services (*consultorios empresariales*) to entrepreneurs provided by undergraduate students of Economics, Finance, Accounting, Business Administration, Law, Design, Engineering, etc.

Source: Law 2069 of December 2020.

67. **Expected results.** The Entrepreneurship Law establishes a regulatory framework to consolidate the entrepreneurial ecosystem in Colombia. It reduces regulatory burdens for entrepreneurs; expands access to market opportunities through public procurement; promotes diversification and expansion of financing schemes across the entrepreneurship cycle; supports the generation of entrepreneurial skills; and strengthens the institutional framework for higher efficiency and effectiveness of public support for entrepreneurship around iNNpulsa. The overall aim is to strengthen and accelerate ventures, positively impacting their sales, employment, and productivity. Thus, the law is expected to favor the creation and growth of dynamic enterprises, defined as those exhibiting at least 9 percent increase on sales or employment per year or at least 5 percent of profits per year; reflected in a rise from 1,795 dynamic enterprises supported by iNNpulsa's acceleration programs in 2020 to 3,000 in 2022 (a 133 percent

increase).[111] This indicator and target are part of the National Development Plan 2018-2022. Also, the number of equivalent dynamic enterprises led by women is expected to double, going from 39 dynamic enterprises in 2020 to 80 enterprises in 2022. Note, however, that this target does not consider the female entrepreneurship programs being created as per Prior Action 9. Finally, since this measure promotes green business that favor the protection and preservation of the environment, the CEmprende centers are focused on renewable energies and sustainable development, and it introduces regulatory sandboxes to further the development of business intensive in sustainable use of natural capital or aimed at mitigating climate action, it will also contribute to climate change adaptation and mitigation.

Prior Action #9. *The Republic of Colombia has approved a regulatory framework to further female entrepreneurship by creating and consolidating the autonomous trust fund Fondo Mujer Emprende to provide differentiated technical and financial support to women entrepreneurs and establishing incentives for the creation, formalization and strengthening of MSMEs led by women, as evidenced by Legislative Decree No. 810, published in the Official Gazette on June 4, 2020; Article 47 of Law No. 2069, published in the Official Gazette on December 31, 2020; and Law No. 2125, published in the Official Gazette on August 4, 2021.*

68. **Rationale**. Women are less likely than men to be entrepreneurs and to own or lead businesses. They also have lower access to finance, assets and skills (see Box 6). An effective and inclusive entrepreneurship policy needs to incorporate targeted support to female entrepreneurs. This is of particular relevance in the recovery strategy considering that women were more affected than men by the COVID-19 pandemic.[112] The Government of Colombia has recently adopted this view. Under the leadership of the Vice Presidency of the Republic and the Presidential Advisor for the Equality of Women (*Consejería para la Equidad de la Mujer*, CPEM), it has formulated a strategy of female empowerment through entrepreneurship. The strategy is made up of three pillars: (i) generation of information on female entrepreneurship; (ii) promoting access to financing, support, and business strengthening and empowerment for women entrepreneurs; and (iii) articulation of the institutional offer and creation of customized programs. Furthermore, the support for female entrepreneurship is integrated within the National Entrepreneurship Policy recently approved by CONPES, which mandates CPEM to implement a strategy that provides comprehensive technical assistance for the creation of sustainable business models and the productive development of women.

[111] Unfortunately, there is not available data to have this measure as a share of the target population. For context, as of 2019, the main acceleration program run by iNNpulsa (Aldea) had enrolled 600 enterprises, out of which 180 were accelerated and achieved at least 9 percent annual growth.

[112] See for instance: (i) Cucagna, Emilia; Romero, Javier (2021) The Gendered Impacts of COVID-19 on Labor Markets in Latin America and the Caribbean. World Bank, Washington, DC. © World Bank. *https://openknowledge.worldbank.org/handle/10986/35191*; (ii) Cuesta, Jose; Pico, Julieth. 2020. COVID-19 Affects Everyone but Not Equally: The Gendered Poverty Effects of the COVID-19 Pandemic in Colombia. World Bank, Washington, DC. © World Bank. *https://openknowledge.worldbank.org/handle/10986/34315*.

Box 6. Female entrepreneurship in Colombia.

Women are less likely to be entrepreneurs than men and tend to be driven by necessity. In Colombia, the female to male entrepreneurship rate ratio is 0.88, with an entrepreneurial activity rate for females at 20.9 percent, compared to 23.8 percent for males. This gap is even marked for entrepreneurship due to necessity, for which the ratio of female to male entrepreneurship rate is 0.9 (vs. 0.81 in entrepreneurship motivated by wealth creation) as per the GEM 2019-2020. The larger share of female entrepreneurship is out of necessity, a consequence of the lack of job opportunities for women and the prominent gender gap in the labor market.

Female entrepreneurs have lower access to finance, assets and skills. Although the ease to start a business perception seems to be equally favorable for women and men (ratio equal to 1), only 38.1 percent of women perceive starting a new business is a good career, compared to 78.9 percent of men (GEM 2018-2019). While 7.5 percent of men entrepreneurs have access to investment, only 3.1 percent of women entrepreneurs do. Women are also less likely to have access to financial institutions. Other constraining factors include female gaps in formal education, management skills, and socio-emotional skills. Women tend to have lower self-perception of their skills and capabilities. Furthermore, training and business development programs do not adequately target women's needs and interests and have limited awareness of the constraints faced by female entrepreneurs and their specific needs (e.g., childcare). All these constraining factors also limit participation of women-led businesses in public procurement (International Trade Centre, 2020; Value for Women and the Open Contracting Partnership, 2020).

Women also face legal and regulatory barriers and constraining cultural and social norms. Globally, over 2.7 billion women are legally restricted from having the same choice of jobs as men. In Colombia, women cannot work by law in industrial paint construction jobs, in underground workings of mines or in jobs that require substantial physical exertion (Labor Code, Article 242). Additionally, social norms exert a strong influence over the choices of female entrepreneurs and constrain their ability to grow their businesses.

The impact of the pandemic on businesses has been felt disproportionately by female entrepreneurs, given the sectoral composition of women entrepreneurship, their demanding domestic duties, and their restrictive access to resources to address the crisis. First, the shock has hit hardest sectors where Colombian women entrepreneurs are relatively more represented –commerce and health, education, and social services. Second, women-led businesses are often at a disadvantage in specific factors or resources that are key for survival and recovery (finance, technology, and networks). Third, the burden of additional domestic responsibilities exacerbates the effect of the shock on women-led businesses' productivity. Globally, 31 percent of female business leaders spend more time on domestic tasks relative to pre-pandemic levels (vs. 26 percent of male business leaders), as per The Future of Business Survey (Facebook/OECD/World Bank (2020).

Closing gender gaps in entrepreneurship, to take full advantage of women's capacity and skills, will make an essential contribution to poverty reduction, job creation, growth, and innovation. The 'misallocation of talent' across firms can have implications for economic growth at the macroeconomic level (Hsieh, C. T., Hurst, E., Jones, C. I., & Klenow, P. J., 2019).

69. **Substance of the prior action.** To implement the female entrepreneurship strategy and in response to COVID-19, in June 2020, the Government through Legislative Decree 810/2020, created an autonomous trust fund (*patrimonio autónomo*) to support entrepreneurship, formalization and empowerment of women. The Entrepreneurship Law has advanced these efforts by integrating the trust fund *Fondo Mujer Emprende* (as denominated by this law) into the current entrepreneurship institutional framework with a permanent mandate.[113] The *Fondo Mujer Emprende*, that will be administered by iNNpulsa, will design and execute plans, programs, initiatives and policy instruments to promote, support and finance entrepreneurship, formalization and business development of women.[114] The policy

[113] It was created as an emergency measure to counteract the relatively larger negative effect of the COVID-19 crisis on women and outside the institutional entrepreneurship framework.

[114] Current initiatives include a training program with EAM University, technology workshops with IBM, digital marketing training and empowerment with Facebook, Women Mentoring Network, and regional productive projects. The Fund will concentrate these and new initiatives, including financing and tailor-made technical assistance for women entrepreneurs.

guidelines will continue to be dictated by the offices of the Vice Presidency of the Republic and CPEM. The Law also authorizes annual allocations to the fund from the national general budget (*Presupuesto General de la Nación*, PGN), according to the Medium-Term Spending Framework and fiscal availability, guaranteeing continuity of initiatives. To start, the Fund received COP 20 billion from the PGN 2021 allocations. Subject to demonstrated execution capacity, the Fund could receive additional resources from public and private sources. Complementing these efforts[115], the GoC enacted the Female SMEs Law (Law 2125 of 2021) that introduces (i) a women entrepreneurship branding certificate (*Signo Distintivo*) to promote formalization and strengthening of MSMEs led by women in vulnerable situations as defined by the law[116]; (ii) credit risk ratings systems that incorporate a gender lens by Bancoldex, Finagro, FNA, Banco Agrario and other public financial institutions[117]; (iii) microcredit programs for microenterprises led by women to be offered under the leadership of the Ministry of Commerce with 90 percent guarantees from FNG; (iv) a formalization program that comprises a discount business registration rate and credit access stimulus including use of movable collateral and a special interest rate for new female led MSMEs benefiting from the branding certificate; and (v) quarterly statistical bulletins by the National Statistics Office (DANE) with information on female business participation; among other promoting initiatives.

70. **Expected results**. With the consolidation of *Fondo Mujer Emprende,* the preferential criteria for women led MSMEs in public procurement[118] and other formalization and business development incentives, it is expected that the number of female-led enterprises benefitting from technical assistance and co-financing government programs will increase from 2,230 in 2020 to 10,073 in 2022,[119] an increase of 352 percent (almost five times the number of female MSMEs served in 2020). Additionally, as data becomes available, the operation will monitor expected increases in the average of women-led MSMEs bidders per tender and/or in the number of awarded contracts to women-led MSMEs.

Prior Action #10. *The Republic of Colombia has adopted measures aimed at reducing the cost and time for firms to trade and facilitate their integration in global value chains through the extension of the Authorized Economic Operator Program (AEO) to operators of port installations, as evidenced by Resolution No. 48 dated May 15, 2020, published in the Official Gazette on November 4, 2020.*

71. **Rationale**. Firms that both import and export dominate GVC participation. In Colombia, these

[115] The Entrepreneurship Law also mandates the definition of differentiated and preferential criteria in public procurement for MSMEs led by women.

[116] The branding certificate will be provided by the Superintendence of Industry and Commerce upon fulfillment of established requirements and in accordance with Decision 486 of the Andean Community. Potential beneficiaries include women recognized victims of conflict, with disabilities, Female caregivers of disabled people with care dependency, accredited community mothers, survivors of attacks with chemical, acid or similar substances, reincorporated ex-combatants, rural and peasant women, current entrepreneurs affected by the COVID-19 pandemic, beneficiaries of *Familias and Acción* program, mothers, daughters and wives or permanent companions of members of the Military Forces or National Police deceased in services, women in prison or that served time in prison, women residents of the municipalities participating in Development Programs with a Territorial Focus (*Programas de Desarrollo con Enfoque Territorial*, PDET), women participating in illicit crop substitution programs, women belonging to indigenous, black, Afro-Colombian, Palenqueras and Raizales communities, informal vendors who have performed this work during the five years prior to the enactment of this law.

[117] The law provides a one-year deadline for the design of such mechanisms.

[118] As per the Entrepreneurship Law.

[119] It includes firms led by women benefiting from current programs by iNNpulsa (Aldea and Empodera) and SENA (creation and strengthening). This is the only available data considering that this law mandates DNP and iNNpulsa to create a set of indicators to measure its impact.

firms represent 80 percent of total trade value and 15 percent of the total number of trading firms (World Bank, 2020). Border management and trade facilitation measures become increasingly critical as firms upgrade in GVCs towards complex manufactures that imply frequent and just-in-time import and export transactions.[120] Colombia's low score in the 2020 Doing Business Trading Across Borders (TAB) indicator, below the LAC and OECD averages, suggests significant performance gaps in terms of border compliance costs and time.[121] Likewise, even though Colombia performs better than the average for the region in terms of compliance with the Trade Facilitation Agreement, the related OECD indicator reveals performance gaps relative to OECD countries in terms of internal and external border agency co-operation, procedures and documents.[122] Accordingly, the Government of Colombia has launched initiatives aiming at transforming the way borders are managed to balance border controls with trade facilitation, through the deployment of ICT, business processes reengineering and automation, simplification of documentary requirements and data harmonization, and use of innovations and new technologies (e.g. non-intrusive inspections equipment, tracking and tracing solutions, etc.). The improvement of risk management capacities, underpinned by comprehensive compliance strategies that complement border inspections with controls beyond the borders, can limit the shipments submitted to inspections and hence reduce overall clearance times and costs. The Government of Colombia has initiated an Integrated Risk Management System project to enhance capacity and improve coordination of Customs and other border control agencies.[123] Expanded usage of prior-arrival processing and release has the potential to reduce the gap in performance between Colombia and OECD countries.

72. **Substance of the prior action**. The Government of Colombia is adopting important measures to reduce costs and time to trade by extending the Authorized Economic Operator (AEO) Program[124] to players along the transport and logistics chain. Through Resolution 48 of 2020, the government expanded the AEO program to port installations while it is currently preparing the expansion for road freight transport, bonded warehouses, and free zones operators. Before the supported reform, the AEO Program provided benefits that included lower border control clearance time and higher predictability to exporters[125], importers[126], and customs brokers[127] that were compliant with a list of security, tax, and customs requirements ("trusted operators"). In 2020, 229 firms representing 20 percent of Colombia's import value and 10 percent of export value (18 percent of non-oil export value) were certified as

[120] Delays in border control processes force firms to adopt costly hedging strategies and complicates their ability to engage in just-in-time production or react quickly to demand shifts. Evidence suggests that inventory-holding costs can vary from 15 percent of the cost of goods per year to as much as 50 percent (Clark et al., 2016). Similarly, each day in transit is equivalent to an ad-valorem tariff ranging between 0.6 percent and 2.3 percent; and trade in components is extremely time-sensitive (Hummels and Schauer, 2013). Customs delays also reduce exports value and export market diversification (Volpe Martincus et al., 2015). Import delays uncertainty affects survival rates for new exporters, especially for firms from developing countries exporting to high-income markets (Vijil et al., 2019).

[121] Designed as a proxy for national performance, TAB is an imperfect measure for countries that have multiple systems operational in different ports and regions like Colombia, but it is broadly illustrative of general performance and can identify particular areas for potential improvement.

[122] The World Trade Organization (WTO) TFA sets multilateral rules that seek to address specific procedural hurdles in order to facilitate trade procedures. The TFA was ratified by Colombia on August 6, 2020 and represents a significant opportunity to reap the economic benefits from improving the speed and efficiency of border procedures.

[123] The Ministry of Commerce, Industry and Tourism is currently negotiating Memorandum of Understanding between DIAN, INVIMA and ICA to enable automatic exchange of data for risk management purposes.

[124] Created by Decree 3568 of 2011, modified by Decree 1894 of 2015 and the DIAN resolutions.

[125] Resolution 15 of 2016 by DIAN.

[126] Resolution 67 of 2016 by DIAN.

[127] Resolution 4089 of 2018 by DIAN

"trusted operators" by the AEO Program. However, firms participating in GVCs still had a minor participation, representing only 12 percent of the trade value of the firms that both import and export (excluding oil trade). As of November 19, 2020, the AEO Program was extended to port installations and operators upon compliance with safety and security measures, through Resolution 48 of May 15, 2020.[128] This measure will lower logistics costs due to reduced movement of cargo within port terminals, mitigate risks of illicit interventions or tampering of cargo and reduce burdensome inspections on exports through the ports, particularly by the Antinarcotics Police.[129] The reform supported by this operation expands the benefits granted by the AEO Program in line with best international practices.[130]

73. **Expected results**. The proposed reform is expected to reduce the time and costs to move cargo within port terminals and reduce burdensome inspections on trade through the ports, benefiting firms participating in GVCs that both export and import. The GVC-related trade value covered by the AEO Program (trade value of AEO certified firms that both import and export over the total trade value of firms that both import and export) is expected to increase by 2 percentage points, from 12 percent in 2020 to 14 percent in 2022[131]. Also, the proposed reform is expected to reduce the time and cost to trade across borders. The import time release is expected to be reduced from 150.1 hours in 2019 to 123.8 hours in 2022. Furthermore, the AEO Program supports better risk management and resource allocation to the enforcement agenda, including the one related to environmental control (particularly, fauna and flora), dual usage of goods, security, etc. The Program also encourages participant companies to adopt related preventive measures and internal controls.

[128] The Resolution 48 of May 15, 2020 entered into effect fifteen calendar days after its publication on November 4, 2020.

[129] In the Colombia context this is a sensitive issue due to the traffic of drugs.

[130] The reform is in line with the World Customs Organization Framework of Standards to Secure and Facilitate Global Trade (SAFE) and with article 7.7 on Trade Facilitation Measures for Authorized Operators of the WTO TFA.

[131] The indicator excludes oil exports and imports (Chapter 27 of the harmonized system code). Imports' value includes costs, insurance, and freight (CIF) and exports value are free on board (FOB).

Table 4: DPF Prior Actions and Analytical Underpinnings

Prior Actions	Analytical Underpinnings
Pillar I--- Improving the regulatory environment for private sector led recovery	
Prior Action #1. Better regulation	• World Bank (2020). *Productivity in Colombia* (P603466). • World Bank (2020). *Colombia - Programmatic Approach for Productivity and Reactivation* (P165596) • Consejo Privado de Competitividad (2020). *Informe Nacional de Competitividad 2020-2021*. • World Bank (2018). *Colombia Policy Notes*. • OECD (2018). *OECD Regulatory Policy Outlook 2018*, OECD Publishing, Paris • OECD (2014). *OECD Regulatory Compliance Cost Assessment Guidance*. • DNP (2014). *Mejora Normativa: Análisis de Impacto*. CONPES 3816. Inappropriate regulations can hinder enterprise operation, productivity, competition, and international integration. A high-quality and frequent assessment of compliance costs can contribute to creating a more favorable business environment. The regulatory agenda established in CONPES 3816 sets Colombia on the path to better regulatory practices. Going forward, improvements are needed in the effective and frequent implementation of Regulatory Impact Assessments (RIA), ex-post evaluation of regulations, and centralized public consultation.
Prior Action #2. Green finance	• World Bank (2021). *Colombia Country Private Sector Diagnostic*. • World Bank (2020). *Greening the Financial System in Colombia* (P171408). • World Bank (2020). *Colombia Capital Markets Strengthening Facility* (P167816). • World Bank (2019). Financial Sector. *Colombia Policy Note.* • Asobancaria (2019). *Caracterización del Mercado de Capitales Colombiano: Una perspectiva integral.* Well-developed capital markets are relevant to channel savings into financing, generate value-added, and transfer risk among the different agents in the economy. Colombia is highly vulnerable to climate change, which can translate into financial risks (physical and transitional). Green finance presents opportunities to deepen the financial sector and contribute to climate mitigation and adaptation.

<table>
<tr><th>Prior Actions</th><th>Analytical Underpinnings</th></tr>
<tr><td>Prior Action #3. Competition and transparency in public procurement</td><td>

World Bank (2021). Colombia Country Private Sector Diagnostic.
World Bank (2020). Case Study 6: Open Contracting Reforms in Colombia. Enhancing Government Effectiveness and Transparency: The Fight Against Corruption.
Contracting Observatory of the Colombian Chamber of Infrastructure (2020). Report on the performance of the implementation of Standard Bidding Documents in roads infrastructure from April 1, 2019 to August 31, 2019.
Deloitte & European Commission (2020). Study on up-take of emerging technologies in public procurement. Final Report.
Colombia Compra Eficiente [with the World Bank as member of the Technical Advisory Group] (2020). Evaluación del Sistema de Compras y Contrataciones Públicas de Colombia – Metodología MAPS.
World Bank (2016). 2015 Colombia Public Expenditure and Financial Accountability (PEFA) - Colombia's Public Financial Management Systems.
OECD (2016). Towards Efficient Public Procurement in Colombia: Making the Difference, OECD Public Governance Reviews, OECD Publishing, Paris

Public procurement is critical to delivering services to citizens. Colombia has shown improvements in procurement data availability and the establishment of an anti-corruption agency to monitor public procurement. However, historically there have been concerns about transparency, non-competitive methods, and conflicts of interest. The development of open contracting and the standardization of biding documents are essential to enhance competitiveness, transparency, and public procurement efficiency. Also, digital tools are useful to detect anomalies in public procurement procedures as well to foster transparency and efficiency.
</td></tr>
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Prior Actions	Analytical Underpinnings
Pillar II--- Promoting innovation and digital finance	
Prior Action #4. Innovation tax credits for MSMEs	• World Bank (2021). *Colombia Country Private Sector Diagnostic*. • World Bank (2020). *Productivity in Colombia* (P606466). • DNP (2020). *Política Nacional de Ciencia, Tecnología e Innovación 2021-2030*. Borrador. • Consejo Privado de Competitividad (2020). *Informe Nacional de Competitividad 2020-2021*. • World Bank (2017). *Colombia Innovation and Competitiveness* (P144510). • Crespi, G., Garone, L. F., Maffioli, A., & Melendez, M. (2015). *Long-term productivity effects of public support to innovation in Colombia.* Emerging Markets Finance and Trade, 51(1), 48-64. • Arbeláez, M. A., & Parra Torrado, M. (2011*). Innovation, R&D investment and productivity in Colombian Firms* (Working Paper IDB-WP-251). Washington: Banco Interamericano de Desarrollo. Investment in public and private innovation is critical to foster productivity in Colombia, mainly through product diversification. Despite the overall increase in R&D and STI activities over the last decade, innovation continues to be low. There are several factors constraining innovation (e.g., insufficient development of scientific vocations and human capital, low transference of science and technology to the productive sector, and unfavorable conditions and abilities to innovate within firms), and most of them rely on the lack of incentives and resources to develop innovation activities that effectively support the private sector activity. Aligned efforts in the public and private sector are critical to enhancing innovation and productivity, mainly through diversification of the mechanisms and sectors of government investment in STI, promotion of private investment (via financing or new benefits), and technology implementation in the private sector.
Prior Action #5. Green innovation through the SGR	• World Bank (2021). *Colombia Country Private Sector Diagnostic*. • Martínez, C. I. P., & Poveda, A. C. (2021). *The Importance of Science, Technology and* Innovation *in the Green Growth and Sustainable Development Goals of Colombia*. Environmental and Climate Technologies, 25(1), 29. • World Bank (2020). *Productivity in Colombia* (P606466). • DNP (2018). *Política de Crecimiento Verde*. CONPES 3934. • World Bank (2017). *Colombia Innovation and Competitiveness* (P144510). • OECD (2017). *Investing in Climate, Investing in Growth*, OECD Publishing, Paris • OECD (2017). *Green Growth Indicators 2017*, OECD Publishing, Paris • World Bank (2016). *Public Expenditure Review in Colombia.* Productivity gains from innovation amplify when innovation activities and research are focused on environmental issues. Green innovation can help achieve environmental objectives at lower costs and lead to new business opportunities and markets. At the department level, higher research activities in environment-related topics have an inverse relationship with deforestation. Moreover, climate change mitigation and adaptation actions bring growth and productivity gains as they help set a more favorable and certain environment for business activity.

Prior Actions	Analytical Underpinnings
Prior Action #6. Crowdfunding	• World Bank (2021). *Colombia Country Private Sector Diagnostic*. • World Bank (2020). *Colombia Capital Markets Strengthening Facility* (P167816). • OECD (2019). *OECD Reviews of Digital Transformation: Going Digital in Colombia*, OECD Publishing, Paris. • Eldridge, D., Nisar, T. M., & Torchia, M. (2019). *What impact does equity crowdfunding have on SME innovation and growth? An empirical study.* Small Business Economics, 1-16. • URF, Ministerio de Hacienda y Crédito Público. (2016). *Alternativas de regulación del crowdfunding.* • World Bank, infoDev. (2013). *Crowdfunding's Potential for the Developing World*. Digital finance increases the availability of financing platforms. It facilitates access to financial services for consumers and MSMEs, thus increasing competition in a highly concentrated capital market. The Fintech sector in Colombia has been very dynamic lately, notably in the crowdfunding sector. Considering the limited MSME's financial access, the crowdfunding industry provides an alternative opportunity for MSMEs to raise funds. In fact, crowdfunding has a positive and strong correlation with the growth opportunity of small firms. A credible and supportive crowdfunding ecosystem depends on a regulatory framework that leverages transparency and speed and reaches early-stage businesses.
Prior Action #7. Digital payments	• World Bank (2021). *Colombia Country Private Sector Diagnostic*. • Agur, I., Peria, S. M., & Rochon, C. (2020). *Digital financial services and the pandemic: Opportunities and risks for emerging and developing economies*. International Monetary Fund Special Series on COVID-19, Transactions, 1, 2-1. • Yin, Z., Gong, X., Guo, P., & Wu, T. (2019). *What drives entrepreneurship in digital economy? Evidence from China*. Economic Modelling, 82, 66-73. • Seethamraju, R., & Diatha, K. S. (2018). *Adoption of Digital Payments by Small Retail Stores*. Unpublished manuscript. • Arango-Arango, C. A., Zárate-Solano, H. M., Suárez-Ariza, N. F., & Arango-Arango, C. A. (2017). *Determinantes del acceso, uso y aceptación de pagos electrónicos en Colombia*. Borradores de Economía; No. 999. • World Bank Group, Bank for International Settlements. (2016). *Payment aspects of financial inclusion.* The legal and regulatory framework development play a critical role in creating an enabling environment for inclusive payment services. In fact, the lack of trust in the regulatory environment and bureaucracy seems to hamper the adoption of digital payments in small retail businesses and first-time users. Widespread use of digital payments (e.g., mobile payments) promotes entrepreneurship, and businesses' adoption of this type of payment services facilitates consumer's adoption, making a virtuous circle for financial inclusion. Moreover, in the pandemic context, digital payments are critical to maintaining commercial transactions while allowing social distancing.

Prior Actions	Analytical Underpinnings
Pillar III--- Fostering entrepreneurship and internationalization	
Prior Action #8. Entrepreneurship and business growth	• World Bank (2021). *Colombia Country Private Sector Diagnostic* • World Bank (2020). *Colombia - Programmatic Approach for Productivity and Reactivation* (P165596) • DNP (2020). *Política Nacional del Emprendimiento*. CONPES 4011. • Consejo Privado de Competitividad (2020). *Informe Nacional de Competitividad 2020-2021*. • GEM (2020). *Global Entrepreneurship Monitor 2019/2020 Global Report.* • World Bank (2020). *Colombia Country Private Sector Diagnostic.* • OECD (2020), *Financing SMEs and Entrepreneurs: An OECD Scoreboard*, OECD Publishing, Paris. • OECD (2018). *SMEs in Public Procurement: Practices and Strategies for Shared Benefits*, OECD Public Governance Reviews, OECD Publishing, Paris. Although Colombia has high rates of early entrepreneurship, the main motivation is the lack of opportunities in formal and well-paid job. Key obstacles for entrepreneurship and business growth include burdensome and expensive regulatory procedures, lack of finance for new entrepreneurs, and limited entrepreneurial culture and abilities. In particular, difficulties in access funding impose barriers for early entrepreneurs to boost growth and productivity in their businesses. Although credit interest rates for SMEs seemed to be favorable before the pandemic, new SME credit flows had a declining trend. Other opportunities and facilities, like participation in public procurement and less regulatory costs, are relevant to fostering access to markets and strengthening business capacities.
Prior Action #9. Female entrepreneurship	• World Bank (2021). *Colombia Country Private Sector Diagnostic*. • Panda, S. (2018*). Constraints faced by women entrepreneurs in developing countries: review and ranking*. Gender in Management, Vol. 33 No. 4, pp. 315-331. *https://doi.org/10.1108/GM-01-2017-0003* • OECD, European Commission. (2016). *Policy Brief on Women's Entrepreneurship.* • Valdivia, M. (2015). *Business training plus for female entrepreneurship? Short and medium-term experimental evidence from Peru*. Journal of Development Economics, 113, 33-51. • Weber, O., & Ahmad, A. (2014). *Empowerment through microfinance: The relation between loan cycle and level of empowerment.* World development, 62, 75-87. • Inter-American Development Bank, World Bank. (2014). *Entrepreneurship in Latin America: A STEP UP THE SOCIAL LADDER?* Constraints for female entrepreneurship include lower access to finance, assets, skills, and networks. Women in developing countries face continually marked restrictions on financial access because of the lack of credit history, high collateral requirements, higher risk aversion, distrust towards women entrepreneurs by bankers, etc. Moreover, the lack of networks and training programs hinder their ability to achieve high-growth entrepreneurship. Strategies to i) facilitate financial access (especially for those in their first loan cycle or without collaterals), ii) provide training programs accompanied by technical assistance, and iii) foster networks and mentoring contribute to empower female entrepreneurship.

Prior Actions	Analytical Underpinnings
Prior Action #10. Trade facilitation	• World Bank (2020). *Colombia Trade Engagement* (P174297). • Consejo Privado de Competitividad (2020). *Informe Nacional de Competitividad 2020-2021*. • Banco de la Republica (2019). *Comercio exterior en Colombia: Política, instituciones, costos y resultados.* • World Bank (2017). *Regulatory Business Environment in Colombia* (P158863). Trade contributes little to Colombia's economic growth, and its participation in international trade is restricted, given its limited openness, export concentration in commodities, and low insertion in GVC. A high concentration in commodities makes Colombia vulnerable to international shocks, which could threaten other positive advancements in trade competitiveness. Although Colombia participates in numerous trade agreements and has made tariff liberalization efforts, it remains closed to trade mainly due to non-tariff measures. The protection of domestic production, the scarcity of quality infrastructure, and the high logistic costs (e.g., time in borders operations) have hindered Colombian trade. Although costs nonrelated to protection (i.e., logistic, regulatory, and transport costs) have declined over the last half-century, they still account for 37 percent of the exporter's gross income. In fact, Colombia continues to have a weak performance on the WB's LPI (Logistic Performance Index), dragged by the customs dimension performance.

4.3. LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY

74. **The proposed operation is aligned with the Country Partnership Framework (CPF) 2016-2021** for Colombia[132] and the Performance and Learning Review (April 23, 2019). The proposed DPF is aligned with Pillar 3 Supporting Fiscal Sustainability and Productivity through two of its four objectives. It supports Objective 6, Improving the Business Environment and Innovation to Boost Productivity, particularly by supporting the government's regulatory simplification agenda, contributing to national competition policy and to international trade integration. Also, some of the reforms related to innovation derive from the implementation of the revised public innovation programs currently used in the formulation of the 2021-2030 innovation policy. Additionally, the proposed DPF supports Objective 7, *Deepened Financial Intermediation for Productive Purposes*, by improving financial infrastructure to increase firm's access to finance and capital markets.

75. **To support Colombia in its response to the COVID-19 crisis and promote a sustainable and robust recovery, the WBG is adjusting its financing and knowledge support flexibly, using the existing Country Partnership Framework (CPF) 2016-2021[133] as a starting point, and in line with the WBG COVID-19 Crisis Response Approach Paper (WBG AP).** The World Bank has been implementing key adjustments to its strategy and program in response to Colombia's rapidly evolving development priorities and financing needs due to the impact of COVID-19, including the inclusion of the proposed Competitiveness and Recovery DPF in support of the government's recovery strategy[134]. Due to the significant impact of the COVID-19 crisis in Colombia and its extended duration, an SCD Update is planned for FY22 when a meaningful assessment of the impact of the crisis and medium-term priorities is expected to be possible, followed by a new CPF, now planned for FY23 when a new government takes office.[135]

76. **The proposed DPF will contribute to the achievement of the twin goals of eliminating extreme poverty and boosting shared prosperity in a sustainable manner**. The proposed operation aims at increasing innovation, productivity, competitiveness, and international integration of the private sector to be reflected in higher economic growth and job creation in higher value-added activities, with positive effects on poverty. Promoting the digital economy through digital finance will also contribute to more inclusive and productive economic growth. Also, the proposed operation will contribute to shared prosperity as it focuses on supporting MSMEs to achieve higher impact and generate better jobs. Likewise, the focus on women-led enterprises will support closing the gender gap.

77. **The proposed operation is also aligned with the long-standing support of the World Bank Group in efforts to promote productivity, better business regulation, innovation, digitalization, deepening of**

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[132] http://documentos.bancomundial.org/curated/es/940691468184792587/pdf/101552-CPF-P155964-R2016-0053-IFC-R2016-0054-MIGA-R2016-0014-Box394872B-OUO-9.pdf

[133] Report No. 101552-CO, discussed by the Board of Executive Directors on April 7, 2016.

[134] The adjustments include additional support in the health sector (both advice and financing) to protect the poor and vulnerable (targeted transfers, reform of the social registries, resilient and inclusive support, increased support for migrants and host communities), and to build resilient and sustainable infrastructure for medium-term growth while maintaining robust macroeconomic policies and fiscal sustainability. The Bank is also supporting Colombia's medium-term structural and institutional reform agenda in internationalization, employment, and improved targeting of subsidies and benefits.

[135] National elections will take place on May 22, 2022 (first round) and on June 19, 2022 (second round if in the first round none of the candidates obtain half plus one of the total valid votes.

capital markets, and international competitiveness to foster growth and better jobs. For instance, through the Colombia Programmatic Approach (P165596) the World Bank has been providing technical assistance to the Government of Colombia in improving the investment environment and strengthening government capabilities at the national and subnational levels, as well as enabling the digital transformation, increasing innovation and improving capabilities at the firm level. Similarly, in a World Bank-IFC joint effort (Colombia Productivity, ID: 603466), the WBG has provided technical support in the design and implementation of the Regulatory Governance System and in improving the effectiveness of public investment in STI and leveraging it to support private sector driven growth. Also, it has provided technical advice to the design and implementation of a program that aims at improving practices of SMEs with strong export potential and carried out the impact evaluation. Furthermore, the World Bank has provided technical assistance towards the development of a sound, efficient, deep, and inclusive Colombian financial system, strengthening financial sector oversight, developing the capital markets, and supporting financial inclusion (P157596, P169580). Currently, the World Bank is supporting Colombia's efforts to further integrate into the global economy, with a special focus on increasing the role of modern services, FDI and global value chains, in the context of the recently launched "Internationalization Taskforce" (P174297).

78. **The proposed DPF is informed by the Colombia Country Private Sector Diagnostic (CPSD)**. The CPSD is a joint IFC-World Bank diagnostic that aims to make concrete recommendations for boosting the private sector and crowding-in private investment in support of the country's development constraints. The Colombia CPSD has identified four cross-cutting constraints that coincide with the areas supported by the proposed operation: fintech and access to capital markets, competition, innovation, and digitalization. Also, the Colombia CPSD emphasizes integration with global value chains in the sector assessments (agribusiness, bioeconomy, and tourism). The teams have closely collaborated to guarantee consistency across tasks. Analysis from the CPSD on fintech and capital markets, competition and innovation and entrepreneurship have served as inputs for the proposed operation, particularly in the rationale of prior actions 2 (capital markets), 4 and 5 (innovation), 6 and 7 (digital finance), and 8 and 9 (entrepreneurship). The Colombia CPSD is ongoing.[136].

79. **This DPF builds on the long-term collaboration with the IFC and MIGA.** The proposed operation is aligned with the IFC's strategic priorities to address the most critical development challenges for the private sector by leveraging Government reforms and policy implementation, in collaboration with the World Bank. This DPF coincides with two of the four priorities identified in the CS: enhance financial inclusion (improve MSME access to finance, green finance, support capital markets development and fintech) and improve competitiveness (promote higher value-added sectors and improve business environment, innovation, competition and digitalization). Furthermore, the teams across both institutions have closely collaborated in the review of reforms and identification of priorities. In particular, IFC specialists from the Financial Institutions Group joined efforts in the preparation of some of the prior actions. Likewise, the World Bank and IFC collaborated with MIGA in the dialogue with the Government of Colombia regarding the COVID-19 crisis support, particularly with Bancoldex to which MIGA approved for the first time a guarantee of US$385 million. The Project, which aims at providing liquidity to MSMEs and corporates to increase their resiliency and helping preserve employment in the face of the COVID-19 crisis, is well aligned with the proposed operation, and it could have significant positive effects on Colombian MSMEs, which contribute approximately 40 percent of GDP and generate

[136] The Decision Review Meeting is planned for June 2021.

about 71 percent of formal employment in the country.

4.4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

80. **The declaration of the general state of emergency within Colombia on March 17, 2020, led to consultation and communication processes adapted to the emergency.** The State of Emergency provided the Government the constitutional basis to rapidly put in place the necessary legislation to support the broad government program aiming to stop the spread of COVID-19 and to mitigate its impact. While traditionally in Colombia decrees undergo an extensive public consultation before they are signed, this has not been possible to the same extent given the need to move rapidly to respond to the crisis. The Government has sought views from a wide range of stakeholders on proposed legislation. Moreover, it has implemented a communication campaign, including an extensive, dedicated website, hotlines, social media contact point and a public communications campaign focusing on informing the public about the COVID-19 pandemic as well as economic and social mitigation programs that the Government has launched. Individual programs have also put in place measures to receive feedback from citizens related to access to the program.

81. **Colombia's Reactivation and Sustainable and Inclusive Growth policy was formulated in a collaborative and innovative manner.** DNP led a public process with 22 virtual working groups with 551 participants from the public and private sectors over less than three weeks that produced the first version of the policy. The discussion was organized along 6 axes: Governance, human capital, poverty, productive diversification, the productive apparatus, and digital enablers. The World Bank participated in working groups contributing to the latter three axes. In a second stage, DNP led the negotiation process among 53 participating government institutions. It held 10 main sessions to discuss 145 policy actions in five pillars: poverty (11), human capital (47), productive sector (59), governance (20) and digital transformation (5). The policy was approved by CONPES on February 11, 2021. The development of this DPF has benefited from the World Bank's engagement with the DNP leading teams throughout the formulation process. The close collaboration has allowed the DPF preparation to be aligned with the Government program priorities maximizing its potential impact.

82. **The preparation of all policy reforms to be supported under the proposed DPF reflects a dedicated consultation process with the Government of Colombia**. Consultation meetings were held with the relevant Government institutions for each of the explored areas and DNP as technical leader of the Government. This process relied on the ongoing engagement between the World Bank Group and counterparts. Exploratory and identification virtual meetings were held with the High Advisor Office for the Vice-President, Ministry of Commerce, Industry and Tourism, the Ministry of ICT, the Superintendence of Corporations, the Superintendence of Industry and Commerce, the Regulatory Commission for Communications, the National Spectrum Agency, DIAN, and DNP's Deputy Director for Sectoral Issues and DNP's Technical Directors for Digital Development, Business Development, Rural and Sustainable Development. During these meetings, potential policy reforms were discussed in terms of their impact, technical soundness, priority within the Government reactivation program, and likelihood of execution within the estimated timeline.

83. **Since the onset of the COVID-19 crisis, the World Bank has further intensified its traditionally close dialogue and collaboration with development partners in Colombia**. IDB support to the Colombian

Government to address the COVID-19 crisis is focused on four areas: (i) the immediate public health response; (ii) safety nets for vulnerable populations; (iii) economic productivity and employment; and (iv) fiscal policies for the amelioration of the economic impact. The IDB saw a substantial increase of its financing to Colombia in 2020. IDB Invest, the private sector institution of the IDB Group, structured and subscribed a social bond (4-year tenor of US$39.6 million) with a gender focus issued by Banco W (bank dedicated to microfinance) and registered in the Colombian Stock Exchange. Also, it granted a US$60 million loan to Bancoldex to support MSMEs affected by the COVID-19 crisis. CAF approved a US$350 million to support the measures adopted by Colombia to contain the social, economic, and financial crisis generated by COVID-19. Additionally, the World Bank is in close dialogue with the French *Agence Française de Développement* (AFD) and the German *Kreditanstalt für Wiederaufbau* (KfW) – both still in the process of defining their level of support to Colombia to address the crisis. Beyond financing, the World Bank also works very closely with all development partners, including the United Nations system, on providing analytical support to Government. Particularly, the World Bank Group has partnered with SECO to support the Government of Colombia to develop the capital markets, implement reforms on the secured transactions regime and system for the use of electronic invoices as a negotiable instrument, strengthen regulatory governance, improve the effectiveness of public investment in STI and corporate governance.

84. **The World Bank is also closely coordinating within the World Bank Group with the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA).** IFC support in response to the COVID-19 crisis may include credit lines to existing global IFC clients under streamlined approval processes for financial institutions (US$2 billion Working Capital Solutions Program) and infrastructure, manufacturing, agriculture, and services companies (US$2 billion Real Sector Crisis Response Facility). IFC clients in the financial sector will also be able to access short-term financing in the form of trade guarantees (US$2 billion Global Trade Finance Program) and risk sharing facilities (US$2 billion Global Trade Liquidity Program and the Critical Commodities Finance Program). MIGA has also designed a COVID- 19 fast-track response package of US$6 billion that focuses on three main areas: (i) procurement of urgent COVID-19 medical supplies/services (up to US$ 1.0-1.5 billion); (ii) countering the adverse economic impact during the COVID-19 crisis through a credit enhancement and a capital optimization program (up to US$ 4 billion); and (iii) complementing IFC Trade Finance, post COVID-19 (up to US$0.5-1 billion). MIGA approved a US$385 million guarantee to Colombia's development bank Bancoldex to support loans to the business sector for working capitals, and the Bank infrastructure team is evaluating a coordinated effort with MIGA in order to leverage capital markets to support the liquidity needs of the infrastructure sector. The World Bank has also collaborated with the IMF on the review of macroeconomic developments and the impact of the COVID-19 crisis on the economy.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

85. **The prior actions supported by this operation are expected to have neutral or positive effects on poverty in the short term, and positive effects on distributional outcomes over the medium to long term, particularly through higher productivity and job creation.** Overall, a more productive and competitive private sector is expected to create more and better jobs, with positive poverty and distributional impacts. Certain measures are expected to have positive short-term implications, including among the firms more affected by the COVID-19 shock, such as MSMEs and women-led businesses. An enhanced regulatory and competition framework for a more competitive, productive, and innovative private sector is expected to support poverty reduction and boost shared prosperity over the medium- and long-term through the faster recovery of firms, and through lower market barriers and increased job creation. Through increased competition, the reforms can also have positive medium and long-term impacts on consumer welfare through lower prices and lower market barriers.

86. **Policies in Pillar 1 aim at improving regulation for private sector-led recovery. The three prior actions included in this pillar are likely to have a neutral poverty and distributional effects in the short run, but a wider range of moderately positive effects in the longer run.** Prior Action 1 aims at adopting better regulation practices; it is expected to have positive direct effects on poverty and distribution, with the effects potentially materializing in the short-term. It is estimated that around 75 percent of the households in the first three deciles have a household member working in a microenterprise, while just 40 percent of the households in decile 10 do so (GEIH), and the average income for workers in micro and small firms is lower than that of larger firms. Improving the business environment and reducing regulatory cost faced by MSMEs is expected to increase their profitability, likely with direct implications on household income, and promote the creation of new jobs. Prior Action 2 that aims to promote transparency and integrity of green bond markets is expected to have moderate medium to long-term poverty and inequality reduction. This effect materializes from the promotion of incentives and removal of barriers for firms' operations that can increase sustainable growth and job creation. Finally, Prior Action 3, through increased competition and transparency in public procurement practices, will allow for savings that can open fiscal space to allocate resources to poverty and inequality reduction strategies more effectively and efficiently, as well as have a potential positive impact through a reduction in prices of goods and services.

87. **The poverty and distributional effects of prior actions in Pillar 2 vary between neutral to positive both for medium to long run.** Prior Actions 4 and 5 that aim to promote investment in science, technology, and innovation from private and public sides, are expected to have a positive impact on reducing poverty and promoting equity in the medium to long-term. It is expected that research projects in STI among MSMEs and in territories with higher poverty incidence enhance human capital accumulation, increase market efficiency, and foster labor market opportunities. Projects financed by the STI fund in the SGR have the scope to boost knowledge-generation on natural resource usage that can facilitate mitigation of environmental risk. On the other hand, policies supported by Prior Actions 6 and 7 aimed at reducing barriers to electronic commerce for low-value payments and facilitating the access to capital markets for MSMEs are expected to have neutral effects on poverty in the short term

and moderate positive effects in the medium to long term, through lower prices, more competitive financial markets, lower market barriers and financial inclusion.

88. **Policies under Pillar 3 to promote high-growth entrepreneurship are likely to have a positive or neutral poverty and distributional effects.** The policy action to foster internationalization is not likely to have significant direct effects on poverty or on the distribution and their contribution to welfare – through indirect mechanisms – may vary by sector, occupation, and structural market characteristics. Prior Action 8 which facilitates public efficiency for public policies that promote entrepreneurship, facilitate financial access and the creation of centers for entrepreneurship and innovation have the potential of economic transformation and job creation. Prior Action 9, which promotes female entrepreneurship, is expected to foster income generation among women and a narrowing of the earning and employment gender gaps and is expected to have positive impacts in the short and medium run-on poverty reduction; this measure is timely as women have been among the most affected by the pandemic. While the policy action related to trade facilitation could reduce time and costs associated with international commerce, it is not expected to have significant direct impact on poverty or inequality. Nevertheless, some positive indirect effects could occur, if it contributes to reducing consumer prices or generate backward linkages that could benefit the less well-off. Nevertheless, constraints related to geography, the market power of intermediaries and the structure of domestic markets can be an obstacle to bringing benefits from lower consumer prices. The policy promoted by Prior Action 10 is expected to facilitate trade by simplifying administrative procedures and improving risk management but is not expected to have a direct or short-term impact on poverty or inequality.

5.2. ENVIRONMENTAL, FORESTS, AND OTHER NATURAL RESOURCE ASPECTS

89. **The prior actions supported under this operation are not likely to result in any significant negative impact to the environment, forests, or natural resources, and, if anything, several actions (including green finance, green innovation and entrepreneurship, digital procedures and payments) could have a positive impact.** The body of prior actions, structured in three pillars, support the recovery of the Colombian economy from the COVID-19 shock and lay the basis for strengthened productivity and growth over the medium term. Pillar I aims to improve the regulatory environment for private sector led recovery through prior actions that improve the regulatory business environment (PA #1), develop the taxonomy of green bonds to support green finance (PA #2), and increase transparency and competition in public procurement (PA #3). Prior actions 1 and 2 are likely to have a positive impact on the environment and natural resources. On one hand, by indirectly, reducing the need for travel as the citizens and business will be able to conduct business and undertake formal business procedures and processes locally, reducing GHG emissions, air pollution, and lowering noise levels in territories. Also, a potential reduction of resource use and waste generation is also expected as all-new procedural information must be digitalized (PA #1). On the other hand, by increasing low-carbon and carbon-resilient investments by enhancing the minimum standards of securities issuances that qualify as green finance (PA #2), funding directed to projects with positive environmental and climate contributions through increased low-carbon investment from green bond-mobilized finance to the mitigation and adaptation sectors, including in pursuit of Colombia’s Nationally Determined Contribution (NDC). Prior action 3 has a neutral impact on Colombia’s environment and natural resources.

90. Under Pillar II, which focuses on promoting innovation and digital finance, relevant prior actions foster investment in innovation through the regulation of tax credits use by MSMEs (PA #4), increasing the allocation of science, technology and innovation resources from the General Royalties System (PA #5),target the development of digital finance through crowdfunding (PA #6) and digital payments (PA #7). Prior actions 4 and 5 are likely to have a positive impact on the environment and natural resources by earmarking at least 2 percent of all resources for environmental innovation and sustainable development with several climate benefits as described in Annex 4. PA #6 is unlikely to result in significant negative impacts to the environment, and PA #7 may contribute to the GHG emission reductions, air quality improvement, and minimize noise levels through online purchasing, reducing the need for travel.

91. Pillar III focuses on fostering entrepreneurship and internationalization, with prior actions focusing on measures to promote high-growth entrepreneurship (PA #8), promote female entrepreneurship (PA #9), and measures to reduce the cost and time to trade (PA #10). PA #8 facilitates the development of green entrepreneurship business models that promote sustainable use of natural capital and will have significant positive effects on the environment by promoting the implementation of cleaner technologies, reduction of GHG emissions, biodiversity conservation and resource efficiency, especially in rural areas and regions with high poverty rates. PA #9 is likely to be environmentally neutral, with no significant impact on the environment, forests, or natural resources. PA #10 indirectly improves the efficiency of environmental controls in borders as the AEO programs reduce time of procedures to be applied to AEO program traders and increase resources for non-certified traders.

92. **The environmental assessment of this operation included a review of Colombia's legal and institutional framework to determine the management capacity of GOC to handle potential environmental effects.** The main financial institutions in Colombia have implemented their own environmental policies. These are focused on the environmental regulatory compliance of their own activities but also include an environmental and social risk analysis system developed to identify, evaluate and timely manage the environmental and social risks that can be generated by the activities and projects they finance, and to promote the production and sustainable management of natural resources. Also, national environmental legislation (compiled in the Single Regulatory Decree for the Environmental Sector, Decree 1076/15) includes environmental requirements on micro and small firms. Regardless of the size of the company, environmental requirements will apply to MSMEs to manage potential environmental negative impacts and risks.

5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS

93. **Public financial management (PFM).** A Public Expenditure and Financial Accountability Assessment for Colombia, finalized in 2016[137], concluded that Colombia's PFM system exhibits reasonable alignment with international good practices at the national government level. The more recent Fiscal Transparency Evaluation completed in 2018 reaches a similar conclusion.[138] The budget is comprehensive, well documented, and implemented as planned, with actual expenditures deviating on

[137] Public Expenditure and Financial Accountability Assessment (PEFA) 2015 of Colombia's Public Financial Management Systems, October 14, 2016.

[138] Colombia Fiscal Transparency Evaluation report (https://www.imf.org/en/publications/cr/issues/2018/08/02/colombia-fiscal-transparency-evaluation-46148).

average from initially planned levels for 2020 and 2019 in 7.5 percent. DNP applies a multiyear perspective, with a Medium-Term Fiscal and Expenditure Framework in place since 2003, though these instruments have yet to be integrated with the budget process[139]. Nonetheless, the budget reflects a mostly well-functioning policy-based system.[140] Execution of budgeted expenditures suggests an overall credible budget that is published and accessible on the Ministry of Finance and Public Credit's website. The GoC has published its annual budget in a timely fashion.[141]

94. Fiscal transparency is generally aligned with good practices except for inconsistent budget classification systems, the on-going transition to public sector international accounting standards and lack of disclosure of internally available information on macroeconomic scenarios, long-term projections, and public corporations.[142] The Government has committed to addressing these weaknesses through a comprehensive reform plan. A trust-funded project[143] was established in 2020 with the objective to "*improve the quality of public financial management information and the efficient allocation of public resources through the development and implementation of tools and methodologies in selected sectors."* Revenue and expenditure controls are comprehensive. Records and controls on cash flows, balances, and public debt support sound fiscal management and provide public institutions with the tools for predicting funding to execute their budgets in an orderly manner.

95. Consolidated public accounts are prepared within six months after the end of the fiscal year. They include full information on revenues, expenditures, financial assets, and liabilities. Year-end accrual-based financial statements are issued by the Accountant General and presented by May 15 of the following year to the Controller General for audit purposes. Controller General auditing policies and procedures provide for the application of financial, compliance, and perform procedures consistent with national government auditing standards. Audit reports are submitted before July 1 of the following fiscal year to Congress and the President.

96. **Public Procurement**. Colombia has made significant progress over the past years in strengthening the performance of the procurement systems. Procurement is based on the legal framework provided in the Law 1150 of 2007, and ruling decrees, the most recent being Decree 1510 of 2013. The Public Procurement Agency (*Colombia Compra Eficiente, CCE*), oversees and leads procurement regulatory reforms. CCE has consolidated its role and its principal programmatic priorities include the adoption of a more strategic approach to procurement as an essential component of public sector expenditure management; the universalization of the use of the transactional electronic procurement system SECOP II (in 2018, 23 percent of the transactions were processed through this system); and *professionalizing* the

[139] CONPES 4008 of October 26,2020 "National Information Policy for the PFM" the National Development Plan (PND) 2018-2022 Pact for Colombia, Pact for equity, included the proposal to reengineer the PFM. The conditions provided by the PND are materialized through the two strategic axes of this policy, oriented to the production of information from PFM in quality conditions and harmonized with international references. The planned actions have an estimated cost of COP 135 billion, implemented from 2020 to 2029.

[140] Colombia: Fiscal Transparency Evaluation report; (2018) PEFA 2015, IMF 2012.

[141] National Decree 2411 of December 30, 2019.

[142] SECO Trust Fund Program for the Strengthening of Public Finance Management will supporting transitional activities in process of agreement with CGN. The Adoption Status of IPSAS in Colombia, July 2017, annex E, calculation of the overall level of accrual alignment according to IPSAS reached 84%.

[143] "Strengthening Public Financial Management in Colombia" P170468, Single Donor Trust Fund closing in 2024, with a USD 7.9 Million contribution from the Swiss State Secretariat for Economic Affairs (SECO)

procurement staff. The current principal priority of CCE is the promotion of the use of Standard Procurement Documents (SPD). In April 2019, the first kit of SPD, in this case for roads, was launched, its use is mandatory, and so far, results have been very positive. The Congress of Colombia has recently approved the Procurement Documents Law, Law 2022 of 2020, which mandates that CCE will adopt Standard Bidding Documents (SBD) that will be mandatory in the contractual activity of all entities subject to the General Contracting Statute of the Public Administration (as described in Prior Action 3). Public-private partnerships are regulated by Law 1508 of 2012.

97. **Foreign Exchange Control Environment**. The Ministry of Finance and Public Credit has requested to the Bank to consider two options for depositing the proceeds of the DPF. The first option is to deposit to its bank account at Citibank N.Y., and the second option is to deposit into the Colombian Central Bank (*Banco de la República)*. Fiduciary due diligence was conducted to cover both options. The external audit of the Consolidated *Financial* Statements of Citigroup Inc. and Subsidiaries for 2018-2019, had an unmodified opinion, and the effectiveness of the Company's internal control over financial reporting was confirmed; this financial institution Citibank N.Y. is acceptable to the Bank. The due diligence did not reveal any fiduciary risks to the development objectives. The 2019 financial statements of the Colombian Central Bank were prepared following International Financial Reporting Standards (IFRS) and the audit was carried out per International Standards on Auditing (ISA), by an independent internationally recognized audit firm, acceptable to the World Bank. Unmodified opinions from the external auditors did not reveal any significant issues related to the internal control environment. The fiduciary due diligence therefore concluded that the FOREX internal control environment does not pose risks to the development objectives of this operation.

98. **The proposed loan will follow the World Bank's standard disbursement procedures for development policy support.** Upon approval of the operation, the effectiveness of the Loan Agreement, and the submission of a signed withdrawal application, the proceeds of the loan will be disbursed into an account denominated in U.S. dollars in a commercial bank, controlled by the National Treasury and part of the Government's foreign exchange reserves, acceptable to the WB or (alternatively into an account denominated in U.S. dollars at the Colombian Central Bank for subsequent credit of the equivalent amount in Colombian Peso into the Treasury Single Account of the Ministry of Finance and Public Credit, thus becoming available to finance budgeted expenditures. The Borrower shall, within thirty (30) days after the withdrawal of the Loan report to IBRD: (a) the exact sum received into the forex account in the Citibank N.Y./Central Bank; (b) the details of the account to which the Colombian Pesos equivalent of the Loan proceeds have been credited; and (c) the record that an equivalent amount has been accounted for in the Borrower's budget management systems. This confirmation will include the applied rate of exchange and the date of transfer. The financial support provided under this operation is not intended to finance goods or services on the list of "Excluded Expenditures".[144] If any portion of the credit is used to finance ineligible expenditures as so defined in the General Conditions of the Loan Agreement, the Bank shall require the borrower to refund the amount and such payments made for excluded expenditures would be canceled.

99. **Overall Integrated Fiduciary Risk is considered low.** As detailed in the PFM, Disbursement And

[144] See the General Conditions for DPF.

Auditing Aspects section, the analysis of Colombia's PFM system, including public procurement, reveals strengths to support the transparent management of budget resources in a reliable manner and the identified PFM weaknesses are being addressed through a reform plan and do not pose risks to the achievement of the program development objectives. The internal control environment over FOREX at the Colombian Central Bank and the internal control environment at the Citibank NY (if this option is chosen) do not pose risks to the achievement of the program development objectives. On this basis, no specific audit of the deposit of the credit proceeds will be required and no additional fiduciary arrangements are considered necessary.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

100. **The Ministry of Finance and Public Credit and DNP are responsible for collecting and monitoring information related to program implementation and progress towards the achievement of results for this DPF**. The Ministry of Finance and Public Credit and DNP are further responsible for coordinating necessary actions among the agencies involved in the reform program supported by this DPF. The World Bank has worked closely with the Ministry of Finance and Public Credit, DNP and sector agencies to define results indicators that are clear and measurable, and that have realistic targets in the context of the COVID-19 crisis. Monitoring and evaluation of the operation will also be carried out through the ongoing policy dialogue and the technical assistance programs linked to this DPF and focused on both the immediate impact and the mitigation measures associated with the COVID-19 crisis and the medium-term agenda focused on a broad-based, inclusive, and sustainable recovery.

101. **Grievance Redress**. Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

6. SUMMARY OF RISKS AND MITIGATION

102. **The overall risk to achieving the development objective is assessed as *substantial*.** Macroeconomic risks and political and governance risks are rated as *substantial* in affecting the achievement of the operation's development objectives. Risks related to sector strategies and policies, technical design of the program, and institutional capacity for implementation and sustainability are assessed as moderate, in light of the high institutional capacity of implementing agencies and of the high degree of political ownership of the reform program, which is in large part derived from the findings of the Government's Taskforces on Capital Markets, Employment and Internationalization. Other risks are assessed low. Risks will be monitored throughout the implementation period of the DPF.

103. **Given that the long-term economic effects of the COVID-19 crisis are still not fully known, that new strand of SARS-CoV-2 could force new lockdowns and require another round of massive vaccination, and that uncertainty about the medium-term fiscal framework persists, the macroeconomic risk is rated as substantial.** First, there is still uncertainty as to whether the COVID-19 crisis has permanently affected both the level and the slope of the potential GDP trend. This has implications for determining the sustainability of macroeconomic policies, and the recuperation of activity and employment. Second, although vaccination against COVID-19 in Colombia and in many of Colombia's trading partners is progressing, the emergence of more transmissible variants of the virus poses the risk of breakouts of infections down the road, which could require further lockdown measures, leading to weaker domestic and external activity. Finally, confidence and credibility of macroeconomic policies over the medium-term depend crucially on the strength and durability of the measures that the government will be able to implement to normalize fiscal policy. Some of these measures would require legislation. The materialization of these exogenous shocks, or the lack of a strong and credible fiscal normalization plan could directly affect Colombia's short and medium-term growth prospects, and erode Colombia's fiscal capacity to support firms, households, and the recovery. If this happened, the Government's priorities could change in a way that could impact the implementation of this DPF series. To mitigate the macroeconomic risks, the Government is working closely with international financial institutions to secure fiscal buffers and formulate a balanced reactivation plan for the economy.

104. **Political and governance risks after mitigation are also assessed as *substantial***. The actions supported in the DPF to broaden access to capital markets, increase the use of digital finance, level the playing field in public procurement and facilitate exports have the overall effect of increasing the intensity of competition across the economy. Whereas this is beneficial to productivity growth and to sharing prosperity more widely, it can dent the vested interests that control large swathes of the Colombian economy. Incumbents may attempt to derail implementation of the reform package since they stand to lose their monopolistic or oligopolistic rents. The high level of political ownership - through the Government's Taskforces on Capital Markets, Employment, and Internationalization - is a mitigating factor that can moderate the influence of such vested interests. In addition, swift implementation of the reform program can give voice to the winners from the reforms (small firms, innovators, new exporters, etc.) who can act as a countervailing force to ensure reforms are implemented.

105. **The proposed DPF has been screened for climate and disaster risks using the WB National Policy In-Depth Screening Tool.** The overall sector risk has been rated as Moderate. For the finance and industry

sector (as the prioritized sectors for the screening of this operation), the current and future impact of identified climate and geophysical hazards have been rated as moderate. The institutional readiness score for both finance and Industry is considered Moderate. The development context considerations included population growth, gender inequity, conflict, financial resources, land ownership issues and access to technology. The key drivers of impacts on priority sectors are related to extreme precipitation, drought, and storm surge, which are common climate-related events in Colombia that result in infrastructure and financial losses. The proposed operation, through a series of policy actions, would help the country overcome and adapt to the climate scenario by promoting the integration of green development projects in medium and small enterprises, and increase sector preparedness and competitiveness.

Risk Categories	Rating
1. Political and Governance	Substantial
2. Macroeconomic	Substantial
3. Sector Strategies and Policies	Moderate
4. Technical Design of Project or Program	Moderate
5. Institutional Capacity for Implementation and Sustainability	Moderate
6. Fiduciary	Low
7. Environment and Social	Low
8. Stakeholders	Low
9. Other	Low
Overall	Substantial

ANNEX 1: POLICY AND RESULTS MATRIX

Prior actions and Triggers	Results		
Prior Actions	**Indicator Name**	**Baseline**	**Target**
Pillar I--- Improving the regulatory environment for private sector led recovery			
Prior Action #1. The Republic of Colombia has taken measures aimed at reducing the cost of doing business by: (a) mandating the simplification, automatization and digitalization of administrative procedures and information obligations on businesses; and (b) institutionalizing the steps required for improving the quality and predictability of technical regulations that directly impact production and marketing costs, as evidenced, respectively, by Law No. 2052, published in the Official Gazette on August 25, 2020, and Decree No. 1468, published in the Official Gazette on November 12, 2020.	Results Indicator #1: Reduction in regulatory burden measured as total savings in compliance costs[145].	COP 0 [2020]	COP 179,468 million [2022]
Prior Action #2. The SFC has adopted measures to ensure transparency and integrity of the market for green finance by developing the taxonomy of Green Bonds in securities issuances as well as instructions on the minimum information that the prospectus for issuance of these bonds should contemplate, as evidenced by SFC External Circular No. 028/2020 dated September 7, 2020 and published in the SFC's website.	Results Indicator #2: Number of green bond issuances that comply with the Green Bond taxonomy and guidelines.	0 [2019]	4 [2022]

[145] DAFP developed a methodology to measure compliance costs savings related to regulatory and administrative simplification policies and programs. The methodology is similar to a Standard Cost Model (SCM), a tool commonly used in the world to measure and monetize regulatory burdens. In the case of Colombia, compliance cost savings from government policies and programs come from reducing the time to complete an administrative procedure (*trámite*); eliminating the need to physically be present to deliver documents or pay fees; eliminating associated costs for transportation or shipment of documents; reducing fees; and eliminating other costs related to compliance with regulatory requirements.

Prior actions and Triggers	Results		
Prior Actions	**Indicator Name**	**Baseline**	**Target**
Prior Action #3. The Republic of Colombia has taken measures to facilitate an increase in competition and transparency in public procurement by mandating the National Agency of Public Contracting Colombia Compra Eficiente to adopt mandatory standard bidding documents in the contractual activity of all entities subject to the General Contracting Statute of the Public Administration, as evidenced by Law No. 2022, published in the Official Gazette on July 22, 2020.	Results Indicator #3: Average number of bids per public bidding process in all the sectors where standard documents are mandatory.	3 [2019]	7.5 [2022]
Pillar II---Promoting innovation and digital finance			
Prior Action #4. The Republic of Colombia has taken measures to promote investment in innovation by regulating the use by MSMEs of tax credits for up to 50 percent for investment in research, technological development and innovation, as evidenced by Decree No. 1011, published in the Official Gazette on July 14, 2020.	Results Indicator #4: Yearly investment by MSMEs in STI projects leveraging on tax incentives.	COP 168.000 million [2020]	COP 285.000 million [2022]
Prior Action #5. The Republic of Colombia has taken measures to promote investment in green innovation by increasing the allocation of science, technology and innovation resources from the General Royalties System for projects related to the environment and sustainable development or to non-conventional renewable energies oriented to energy transition and reduction of carbon emissions, as evidenced by Articles 9-11, 22(5), 50(b) and Chapters IV and V of Title IV of Law No. 2056, published in the Official Gazette on September 30, 2020, and Decree No. 1821, published in the Official Gazette on December 31, 2020.	Results Indicator #5: Total value of projects presented by the private sector that are approved for SGR co-financing and are associated with environmental, sustainable development and renewable energy projects oriented to energy transition and reduction of carbon emissions.	COP 4,845 million [2019]	COP 21,232 million [2022]

Prior actions and Triggers	Results		
Prior Actions	**Indicator Name**	**Baseline**	**Target**
Prior Action 6. The Republic of Colombia has enabled the development of digital finance by increasing the limits of financing through crowdfunding platforms, as evidenced by Article 12 of Decree No. 1235, published in the Official Gazette on September 14, 2020.	Results Indicator #6: Volume of financing through crowdfunding platforms.	COP 8,000 million [2020]	COP 40,000 million [2022]
Prior Action #7. The Republic of Colombia has improved the regulatory framework for digital transactions by establishing requirements to increase the efficiency and transparency of the low-value payment system, as evidenced by Decree No. 1692, published in the Official Gazette on December 18, 2020.	Results Indicator #7: Percentage of adults who make payments or purchases online.	20 percent [2020]	40 percent [2022]
Pillar III--- Fostering entrepreneurship and internationalization			
Prior Action #8. The Republic of Colombia has enacted the Entrepreneurship Law to support high-growth entrepreneurship by unifying public resources and programs to support the development of the entrepreneurship ecosystem within iNNpulsa Colombia, formalizing the initiative for the creation of centers for entrepreneurship and innovation (CEmprende), facilitating financial access for high-growth enterprises, and mandating the introduction of complementary measures to strengthen entrepreneurs' export capabilities and promote MSMEs and entrepreneurship development (particularly of innovative, green and climate mitigating initiatives), as evidenced by Articles 1, 2, 5-7-9, 12, 13, 25, 30-38, 42-44, 46-48, 50-52, 55, 57, 58 and 74-83 of Law No. 2069, published in the Official Gazette on December 31, 2020.	Results Indicator #8: Number of dynamic enterprises participating in acceleration programs offered by iNNpulsa[146].	508 [2020]	3,000[147] [2022]

[146] The Government of Colombia defines dynamic enterprises as those that increase their sales or employment by at least 9 percent per year or their profitability by at least 5 percent per year (National Development Plan 2018-2022).
[147] Indicator and target established in the National Development Plan 2018-2022.

Prior actions and Triggers	Results		
Prior Actions	**Indicator Name**	**Baseline**	**Target**
Prior Action #9. The Republic of Colombia has approved a regulatory framework to further female entrepreneurship by creating and consolidating the autonomous trust fund Fondo Mujer Emprende to provide differentiated technical and financial support to women entrepreneurs and establishing incentives for the creation, formalization and strengthening of MSMEs led by women, as evidenced by Legislative Decree No. 810, published in the Official Gazette on June 4, 2020; Article 47 of Law No. 2069, published in the Official Gazette on December 31, 2020; and Law No. 2125, published in the Official Gazette on August 4, 2021.	Results Indicator #9: Number of women-led enterprises supported through technical assistance and/or co-financing programs offered by iNNpulsa and SENA.	2.230 [2020]	10,178 [2022]
Prior Action #10. The Republic of Colombia has adopted measures aimed at reducing the cost and time for firms to trade and facilitate their integration in global value chains through the extension of the Authorized Economic Operator Program (AEO) to operators of port installations, as evidenced by Resolution No. 48 dated May 15, 2020, published in the Official Gazette on November 4, 2020.	Results Indicator #10: The GVC-related trade value covered by the AEO Program[148].	12 percent [2019]	14 percent [2022]

[148] Trade value of AEO certified firms that both import and export over the total trade value of firms that both import and export.

ANNEX 2: FUND RELATIONS ANNEX

PRESS RELEASE

PR21/115

IMF Executive Board Concludes Review of Colombia's Performance Under the Flexible Credit Line Arrangement

FOR IMMEDIATE RELEASE

Washington, DC – April 30, 2021: The Executive Board of the International Monetary Fund (IMF) concluded on April 28, 2021 its review of Colombia's qualification for the arrangement under the Flexible Credit Line (FCL) and reaffirmed Colombia's continued qualification to access FCL resources.

The current two-year FCL arrangement for Colombia was approved by the IMF's Executive Board on May 1, 2020 (see Press Release No. 20/201). Access under the FCL was subsequently raised on September 25, 2020 to an amount equivalent to SDR 12.267 billion or about US$17.6 billion (see Press Release No. No. 20/300) and Colombia made a drawing of SDR 3.75 billion or about US$5.4 billion in December (see Press Release No. 20/363). The Colombian authorities stated their intention to treat remaining access under the FCL arrangement as precautionary—an amount equivalent to SDR 8.517 billion (or US$ 12.2 billion).

Colombia's FCL arrangement was first approved on May 11, 2009 (see Press Release No. 09/161) and successor arrangements were approved on May 7, 2010 (see Press Release No. 10/186), May 6, 2011 (see Press Release No. 11/165), June 24, 2013 (see Press Release No. 13/229), June 17, 2015 (see Press Release 15/281), June 15, 2016 (see Press Release No. 16/279), and May 25, 2018 (see Press Release No. 18/196).

Following the Executive Board's discussion on Colombia, Ms. Antoinette Sayeh, Deputy Managing Director and Acting Chairman of the Board, made the following statement:

"Colombia's very strong policy frameworks, anchored by a flexible exchange rate, credible inflation targeting-regime, effective financial sector supervision and regulation, and medium-term fiscal framework, continue to serve the country well and have allowed the authorities to deliver a coordinated and timely response to the COVID-19 pandemic. As a result, following the largest recession on record, Colombia's economy is returning to growth with policies well-positioned to support the nascent recovery.

"Colombia remains exposed to elevated external risks given the uncertainty about the path of the pandemic. Delays in the rollout of vaccines worldwide could hamper the domestic recovery through its impact on global demand and oil prices. Tighter global financial conditions could increase borrowing costs and increase rollover risks. In that context, the authorities continue to show their firm commitment to maintaining sound and prudent policies going forward. As such, the authorities have submitted to Congress a comprehensive fiscal reform seeking to raise revenues in a durable and equitable way to safeguard key social spending and public investment, while strengthening the fiscal framework to anchor sound public finances over the medium term. This reform will help to stabilize public debt and place it on a downward trajectory over time, allowing the authorities to rebuild fiscal buffers to secure the resilience of the economy.

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"The FCL arrangement makes financing available when needed and continues to provide a cushion of international liquidity that signals the strength of Colombia's fundamentals and its policy frameworks. The authorities have clearly stated their intention to treat the remaining access under the FCL arrangement as precautionary and intend to prepare for a gradual phasing out as the exceptional set of risks in the global economy clearly recede, in line with the temporary nature of the instrument. A careful communication strategy remains important to facilitate a smooth exit from the FCL."

Table 1. Colombia: Selected Economic and Financial Indicators

I. Social and Demographic Indicators

Population (million), 2020	49.4	Unemployment rate, 2020 (percent)	16.1
Urban population (percent of total), 2019	81.1	Physicians (per 1,000 people), 2018	2.2
GDP, 2020		Adult illiteracy rate (ages 15 and older), 2018	4.9
Per capita (US$)	5,495	Net secondary school enrollment rate, 2018	77.5
In billion of Col$	1,002,587	Gini coefficient, 2019	52.6
In billion of US$	271	Poverty rate, 2019	35.7
Life expectancy at birth (years), 2018	77.1		
Mortality rate, (under 5, per 1,000 live births), 2018	14.2		

II. Economic Indicators

						Projections					
	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
	(In percentage change, unless otherwise indicated)										
National income and prices											
Real GDP	2.1	1.4	2.6	3.3	-6.8	5.1	3.6	4.0	3.8	3.8	3.6
Potential GDP	3.0	2.9	3.0	3.1	-2.0	2.7	2.8	2.9	3.0	3.1	3.2
Output Gap	0.6	-0.8	-1.2	-1.0	-5.9	-3.7	-2.9	-1.9	-1.1	-0.4	0.0
GDP deflator	5.1	5.1	4.6	4.0	1.4	3.0	3.1	3.2	3.3	3.4	3.5
Consumer prices (average)	7.5	4.3	3.2	3.5	2.5	2.1	2.6	2.7	2.8	2.9	2.9
Consumer prices, end of period (eop)	5.7	4.1	3.1	3.8	1.6	2.5	2.6	2.7	2.8	2.9	3.0
External sector											
Exports (f.o.b.)	-11.7	16.8	11.7	-4.7	-21.0	24.9	4.5	3.7	3.5	4.0	4.1
Imports (f.o.b.)	-16.9	2.3	12.1	2.5	-18.5	16.4	4.2	5.4	5.0	5.1	4.6
Export volume	-0.2	2.6	0.6	3.1	-10.1	6.3	6.5	4.5	3.4	3.6	3.5
Import volume	-3.5	1.0	5.8	7.3	-16.0	7.8	5.9	5.2	3.5	3.5	3.3
Terms of trade (deterioration -)	3.3	9.6	5.9	-1.8	-11.8	8.0	0.0	0.0	-0.3	-0.7	-0.4
Real exchange rate (depreciation -) 1/	-4.7	5.7	0.6	-9.1	-11.1	NA	NA	NA	NA	NA	NA
Money and credit											
Broad money	9.5	6.4	5.7	10.0	-3.0	11.1	9.5	9.9	9.9	9.9	9.7
Credit to the private sector	7.7	12.8	6.8	11.6	2.8	9.4	10.9	11.3	11.3	11.4	11.3
Policy rate, eop	7.5	4.8	4.3	4.3	1.8	NA	NA	NA	NA	NA	NA
	(In percent of GDP)										
Central government balance 2/	-4.0	-3.6	-4.8	-2.5	-7.7	-9.5	-4.4	-3.5	-2.9	-2.5	-2.4
Central government structural balance 3/	-3.3	-2.6	-2.3	-2.2	-6.4	-8.0	-3.5	-3.0	-2.7	-2.4	-2.3
Consolidated public sector (CPS) balance 4/	-2.2	-2.4	-4.5	-1.9	-6.8	-8.6	-3.3	-2.9	-1.8	-1.6	-1.5
CPS non-oil structural primary balance	0.0	-0.1	-1.2	-0.8	-4.4	-5.6	-0.6	-1.1	-0.5	-0.4	-0.3
CPS fiscal impulse	-3.3	0.1	1.0	-0.4	3.6	1.3	-5.1	0.5	-0.6	-0.1	0.0
Public sector gross debt 5/	49.8	49.4	53.6	52.3	62.8	64.2	64.3	63.5	61.4	59.3	57.2
Gross domestic investment	23.2	21.6	21.2	21.5	18.8	19.2	19.8	20.5	20.8	20.8	20.8
Gross national savings	18.6	18.2	17.1	17.1	15.5	15.4	16.0	16.6	16.8	16.9	16.9
Current account (deficit -)	-4.5	-3.4	-4.1	-4.4	-3.3	-3.8	-3.9	-3.9	-3.9	-3.9	-3.9
External Financing Needs	13.2	13.5	14.2	15.1	17.4	16.3	15.2	15.4	16.1	15.6	15.5
External debt 6/	49.4	47.2	46.6	49.9	64.4	62.4	61.9	61.1	60.2	59.2	58.3
Of which: public sector 6/	31.9	30.3	29.0	30.0	39.3	38.2	37.5	36.3	34.2	32.6	31.5
	(In percent of exports of goods and services)										
External debt service	66.6	72.0	68.9	75.1	109.3	88.4	80.2	81.3	85.2	83.8	84.5
Interest payments	11.1	10.7	10.5	14.2	16.8	14.9	15.3	15.1	14.8	15.0	15.2
	(In billion of U.S. dollars; unless otherwise indicated)										
Exports (f.o.b.)	34.1	39.8	44.4	42.4	33.5	41.8	43.7	45.3	46.9	48.8	50.8
Of which: Petroleum products	10.8	13.3	16.8	16.0	8.8	13.5	13.4	13.3	12.9	12.9	13.0
Gross international reserves 7/	46.2	47.1	47.9	52.7	58.5	60.7	61.6	62.4	63.3	64.4	65.5
Share of ST debt at remaining maturity + CA deficit	113	103	100	116	124	132	124	113	111	108	104.5

Sources: Colombian authorities; UNDP Human Development Report; World Development Indicators; and IMF staff estimates.
1/ Based on bilateral COL Peso/USD exchange rate.
2/ Includes one-off recognition of previously unrecognized accounts payable worth 1.9 percent of GDP in 2018 and central bank profits. For 2021 includes privatization receipts worth 1.1 percent of GDP that, under GFSM 1986 which is used by the authorities, produces a headline deficit of -8.4 percent of GDP.
3/ IMF staff estimate, excludes one-off recognition of arrears.
4/ Includes the quasi-fiscal balance of Banco de la República, sales of assets, phone licenses, and statistical discrepancy. For 2021 includes privatization receipts, see 2/ above.
5/ Includes Ecopetrol and Banco de la República's outstanding external debt.
6/ Current account deficit plus amortization due including holdings of locally issued public debt (TES).
7/ Excludes Colombia's contribution to FLAR; includes valuation changes of reserves denominated in currencies other than U.S. dollars.

ANNEX 3: LETTER OF DEVELOPMENT POLICY

El emprendimiento es de todos — Minhacienda — El futuro es de todos — DNP Departamento Nacional de Planeación

Bogotá D.C., 9 de agosto de 2021

Señor
DAVID MALPASS
Presidente
Grupo Banco Mundial
Washington D.C.

Asunto: Carta de Política. Competitiveness and Recovery – Development Policy Loan

Estimado Presidente Malpass:

Mediante la presente deseamos manifestar el compromiso del Gobierno de Colombia en avanzar hacia un país más equitativo e inclusivo y alcanzar los Objetivos de Desarrollo Sostenible. Somos conscientes de la imperante necesidad de ser activos en la implementación de acciones de política pública concretas para alcanzar una la recuperación económica, social y ambiental sostenible, de manera articulada con los distintos niveles de gobierno, la ciudadanía y el sector privado.

Teniendo en cuenta que uno de los factores determinantes para la recuperación post-COVID 19 es el crecimiento económico sostenido, y que gran parte de este depende de una actividad económica diversificada y competitiva, Colombia ha venido avanzado en esta dirección de manera decidida y acelerada, a través de acciones y reformas económicas de largo plazo de diversa índole, en línea con nuestro Plan Nacional de Desarrollo 2018-2022 "Pacto por Colombia, Pacto por la Equidad", tal y como el programa de financiamiento y asistencia técnica de Colombia con el Grupo Banco Mundial lo refleja.

A través de operaciones bajo la modalidad de *Development Policy Financing*, Colombia ha recibido históricamente el apoyo, acompañamiento y reconocimiento del Banco Internacional de Reconstrucción y Fomento en su esfuerzo por poner en marcha reformas de política pública precisas, de calidad y con resultados concretos y medibles. En esta oportunidad, específicamente para el impulso a la competitividad de la economía, presentamos un programa que refleja esfuerzos en materia regulatoria, de fortalecimiento del mercado de capitales con un enfoque en financiamiento verde y promoción de herramientas digitales de pago y *crowfunding*, mejora de las reglas y estándares de transparencia en la contratación pública, incentivos a la innovación en micro, pequeñas y medianas empresas, emprendimiento de mujeres y facilitación de comercio, con un énfasis

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particular en los emprendimientos que promueven el uso sostenible de recursos naturales y la mitigación del cambio climático..

Durante décadas y hasta inicios del 2020, Colombia había logrado construir una senda de crecimiento económico, acompañada de una reducción de la pobreza, del desempleo y la informalidad, con criterios responsables de sostenibilidad fiscal. La crisis global originada por la pandemia del COVID-19 impactó fuertemente la economía del país, con efectos importantes en la actividad pública y privada, en respuesta a la cual se implementaron diversas medidas multisectoriales que tuvieron un impacto fiscal importante a nivel de ingresos, gastos y deuda pública en el Gobierno Nacional Central. En consecuencia, en el 2020 Colombia registró un déficit fiscal del 7,8 % del PIB (evidenciando un deterioro de 5,3 puntos porcentuales del PIB respecto de la vigencia fiscal anterior) y unos niveles de pobreza monetaria del 42,5 % y pobreza monetaria extrema del 15,1 %. A mayo de 2021, la tasa de desempleo era del 15,6 %.

No obstante lo anterior, en el año 2021 se han empezado a ver signos de recuperación y reactivación. El Indicador de Seguimiento de la Economía (ISE) registró una tasa de crecimiento anual del 13,56 % a mayo de 2021, evidenciando un desempeño positivo de la actividad económica. Adicionalmente, mientras en mayo de 2020 la tasa de desempleo alcanzó niveles del 21,4 %, a junio de 2021 se encontraba en el 14,4 %. Por su parte, el Producto Interno Bruto del primer trimestre del 2021 creció 1,1 % respecto del mismo periodo de 2020, jalonado principalmente por las actividades artísticas y de entretenimiento (7,6 %), las industrias manufactureras (7 %), las actividades financieras y de seguros (4,9 %), la actividad de la administración pública y defensa, educación y salud (3,5 %) y la agricultura, ganadería, caza, silvicultura y pesca (3,3 %). Por otro lado, el recaudo tributario neto acumulado en el periodo enero-julio 2021 creció el 17,5 % frente al mismo periodo del 2020 y 4,4 % frente al mismo periodo del 2019.

Desde el Gobierno Nacional hemos diseñado y puesto en marcha un plan de reactivación económica para responder a la crisis con estrategias de mediano plazo que incluyen componentes para protección del empleo, promover y apoyar la actividad y competitividad del sector privado e impulsar la ejecución de los presupuestos públicos nacionales y subnacionales.

Convencidos del rol determinante del sector privado en el crecimiento económico sostenido y en la estabilidad social y ambiental del país, construimos acuerdos público-privados que resultaron en 22 pactos sectoriales con 86 gremios de la producción, en virtud de los cuales le apostamos a un incremento de la productividad, la innovación y la competitividad de nuestra economía. Como resultado, a la fecha se han emitido 37 instrumentos de política pública y se han creado varias líneas especiales de crédito por un valor cercano a los 564 billones de pesos. Estos esfuerzos se complementan, adicionalmente, con un plan de inversiones denominado "Nuevo Compromiso con el Futuro de Colombia", el cual comprende inversiones entre 2021 y 2031 por valor de 163 billones de pesos y tiene como objetivo principal la generación de empleo y la reducción de la pobreza y la vulnerabilidad. Para 2030, se espera que el plan aumente el crecimiento económico en un 2,86 % y que genere 758 mil nuevos empleos.

Como complemento a lo anterior, estamos trabajando, entre otros, en el fortalecimiento de los criterios de focalización de programas sociales, en la promoción del crecimiento verde y sostenible, en la formación de capital humano, en el mejoramiento de la relación Estado-Ciudadano, en la mejor coordinación interinstitucional y entre niveles de gobierno, y en medidas para acelerar el desarrollo digital para contar con una mejor infraestructura de datos, adoptar tecnologías de última generación en temas cruciales como la administración de justicia, el acceso a la información y la transparencia en la rendición de cuentas y la gestión del Estado.

Es importante resaltar que, a pesar de los enormes desafíos que enfrentamos, las acciones oportunas y decididas para reactivar la economía, proteger a la población más vulnerable e impulsar la productividad y la competitividad, seguimos firmemente comprometidos con la estabilidad fiscal y la necesidad de salvaguardar la solidez de nuestras instituciones económicas.

Plan Nacional de Desarrollo 2018-2022 "Pacto por Colombia, Pacto por la Equidad"

Uno de los tres pilares de nuestro Plan Nacional de Desarrollo 2018-2022 (PND) busca impulsar la productividad, aumentar la formalización empresarial y promover el dinamismo de las empresas del país. En consecuencia, nuestras estrategias se han enfocado en: (i) construir un entorno empresarial favorable para el establecimiento de negocios formales y competitivos; (ii) apoyar la transformación productiva de las empresas; (iii) simplificar la interacción con el sector público; y (iv) apalancar el comercio internacional para atraer inversiones productivas.

Adicionalmente, a través de dos temas transversales claves en ciencia tecnología e innovación (CTI) y transformación digital, se ha articulado la Política de Desarrollo Productivo con acciones para abordar factores estructurales que obstaculizan el crecimiento de la productividad, situando a la empresa y el entorno productivo en el centro de los esfuerzos gubernamentales. Por ejemplo, proveyéndoles bienes públicos, promoviendo su transformación tecnológica, su acceso a la financiación para innovación y el emprendimiento y fomentando las cadenas de globales de valor. Todo esto, con un enfoque diferenciado que permita aprovechar al máximo las potencialidades de cada región.

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El programa de financiamiento

Este programa de crédito bajo la modalidad Development Policy Financing (DPF) ha sido fundamental para organizar nuestra agenda de acciones de política y fortalecer nuestro marco normativo, en línea con nuestra apuesta de reactivación económica.

Con la puesta en marcha de las acciones de política que se presentan en esta operación esperamos poder avanzar hacia el mejoramiento de la capacidad productiva, abordar las fallas del mercado, eliminar las distorsiones y alcanzar la recuperación económica en el corto y mediano plazo, con un enfoque sostenible, específicamente en: (i) el fortalecimiento del marco regulatorio para la recuperación económica impulsada por el sector privado; (ii) la promoción de la innovación y las finanzas digitales; y (iii) el fomento del espíritu empresarial y la internacionalización así como, el emprendimiento con enfoque de género.

El primer pilar de la operación es el denominado "Mejora del entorno normativo para la recuperación impulsada por el sector privado". Se enfoca en el fomento de la actividad del sector privado a través de una mejor regulación, una ampliación del acceso a los mercados de capital verde y un aumento de la competencia y la transparencia en la contratación pública. Las acciones específicas están dirigidas a: (i) ordenar la simplificación, automatización y digitalización de los trámites administrativos y de las obligaciones de información de las empresas en el marco de la política de mejora regulatoria; (ii) institucionalizar las gestiones necesarias para mejorar la calidad y previsibilidad de los reglamentos técnicos que inciden directamente en los costos de producción y comercialización; (iii) adoptar las medidas necesarias para garantizar la transparencia e integridad del mercado de las finanzas verdes, desarrollando la taxonomía del Bono Verde en las emisiones de valores y (iv) incrementar la transparencia en la contratación pública mediante la adopción de pliegos tipo.

El segundo pilar, denominado "Promoción de la innovación y las finanzas digitales", reconoce los esfuerzos del Gobierno Nacional en el impulso de la inversión en ciencia, tecnología e innovación con un enfoque de sostenibilidad ambiental, así como un aumento del uso de plataformas digitales para recaudar capital a través de la financiación colectiva y la mejora del marco regulatorio del sistema de pagos de bajo valor que promueve la competencia y la inclusión financiera. En esta materia, las acciones de política están enfocadas a: (i) la toma de medidas para promover la inversión en innovación regulando el uso por parte de las mipymes de créditos fiscales de hasta el 50 % para la investigación, desarrollo tecnológico e innovación y el aumento del cupo de incentivos tributarios por inversiones en ciencia, tecnología e innovación; (ii) la promoción de la inversión en innovación verde incrementando los recursos asignados a ciencia, tecnología e innovación del Sistema General de Regalías para proyectos relacionados con el medio ambiente y el desarrollo sostenible, energías renovables y la reducción de emisiones de carbono; y (iii) la

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habilitación de las finanzas digitales aumentando los límites de financiación a través de plataformas de micro financiación; y (iv) la mejora del marco regulatorio de las transacciones digitales estableciendo requisitos para aumentar la eficiencia y la transparencia del sistema de pagos de bajo valor.

Finalmente, el tercer y último pilar, denominado "Fomento del espíritu empresarial y la internacionalización", tiene un enfoque sostenible y de empoderamiento femenino que está relacionado con la promoción de la creación, el funcionamiento y el crecimiento de las empresas, mientras que al mismo tiempo orienta la integración internacional a través del apoyo al emprendimiento de alto crecimiento y la facilitación del comercio. Específicamente las acciones de política en este pilar están dirigidas a: (i) apoyar el emprendimiento y promover la articulación de la oferta del gobierno unificando recursos y programas públicos para desarrollar el ecosistema de emprendimiento dentro de INNpulsa Colombia a través de: la formalización de la iniciativa de creación de centros de emprendimiento e innovación (CEmprende), la facilitación del acceso a financiamiento, el fortalecimiento de las capacidades de exportación y la promoción del desarrollo de las Mipymes y el espíritu empresarial; (ii) impulsar el emprendimiento femenino mediante la creación y consolidación de la fiducia autónoma Fondo Mujer Emprende a través de la creación de un marco normativo para brindar apoyo técnico y financiero diferenciado a las mujeres emprendedoras así como el establecimiento de incentivos para la creación, formalización y fortalecimiento de Mipymes lideradas por mujeres; y (iii) adoptar medidas destinadas a reducir el coste y el tiempo de las empresas para comerciar y facilitar su integración en las cadenas mundiales de valor mundiales mediante la ampliación del Programa Económico Autorizado (OEA) para operadores de instalaciones portuarias.

Con lo expuesto en esta carta de política esperamos haber dado cuenta de nuestros retos y desafíos, así como de nuestra agenda de política pública en materia de competitividad e internacionalización de la economía, proceso que esperamos seguir consolidando en el tiempo con el apoyo técnico y financiero del Banco Internacional de Reconstrucción y Fomento (BIRF).

Sea esta la oportunidad para agradecer una vez más el apoyo incondicional del Grupo Banco Mundial con el desarrollo integral y sostenible de Colombia.

Cordial saludo,

Alejandra Botero.

JOSÉ MANUEL RESTREPO ABONDANO
Ministro
Ministerio de Hacienda y Crédito Público

ALEJANDRA BOTERO BARCO
Directora General
Departamento Nacional de Planeación

Unofficial translation of the Letter of Development Policy

Bogotá D.C., August 9th, 2021

Mr.
DAVID MALPASS
President
World Bank Group
Washington D.C.

Subject: Policy Letter. Competitiveness and Recovery - Development Policy Loan

Dear President Malpass:

We hereby wish to express the commitment of the Government of Colombia to move towards a more equitable and inclusive country and to achieve the Sustainable Development Goals. We are aware of the imperative need to be active in the implementation of concrete public policy actions to achieve a sustainable economic, social and environmental recovery, in a coordinated manner with the different levels of government, citizens and the private sector.

Taking into account that one of the determining factors for the post-COVID-19 recovery is sustained economic growth, and that much of this depends on diversified and competitive economic activity, Colombia has been moving in this direction in a determined and accelerated manner, through various long-term economic actions and reforms, in line with our 2018-2022 National Development Plan "Pact for Colombia, Pact for Equity", as reflected by the financing and technical assistance program of Colombia with the World Bank Group.

Through operations under the Development Policy Financing modality, Colombia has historically received the support and recognition of the International Bank for Reconstruction and Development in its effort to implement precise, quality public policy reforms with concrete and measurable results. On this occasion, specifically to boost the economy's competitiveness, we present a program that reflects efforts in regulatory matters, strengthening the capital market with a focus on green financing and promoting digital payment and crowdfunding tools, improving the rules and standards for public procurement transparency, incentives for innovation in micro, small and medium-sized companies, women entrepreneurship and trade facilitation, with a particular emphasis on companies that promote the sustainable use of natural resources and climate change mitigation.

For decades and until the beginning of 2020, Colombia had managed to build a path of economic growth, accompanied by a reduction in poverty, unemployment and informality, with responsible criteria of fiscal sustainability. The global crisis caused by the COVID-19 pandemic strongly impacted the country's economy, with significant effects on public and private activity, in response to which various multisectoral measures were implemented that had a significant fiscal impact on income, expenses and public debt in the Central National Government. Consequently, in 2020, Colombia registered a fiscal deficit of 7.8% as share of GDP (showing a deterioration of 5.3 percentage points of the GDP compared to the previous fiscal period) and 42.5% monetary poverty levels, and extreme monetary poverty of 15.1%. As of May 2021, the unemployment rate was 15.6%.

Notwithstanding the foregoing, in 2021 we have begun to see signs of recovery and reactivation. The Economic Monitoring Indicator (ISE, for its acronym in Spanish) registered an annual growth rate of 13.56% as of May 2021, showing a positive performance of the economic activity. Additionally, while in May 2020 the unemployment rate reached 21.4%, as of June 2021 it was 14.4%. The Gross Domestic Product of the first quarter of 2021 grew 1.1% compared to the same period of 2020, marked mainly by artistic and entertainment activities (7.6%), manufacturing industries (7%), financial and insurance activities (4.9%), public administration and defense, education and health (3.5%) and agriculture, livestock, hunting, forestry and fishing (3.3%). On the other hand, the accumulated net tax collection in the January-July 2021 period grew by 17.5% compared to the same period in 2020, and 4.4% compared to the same period in 2019.

From the National Government we have designed and implemented an economic reactivation plan to respond to the crisis with medium-term strategies that include components to protect employment, promote and support the private sector's activities and competitiveness, and boost the execution of national and subnational public budgets.

Convinced of the private sector's determining role in sustained economic growth and in the country's social and environmental stability, we built public-private agreements that resulted in 22 sector agreements with 86 production unions, by virtue of which we bet on an increase of productivity, innovation and competitiveness of our economy. As a result, 37 public policy instruments have been issued and several special credit lines have been created for close to 564 billion pesos. These efforts are complemented, additionally, with an investment plan called "New Commitment to the Future of Colombia", which includes investments between 2021 and 2031 for 163 billion pesos, and its main objective is to generate jobs and reduce poverty and vulnerability. By 2030, the plan is expected to increase economic growth by 2.86% and create 758,000 new jobs.

As a complement, we are working, among others, on strengthening social programs' targeting criteria, promoting green and sustainable growth, training human capital, improving the State-Citizen relationship, improving coordination between institutions and between levels of government, and in creating measures to accelerate digital development to have a better data infrastructure, adopt state-of-the-art technologies in crucial issues such as the administration of justice, access to information and transparency in the accountability and State management.

It is important to highlight that, despite the enormous challenges we face, the timely and decisive actions to reactivate the economy, protect the most vulnerable population and boost productivity and competitiveness, we remain firmly committed to fiscal stability and the need to safeguard the strength of our economic institutions.

National Development Plan 2018-2022 "Pact for Colombia, Pact for Equity"

One of the three pillars of our 2018-2022 National Development Plan (PND, for its acronym in Spanish) seeks to boost productivity, increase business formalization and promote the dynamism of the country's companies. Consequently, our strategies have focused on: (i) building a favorable business environment to establish formal and competitive businesses; (ii) supporting the productive transformation of companies; (iii) simplifying interaction with the public sector; and (iv) leveraging international trade to attract productive investment.

Additionally, through two key cross-cutting themes in science, technology and innovation (STI) and digital transformation, the Productive Development Policy has been coordinated with actions to address structural factors that hinder productivity growth, placing the company and the productive environment at the center of government efforts. For example, providing them with public goods, promoting their technological transformation, their access to financing for innovation and entrepreneurship, and promoting global value chains. All this, with a differentiated approach that makes it possible to take full advantage of each region's potential.

The Financing Program

This credit program under the Development Policy Financing (DPF) modality has been fundamental to organize our policy actions agenda and strengthen our regulatory framework, in line with our commitment to economic reactivation.

With the implementation of the policy actions presented in this operation, we hope to be able to advance towards the improvement of productive capacity, address market failures, eliminate distortions and achieve economic recovery in the short and medium term, with a sustainable approach, specifically in: (i) strengthening the regulatory framework for economic recovery driven by the private sector; (ii) promoting innovation and digital finance; and (iii) promoting entrepreneurship and internationalization, as well as entrepreneurship with a gender perspective.

The first pillar of the operation is called "Improving the regulatory environment for recovery driven by the private sector". It focuses on promoting private sector activity through better regulation, expanded access to green capital markets, and increased competition and transparency in public procurement. Specific actions are aimed at: (i) ordering the simplification, automation and digitization of administrative procedures and information obligations of companies in the framework of the regulatory improvement policy; (ii) institutionalizing the necessary steps to improve the quality and predictability of technical regulations that directly affect production and marketing costs; (iii) adopting the necessary measures to guarantee the transparency and integrity of the green finance market, developing the taxonomy of the Green Bond in securities emissions and (iv) increasing transparency in public procurement through the adoption of standard bidding documents.

The second pillar, called "Promoting innovation and digital finance", recognizes the National Government's efforts in promoting investment in science, technology and innovation with a focus on environmental sustainability, as well as an increase in the use of digital platforms to raise capital through crowdfunding and improving the regulatory framework of the low-value payment system that promotes competition and financial inclusion. In this matter, policy actions are focused on: (i) taking measures to promote investment in innovation by regulating MSMEs' use of tax credits of up to 50% for research, technological development and innovation and increasing the quota of tax incentives for investments in science, technology and innovation; (ii) promoting investment in green innovation by increasing the resources allocated to science, technology, and innovation from the General Royalties System for projects related to the environment and sustainable development, renewable energies, and the reduction of carbon emissions; and (iii) enabling digital finance by increasing funding limits through microfinance platforms; and (iv) improving the regulatory framework for digital transactions, establishing requirements to increase the efficiency and transparency of the low-value payment system.

Finally, the third and last pillar, called "Fostering entrepreneurship and internationalization", has an approach on sustainability and female empowerment that is related to promoting the creation, operation and growth of companies, while at the same time it guides international integration through support for high-growth entrepreneurship and trade facilitation. Specifically, the policy actions in this pillar are aimed at: (i) supporting entrepreneurship and promoting the coordination of the government's offer by bringing together resources and public programs to develop the entrepreneurial ecosystem within INNpulsa Colombia through: formalizing the initiative to create entrepreneurship and innovation centers (CEmprende), facilitating access to financing, strengthening export capacities and promoting the development of MSMEs and entrepreneurship; (ii) promoting female entrepreneurship through the creation and consolidation of the autonomous trust Fondo Mujer Emprende through the creation of a regulatory framework to provide differentiated technical and financial support to women entrepreneurs as well as the establishment of incentives for the creation, formalization and strengthening of women-led MSMEs; and (iii) adopting measures aimed at reducing the cost and time for companies to trade and facilitating their integration into global value chains by expanding the Authorized Economic Program (AEP) for port facility operators.

With what is stated in this policy letter, we hope to have informed of our challenges, as well as our public policy agenda in terms of competitiveness and internationalization of the economy, a process that we hope to continue consolidating over time with technical and financial support from the International Bank for Reconstruction and Development (IBRD).

Let this be the opportunity to thank you once again for the unconditional support from the World Bank Group with Colombia's comprehensive and sustainable development.

Kind regards,

JOSÉ MANUEL RESTREPO ABONDANO
Minister
Ministry of Finance and Public Credit

ALEJANDRA BOTERO BARCO
Director General
National Planning Department

ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior Actions	Significant positive or negative environment effects	Significant poverty, social or distributional effects positive or negative
Pillar I--- Improving the regulatory environment for private sector led recovery		
Prior Action #1. The Republic of Colombia has taken measures aimed at reducing the cost of doing business by: (a) mandating the simplification, automatization and digitalization of administrative procedures and information obligations on businesses; and (b) institutionalizing the steps required for improving the quality and predictability of technical regulations that directly impact production and marketing costs, as evidenced, respectively, by Law No. 2052, published in the Official Gazette on August 25, 2020, and Decree No. 1468, published in the Official Gazette on November 12, 2020.	**Bottom-line assessment:** Positive **Positive Environmental Impact:** Yes Indirectly, the measure to simplify, automate and deliver online administrative procedures and information obligations reduces the need for travel as the citizens and business will be able to carry out formalities and procedures from their locality, under provisions of Law 2052. The reduction of travel will reduce GHG emissions, air pollution, and minimize noise levels in territories, a product of transportation activities. A potential reduction of resource use and waste generation is also expected as all-new procedural information must be digitalized. **Risk of a Negative Environmental Impact:** No	Neutral / Neutral
Prior Action #2. The SFC has adopted measures to ensure transparency and integrity of the market for green finance by developing the taxonomy of Green Bonds in securities issuances as well as instructions on the minimum information that the prospectus for issuance of these bonds should contemplate, as evidenced by SFC External Circular No. 028/2020 dated September 7, 2020 and published in the SFC's website.	**Bottom-line assessment:** Likely positive **Positive Environmental Impact:** Yes Developing the taxonomy of green bonds in securities issuances will positively impact on environment as it will reduce potential legal and reputational issues related to its environmental integrity[149] and will increase the use of the instrument. Increasing the use of the instrument may proportionally increase a low-carbon and climate-	Neutral / Neutral

[149] According to Asociación Latinoamericana de Instituciones Financieras para el Desarrollo (ALIDE) -Desafíos de los Bonos Verdes. https://www.alide.org.pe/6582-2/

	resilient investment since the destination of the resources raised from green bonds must be aimed at financing or refinancing all or part of eligible green activities or projects. The green bonds contemplate activities or projects proving to have environmental benefits such as mitigation and/or adaptation to climate change[150], conservation of biodiversity, conservation of national resources, and control of air, water, and soil pollution. Potential economic losses resulting from climate change related risks (floods, droughts, infrastructure damage, fires, loss of ecosystem services) would be mitigated at medium and long term by ensuring financing and implementation of green projects. Also, long term environmental benefits will apply by increasing investment on green projects, including: (i) promoting of NCRE projects, and reduction of fossil fuel consumption; (ii) reduction of GHG emissions and contribution to the Nationally Determined Contributions[151]; (iii) potential noise reduction and further decrease of wildlife displacement; (iv) improvement of air quality by reduction of local pollutants, namely, NOx, CO, CO_2, SO_2, and Particulate Matter (PM) emissions to the atmosphere. The instructions on the minimum information required for issuance of green bonds adopt the Green Bond Principles (GBP), and include a	

[150] With joint IBRD/IFC technical assistance, the Financial Superintendence is implementing a strategy that aims to integrate climate-related risks (and opportunities) in the relevant financial regulatory and supervisory framework.

[151] NDCs embody efforts by each country to reduce national emissions and adapt to the impacts of climate change. Colombia's NDC is emit a maximum of 169.44 million t CO_2 eq in 2030.

	collection of international good practices benchmarking and a section dedicated to evaluation process and project selection that will ensure transparency and integrity of the market, being essential for the issuer to comply with additional obligations to be detailed within the instructions and complementary documents of the issuance. The measure is aligned to the current national and international regulation, policies, and agreements[152] regarding sustainable growth. **Risk of a Negative Environmental Impact:** No	
Prior Action #3. The Republic of Colombia has taken measures to facilitate an increase in competition and transparency in public procurement by mandating the National Agency of Public Contracting Colombia Compra Eficiente to adopt mandatory standard bidding documents in the contractual activity of all entities subject to the General Contracting Statute of the Public Administration, as evidenced by Law No. 2022, published in the Official Gazette on July 22, 2020.	**Bottom-line assessment:** Neutral **Positive Environmental Impact:** No **Risk of a Negative Environmental Impact:** No The National policy shall ensure that the reform does not lead to weakening or eliminating environmental and social requirements. The mandatory environmental, social and health assessments are not affected by the limitation of public consultation process.	Neutral / Neutral
	Pillar II---Promoting innovation and digital finance	
Prior Action #4. The Republic of Colombia has taken measures to promote investment in innovation by regulating the use by MSMEs of tax credits for up to 50 percent for investment in research, technological development and innovation, as evidenced by Decree No. 1011, published in the Official Gazette on July 14, 2020.	**Bottom-line assessment:** Likely positive **Positive Environmental Impact:** Yes The tax benefits granted to MSMEs incentive for investment in research projects, technological development, and innovation as defined by Decree 1011, 2020. Environmental development, research, and	Positive / Positive

[152] National Green Growth Policy (CONPES Document 3934, 2018); National Policy for Air Quality Improvement (CONPES Document 3943, 2018); National Logistics Policy (CONPES Document 3982, 2020); Colombian Strategy for Low Carbon Growth; Renewable Energies Law 1715, 2014; Climate Change Law 1931, 2018; Paris Agreement.

	innovation may proportionally be promoted. Indirectly, it will accelerate the development of green technologies that promote and sustainably improve business productivity, and that contribute to the sophistication and diversification of the productive system. Development, Research, and Innovation may include the thematic focus of environmental interest such as: - Biotechnology, bioeconomy, and environment, - Sustainable energy, - Oceans and hydrobiological resources. **Risk of a Negative Environmental Impact:** No	
Prior Action #5. The Republic of Colombia has taken measures to promote investment in green innovation by increasing the allocation of science, technology and innovation resources from the General Royalties System for projects related to the environment and sustainable development or to non-conventional renewable energies oriented to energy transition and reduction of carbon emissions, as evidenced by Articles 9-11, 22(5), 50(b) and Chapters IV and V of Title IV of Law No. 2056, published in the Official Gazette on September 30, 2020, and Decree No. 1821, published in the Official Gazette on December 31, 2020.	**Bottom-line assessment:** Likely positive **Positive Environmental Impact:** Yes Through Law 2056/2020, the Government increases the allocation of resources from the General Royalties System (*Sistema General de Regalías*, SGR) towards science, technology and innovation (STI) from 9.45 percent to 10 percent of total funds, earmarking 2 percentage points of the 10 percent for projects related or impacting environment, sustainable development, NCRE oriented to power transformation, and carbon emission reductions. In the same law other measures were taken to increase investment on environmental issues in general. Regarding environmental assignment the SGR will also: - Assign a percentage of 1 percent plus 20 percent of the highest collection for the conservation of strategic environmental areas and the fight against deforestation. The Ministry of Environment and Sustainable Development	Positive / Positive

	must prepare a National Strategy for the Protection of Strategic Environmental Areas. This direct allocation of 1 percent of total royalties for environmental matters is unprecedent under the SGR. - Assign at least 2 percentage points of the 15 percent of total SGR funds allocated to the poorest municipalities to projects related to or with an impact on the environment and sustainable development[153]. This allocation by municipality or allocation by local investment rose from 10.7 percent to 15 percent. The allocation of resources to science, technology and environmental innovation, added to the allocations and increases in resources for the environment sector, will generate together positive impacts on the environment at the local and national level. Some of the main positive impacts include: - Climate benefits: Investment on NCRE projects will reduce GHG emissions (as it displaces energy generated by fossil fuels used for conventional energy production) and allow for the improvement of air quality in the long-term. Also, investment on NCRE will promote power projects different from hydroelectric and thermal[154] such as solar photovoltaic, wind, and biomass projects, which have the capacity to produce energy in the place where it is generated and more constantly, increasing the	

[153] Law 2056/2020 requires the Ministry of Environment and Sustainable Development to develop the guidelines and criteria for the viability and approval of investment projects to be financed with the environmental allocation (1 percent of total SGR fund plus 20 percent of the highest collection generated with respect to the biennial SGR budget), helping to minimize the risk of the unclarity and relevance that the term "sustainable development" may have when selecting projects of an environmental nature.

[154] Hydro generation in Colombia accounts for approximately 80 percent of electricity generation, and there is a need for more thermal energy to meet electricity demand.

	energy access to remote places. In Colombia, hydroelectric depends on periods associated with natural phenomena that affect energy supply from hydroelectric, such as El Niño that produces precipitation deficiencies and reduces the levels of reservoirs. The measure will further promote resilience to climate change, resulting in an opportunity to adapt and absorb environmental impacts as well as local temperature changes alteration of the hydrological cycle, and soil erosion. It will reduce the vulnerability of ecosystems and natural resources (water, air and soil) affected by exploitation of fossil fuels. - Increase investment on reforestation projects and fight against deforestation[155] and REDD[156] projects, which will help to mitigate GHG emissions, and significantly will promote biodiversity (fauna and flora) conservation and protection of natural resources. - Increase investment on projects oriented to prevent and mitigate pollution in soil, water, and air; and on development projects oriented to efficiently manage the natural resources, encouraging the investment in infrastructure for sustainable development and clean growth. **Risk of a Negative Environmental Impact:** No	
Prior Action #6. The Republic of Colombia has enabled the development of digital finance by	**Bottom-line assessment:** Neutral **Positive Environmental Impact:** No	Neutral / Neutral

[155] According to the Strategic Action Program Deforestation has been recognized as a priority regional transboundary problem in the Amazon region by the member countries. According to Global Forest Watch organization from 2001 to 2019, Colombia lost 4.34 Mha of tree cover, equivalent to a 5.3 percent decrease in tree cover since 2000, and 1.70 Gt of CO_2 emissions.

[156] Reduction Emission from Deforestation and forest Degradation

increasing the limits of financing through crowdfunding platforms, as evidenced by Article 12 of Decree No. 1235, published in the Official Gazette on September 14, 2020.	**Risk of a Negative Environmental Impact:** No	
Prior Action #7. The Republic of Colombia has improved the regulatory framework for digital transactions by establishing requirements to increase the efficiency and transparency of the low-value payment system, as evidenced by Decree No. 1692, published in the Official Gazette on December 18, 2020.	**Bottom-line assessment:** Positive **Positive Environmental Impact:** Yes Indirectly, digital payments will reduce the need for travel as the population will have greater ability to make payments or purchases online. The reduction of travels will reduce GHG emissions, air pollution, and minimize noise levels, a product of transportation activities. **Risk of a Negative Environmental Impact:** No	Neutral / Positive
Pillar III--- Fostering entrepreneurship and internationalization		
Prior Action #8. The Republic of Colombia has enacted the Entrepreneurship Law to support high-growth entrepreneurship by unifying public resources and programs to support the development of the entrepreneurship ecosystem within iNNpulsa Colombia, formalizing the initiative for the creation of centers for entrepreneurship and innovation (CEmprende), facilitating financial access for high-growth enterprises, and mandating the introduction of complementary measures to strengthen entrepreneurs' export capabilities and promote MSMEs and entrepreneurship development (particularly of innovative, green and climate mitigating initiatives), as evidenced by Articles 1, 2, 5-7-9, 12, 13, 25, 30-38, 42-44, 46-48, 50-52, 55, 57, 58 and 74-83 of Law No. 2069, published in the Official Gazette on December 31, 2020.	**Bottom-line assessment:** Positive The environmental impacts are positive while negative impacts are mitigable. **Positive Environmental Impact:** Yes Law 2069/2020 that promotes the development of entrepreneurship in Colombia establishes in its Article 5 a regulatory mechanism to facilitate the development of business models that leverage and promote the economy with high added and sustainable value in different areas, from the promotion of activities that are intensive in technology, innovation, sustainable use of natural capital and/or aimed at mitigating the climate action. Also, Article 55 of the law establishes that the national government will support and promote green enterprises with revenues through the development of programs aiming to identify, form,	Positive / Positive

	support and promote green entrepreneurship. Both articles indirectly promote the efficient use of natural resources, pollution prevention and climate change resilience by encouraging the creation of productive green enterprises. These articles are aligned to the current national and international regulation, policies, and agreements[157] which will have significant positive effects on environment by promoting the implementation of cleaner technologies and the conservation of natural capital, allowing for a sustainable growth. **Risk of a Negative Environmental Impact:** To be determined. Depending on the type of business model to be developed (technologies, use of natural capital and sustainable development models) and according to national environmental legislation, business models must be evaluated in order to identify (i) potential environmental risks; (ii) overview of potential environmental impacts; (iii) existence of environmental assessment procedures; and (iv) need of modification or adoption of new environmental regulation. The Government (including all related ministries) must review proposed business models to ensure they are in line with good practices and permitting and guaranteeing all mitigation measures are in place to consider all environmental issues regarding new business models. In highly polluting sectors (e.g., manufacturing, industrial production, energy, transportation, agri-	

[157] National Green Growth Policy CONPES 3934, 2018; Colombian Strategy for low carbon growth; Climate change law 1931, 2018.

	processing and food production) financial institutions supporting MSMEs shall (a) incorporate environmental and social risk criteria as part of the risk screening, and (b) have trained staff and procedural guidelines for the screenings. Currently, the main financial institutions in Colombia[158] have implemented their own environmental policies. These are focused on the environmental regulatory compliance of their own activities but also include environmental and social risk analysis system developed to identify, evaluate and timely manage the environmental and social risks that can be generated by the activities and projects they finance, and to promote the production and sustainable management of natural resources. Current national environmental legislation (compiled in the Single Regulatory Decree for the Environmental Sector, Decree 1076/15) includes environmental requirements on micro and small firms. Regardless of the size of the company, environmental requirements will apply to MSMEs to manage potential environmental negative impacts and risks.	
Prior Action #9. The Republic of Colombia has approved a regulatory framework to further female entrepreneurship by creating and consolidating the autonomous trust fund Fondo Mujer Emprende to provide differentiated technical and financial support to women entrepreneurs and establishing incentives for the creation, formalization and strengthening of MSMEs led by women, as evidenced by Legislative	**Bottom-line assessment:** Neutral. **Positive Environmental Impact:** No. **Risk of a Negative Environmental Impact:** No.	Significant / Positive

[158] Banco de la República, Bancolombia, Davivienda, BAC and Grupo Aval.

Decree No. 810, published in the Official Gazette on June 4, 2020; Article 47 of Law No. 2069, published in the Official Gazette on December 31, 2020; and Law No. 2125, published in the Official Gazette on August 4, 2021.		
Prior Action #10. The Republic of Colombia has adopted measures aimed at reducing the cost and time for firms to trade and facilitate their integration in global value chains through the extension of the Authorized Economic Operator Program (AEO) to operators of port installations, as evidenced by Resolution No. 48 dated May 15, 2020, published in the Official Gazette on November 4, 2020.	**Bottom-line assessment:** Positive **Positive Environmental Impact:** Yes Indirect positive environmental effects are expected from the measure as border control agencies may spend less time on controlling AEO program traders, which will be subject of random controls to check periodically that they have not deviated from good practices. The AEO program is expected to improve environmental due diligence during border controls as more resources on the non-certified traders can be dedicated to control phytosanitary requirements as well as wildlife trading. **Risk of a Negative Environmental Impact:** No	Neutral / Neutral

ANNEX 5: DETAILED POVERTY AND SOCIAL IMPACT ANALYSIS

106. **This PSIA is designed to provide an analysis of the potential effects on poverty and inequality of interventions supported by the Colombia Competitiveness and Recovery DPF.** Because of the ex-ante nature of this assessment, the PSIA analyzes the expected impact of the DPF prior actions, distinguishing short from medium to long run effects. The analysis is based on several assumptions about the theory of change for each prior action and the extent to which these actions are effectively implemented.

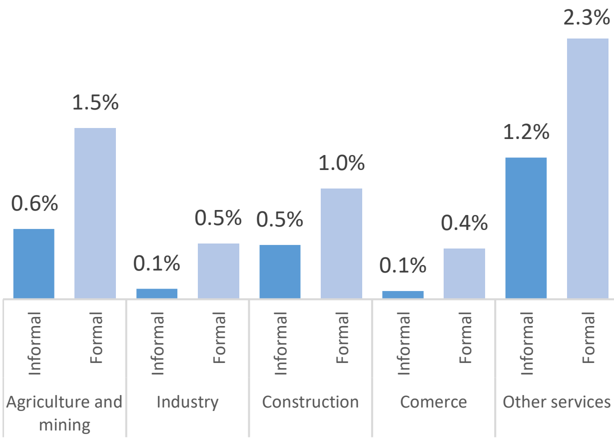
Pillar I: Improving the regulatory environment for private sector led recovery

Prior Action #1. The Republic of Colombia has taken measures aimed at reducing the cost of doing business by: (a) mandating the simplification, automatization and digitalization of administrative procedures and information obligations on businesses; and (b) institutionalizing the steps required for improving the quality and predictability of technical regulations that directly impact production and marketing costs, as evidenced, respectively, by Law No. 2052, published in the Official Gazette on August 25, 2020, and Decree No. 1468, published in the Official Gazette on November 12, 2020.

107. **Streamlining regulatory procedures and reducing regulatory costs for MSMEs is expected to have positive effects in poverty by boosting income generation and incentivizing formality, with positive impacts on job creation and quality.** MSMEs concentrate a large share of jobs in Colombia. In terms of employment, MSMEs up to 100 employees contribute 79.1 percent of total employment, 47 percent of formal employment and 97.6 percent of informal employment. Moreover, these firms generate about 80 percent of the employment among the poor and vulnerable. It is estimated that 45 percent of workers in micro and small enterprises are considered vulnerable workers (compared to 32 percent of workers in big enterprises). MSMEs are intensive in goods and services with less development and use of technology. As reported in the Microenterprise Survey for Colombia (2019) these firms had a substantial regulatory cost burden pre-crisis, representing between 0.5 percent to 2.3 percent of annual cost for formal enterprises, and particularly large in the service sector (Figure 7). Moreover, the Enterprise Survey (2017) points to additional burden from business procedures: small firms (5-19 workers) required more days to obtain a permit or operating license than medium-sized firms, and significantly higher than similar firms in the LAC region (e.g., 115 days to obtain a construction-related permit vs 67 days as LAC average). 29 percent of small firms and 35 percent of medium firms identified business licensing and permits as a major constraint (compared to around 16 percent for each in the region). Moreover, in the context of the COVID-19 shock, these firms have felt the brunt of the COVID-19 shock more severely. Even with some economic recovery in Colombia by the end of 2020, the number of workers in large firms was 5 percent lower compared to the pre-crisis levels, while the loss of jobs in micro, small and medium enterprises was 6 percent, 13 percent and 15 percent, respectively (GEIH, 2020). The supported measures are expected to ease the burden and promote recovery and firm growth among firms, particularly these vulnerable ones.

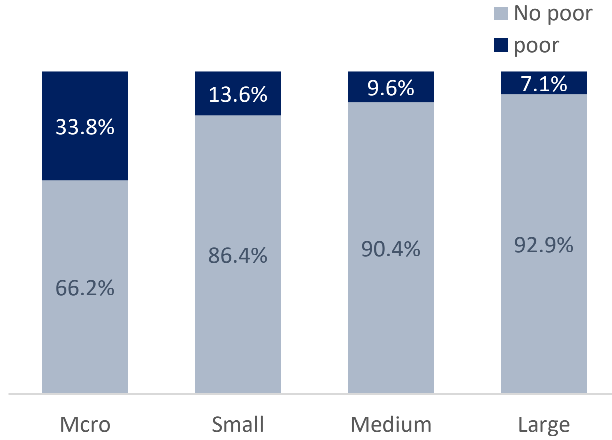
108. By streamlining procedures and reducing regulatory costs, as proposed in Prior Action 1 , MSMEs are expected to increase their profitability and grow, with positive distributional impacts.

Figure 7. Regulatory fees as percentage of annual cost



Source: Own estimations based on Microenterprise Survey (DANE 2019).
Note: Regulatory fees include operating licensing and payments associates to productive activity sush as INVIMA or food handling licence. Informal bussiness does not have registered in RUE or any commercial associations, either do not report paymenrs for social security system.

Figure 8. Proportion of poor employees by businesses size



Source: Own estimations based on GEIH 2019 (DANE).
Note: Micro enterprises have 1 to 10 employees, small 11 to 50, medium 50 to 100 and large enterprises more than 100 employees.

Prior Action #2. *The SFC has adopted measures to ensure transparency and integrity of the market for green finance by developing the taxonomy of Green Bonds in securities issuances as well as instructions on the minimum information that the prospectus for issuance of these bonds should contemplate, as evidenced by SFC External Circular No. 028/2020 dated September 7, 2020 and published in the SFC's website.*

109. **Prior Action 2 is not expected to have a direct impact on poverty in the short-term, yet positive medium to long-term impacts on poverty. The effects would materialize from increases in firm productivity and labor productivity that could lead to job creation and better wages.** Entrepreneurs will access funding in the capital market, potentially in more competitive terms than in commercial banks. It could also mitigate insolvency risk by MSMEs.[159] The supported measure is expected to contribute to the development of business opportunities, economic reactivation, and job creation, and would result in positive effects on poverty in the medium to long run. To the extent that the prior action leads to these impacts for the less well-off that could compensate for concerns over increases of inequalities in capital/financial assets, it would mitigate concerns over rising inequalities in access to assets. Estimates for Gini coefficient in financial assets was over 0.86 in 2014, in the total wealth Gini is equivalent to 0.742[160] for the same year.

Prior Action #3. *The Republic of Colombia has taken measures to facilitate an increase in competition and*

[159] Superintendency of Companies estimates that the probability of insolvency for a small and medium enterprise increase 0,2 and 0,16 percentage points, respectively. In a moderate scenario, in which GDP growth is around 0,6 percent and GDP industry contraction let be 2,7 percent , they show that 15,3 percent of the companies could fall in insolvency, being 30 percent micro and small enterprise.

[160] Núñez, J., Parra, J., and Piraquive, G. (2017). Desigualdad de la riqueza y el ingreso en Colombia. Departamento Nacional de Planeación.

transparency in public procurement by mandating the National Agency of Public Contracting Colombia Compra Eficiente to adopt mandatory standard bidding documents in the contractual activity of all entities subject to the General Contracting Statute of the Public Administration, as evidenced by Law No. 2022, published in the Official Gazette on July 22, 2020.

110. **The policies supported by this prior action are expected to have a positive impact in reducing poverty and income inequality in the medium to long run by increasing transparency in public expending and expanding competitive offer for public goods**. In particular, the effects could be positive through three channels: better quality of goods from a more competitive process, increased opportunities for currently excluded enterprises to participate in public procurement and efficiency savings from the implementation of SBD that allow to expand funding for poverty-focused social programs. The SBD entail a series of benefits such as: the reduction in the time required by the government institutions preparing documents of the bidding process, improving information conditions, and perhaps the most important, they contribute to transparency in the contracting processes, since they have clauses designed to encourage free competition[161] and participation of the largest possible number of bidders in the bidding processes[162]. This would facilitate the entry of competitive bidders with standards for the provision of efficient and higher quality goods of social programs.

111. **MSMEs participate in almost half of public procurements. Improving procurement processes can facilitate access to the public market for potentially efficient new bidders, particularly for MSMEs with lower capacity to navigate cumbersome processes**. Public purchases represent more than 9.9 percent of GDP in Colombia in 2017[163] and cover a wide range of goods and services that are compatible with the main activities of the MSMEs segment. According to the Colombian Observatory of Public Procurement (OCCP), between January 2016 and July 2018, the participation in public procurement of MSMEs was 46 percent at the national level and 47 percent at the territorial level, a figure that contrasts with the fact that MSMEs are 99.6 percent of the country's business enterprise. The factors identified as limiting the participation of MSMEs in public procurement include perceptions of corruption, the distribution of the market between companies and the excess of procedures and regulatory barriers[164]. MSMEs participate in public procurement actively in services sector. In particular some sectors such as management and business for administrative professionals; construction and maintenance; political and civic affairs; engineering, research, technology and educational and training. Expanding SBD can be positive for local employment and development of local markets

112. **Savings from better practices in public procurement can contribute to reallocation of resources in social programs, particularly in a context of tightened budget constraints**. The OECD estimates that the elimination of bid rigging could help to reduce procurement prices by 20 percent or more. Given the

[161] OCDE (2018) Estudios del Sistema Electrónico de Contratación Pública de México: Rediseñando compraNet de manera incluyente, Estudios de la OCDE Sobre Gobernanza Pública, Editions OCDE, París.

[162] It was identified more bidders from the adoption of SBD IN 2019 for public transport sector. The Entities that structured their processes in compliance with the SBD had an average of 33 bidders, in contrast to those that did not apply SBD and had a single bidder. *Cámara Colombiana de la Infrastructura* (2019) "Observatorio de Contratación. Resultados del 1 de abril al 31 de agosto de 2019". Bogotá, Colombia. ***http://www.infraestructura.org.co/16congreso/presentaciones/observatorio-contratacion.pdf***

[163] OECD (2017) Country fact sheet. Government at a Glance Latin America and the Caribbean 2020. http://www.oecd.org/gov/gov-at-a-glance-lac-country-factsheet-2020-colombia.pdf

[164] OCCP (2018). Sobre Agencia Nacional de Contratación Pública - Colombia Compra Eficiente.

above, an illustrative estimate[165] suggests that savings from bid rigging would open resources that can be reallocated to social programs such as *Ingreso Solidario* with significant impact in poverty and income inequality reduction (it could have contributed to a further reduction in poverty in 2020 of 2.4 percentage points due to mitigation measures).[166]

Pillar II: Promoting innovation and digital finance

Prior Action #4. *The Republic of Colombia has taken measures to promote investment in innovation by regulating the use by MSMEs of tax credits for up to 50 percent for investment in research, technological development and innovation, as evidenced by Decree No. 1011, published in the Official Gazette on July 14, 2020.*

Prior Action #5*. The Republic of Colombia has taken measures to promote investment in green innovation by increasing the allocation of science, technology and innovation resources from the General Royalties System for projects related to the environment and sustainable development or to non-conventional renewable energies oriented to energy transition and reduction of carbon emissions, as evidenced by Articles 9-11, 22(5), 50(b) and Chapters IV and V of Title IV of Law No. 2056, published in the Official Gazette on September 30, 2020, and Decree No. 1821, published in the Official Gazette on December 31, 2020.*

113. **Prior action 4 and 5, promoting public and private investment in innovation, research and technological development is expected to have positive impact on poverty and inequality in the medium to long-term.** Private incentives for MSMEs through tax credit can be market-friendly and neutral compared to direct instruments to promote investment in innovation for MSMEs[167]. Tax incentives can increase R&D spending. Despite the fact that MSMEs are more responsive to tax incentives than large firms, is expected that just some MSMEs would participate because of high enterprise informality. As a major concern of tax incentive instruments, concentration of incentives in large firms (who according to previous tax incentives already invest more in technological development and innovation, compared to small business), may need to be monitored to avoid increases in inequality. Even so, is expected that beneficiary MSMEs - hiring new PhD employers or investing in research, development, or innovation - will increase their productivity and of job creation.

114. **An increment in public funds to finance projects trough SGR may potentially benefit the departments where unsatisfied basic need are higher**. The magnitude of the impacts depends on the direction and development of two essential elements. First, the scope of projects financed by the STI fund that could be expected to contribute to knowledge generation in sustainable growth in communities and the effective implementation of practices, both in rural and urban areas. Second, the sustainability over time and efficient utilization of resources. Just in 2020 according with Project Management

[165] Following the estimates from OECD and assuming a probability of preventing bid rigging of 50 percent, savings would allow the expansion of an unconditional cash transfer program created as emergency to mitigate shock from COVID-19 crisis such as Ingreso Solidario. In a microsimulation model we assume three additional monthly transfers up to 12 a year and expanding the program from 3 million to 5,5 million people. The cost of this expansion is equivalent to savings from preventing bid rigging, near 0,99 percent of GDP. The microsimulation assigned to potential recipients who have not participated in other social programs the equivalent monthly amount and then estimates poverty and inequality indexes after accounting for other compensations such as Más Familias en Acción, Colombia mayor or other social programs carried out during 2020.

[166] Before COVID-19 in Colombia 35,7 percent of people were under poverty, is estimated that after pandemic poverty will increase around 6,1 percentage points with mitigation measurements from the government. Thus, assuming savings from measures in this Prior Action, pandemic impacts on poverty would reach 39,4 percent, it is 2,4 less than current estimates since savings would be reallocated in social programs that seek to mitigate poverty.

[167] OECD (2016) Tax incentives for R&D and innovation. OECD Science, Technology and Innovation Outlook

Royalties Index (IGPR[168]) 54 percent of municipalities had insufficient or low performance. More resources for projects in the science, technology and innovation fund of SGR will allow new or large projects to be funded. It will increase the evidence for increasing productivity and sustainable growth. Whether knowledge and technological development is transmitted to communities and the private sector in territories (especially for those with more unsatisfied needs, as shown in Figure 9), with may increase in productivity, sustainable growth, job creation and household income.

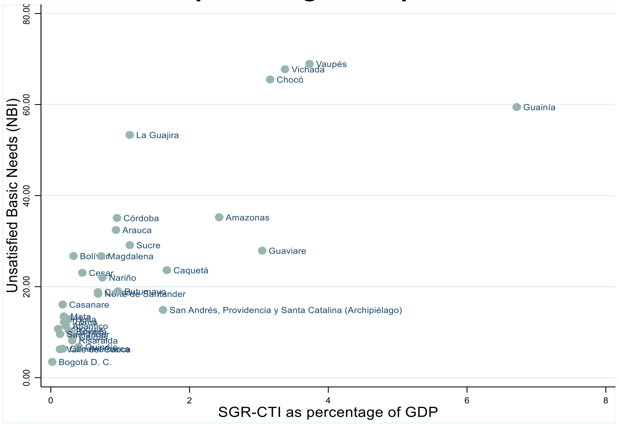
Prior Action 6. *The Republic of Colombia has enabled the development of digital finance by increasing the limits of financing through crowdfunding platforms, as evidenced by Article 12 of Decree No. 1235, published in the Official Gazette on September 14, 2020.*

Prior Action 7. *The Republic of Colombia has improved the regulatory framework for digital transactions by establishing requirements to increase the efficiency and transparency of the low-value payment system, as evidenced by Decree No. 1692, published in the Official Gazette on December 18, 2020.*

115. **Prior actions 6 to 7 are expected to have neutral to positive in the medium to long term in poverty by improving access to alternative financial services and improving financial inclusion.** Increasing limits in crowdfunding can incentivize access to innovative and financial products and services for MSMEs and other firms; closing the gaps for firms with financing needs, it can power the sustainable recovery from COVID-19 generating employments lost by pandemic. Moreover, digital transactions can increase competition, foster productivity, and enhance the quality of financial services in Colombia. It is expected that an increment in efficiency in low-value transactions, switching from cash to digital, increases access to financial services and boosts financial inclusion. Currently, the use of financial mechanism of payment such as e-banking transfer represents around 21 percent for the 25 percent of micro-enterprises with highest sales and just 1.5 percent for those 25 percent with less sales (Figure 10). Financial inclusion can promote access to credit and other financial services for people in low deciles of income, generating opportunities for investment decisions and income generating.

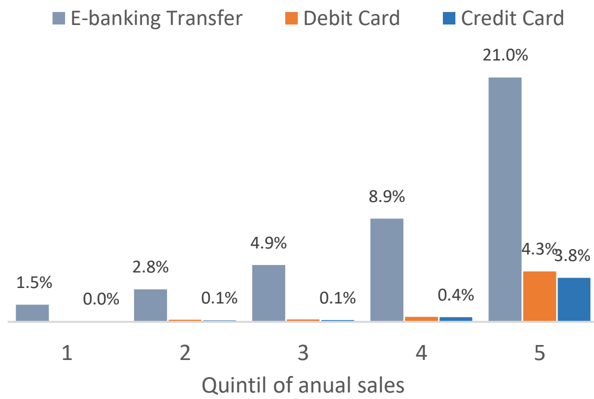
[168] The index is calculated at executory level. It could be National, departmental or municipality level. It measures coverage (prompt and consistency in reporting information) efficiency in contracting, budgetary execution (achievement in costs and schedule, slowing down of procedures), projects ended (costs variation, timing, population benefit etc.)

Figure 9. Relationship between NBI and royalty funds for STI as percentage of departmental GDP



Source: Own estimations based on DNP and DANE.

Figure 10. Banking methods of payment accepted by microenterprise by annual quintile sales



Source: Own estimations based on Micro-enterprise Survey DANE 2019.

Pillar III: Fostering entrepreneurship and internationalization

Prior Action #8. *The Republic of Colombia has enacted the Entrepreneurship Law to support high-growth entrepreneurship by unifying public resources and programs to support the development of the entrepreneurship ecosystem within iNNpulsa Colombia, formalizing the initiative for the creation of centers for entrepreneurship and innovation (CEmprende), facilitating financial access for high-growth enterprises, and mandating the introduction of complementary measures to strengthen entrepreneurs' export capabilities and promote MSMEs and entrepreneurship development (particularly of innovative, green and climate mitigating initiatives), as evidenced by Articles 1, 2, 5-7-9, 12, 13, 25, 30-38, 42-44, 46-48, 50-52, 55, 57, 58 and 74-83 of Law No. 2069, published in the Official Gazette on December 31, 2020.*

Prior Action #9. *The Republic of Colombia has approved a regulatory framework to further female entrepreneurship by creating and consolidating the autonomous trust fund Fondo Mujer Emprende to provide differentiated technical and financial support to women entrepreneurs and establishing incentives for the creation, formalization and strengthening of MSMEs led by women, as evidenced by Legislative Decree No. 810, published in the Official Gazette on June 4, 2020; Article 47 of Law No. 2069, published in the Official Gazette on December 31, 2020; and Law No. 2125,* published in the Official Gazette on August 4, 2021.

116. **Policies promoted by Prior Actions 8 and 9 are expected to have significant direct impacts on poverty and inequality in the short to medium run by increasing income generation through access to entrepreneurship funds; in particular, generating gender inclusion through technical and financial support.** Strategies that promote income generation among women are expected to narrow exiting gaps in opportunities, which have widened during the crisis as women workers have been more affected than men.

117. **Unifying public resources and programs as well as facilitating financial access to high growth enterprises has the potential of boosting entrepreneurship ecosystem, innovation, and job creation**. The new businesses generation necessarily requires an entrepreneurial ecosystem, as well as sources of financing. DANE's EMICRON survey in 2020 revealed that 79.8 percent of micro-businesses nationwide were created by a single owner. Even the same survey indicates that a third of the new businesses were

created because their owners had no alternative income or the required experience, schooling, or training to obtain a job during 2020. To consolidate new enterprises, technical support, and a suitable environment for the exchange of ideas and business opportunities can facilitate the creation of new jobs in the context of a period of economic reactivation such as the one facing Colombia, with the potential to reduce monetary poverty. Financial support in Colombia depends largely on personal savings (63 percent), family loans (10.1 percent) or bank loans (10 percent), however, according to Global Entrepreneurship Monitor for Colombia in 2020 financial support has worsened in recent years, in particular the access and guarantees that Colombian entrepreneurs face.

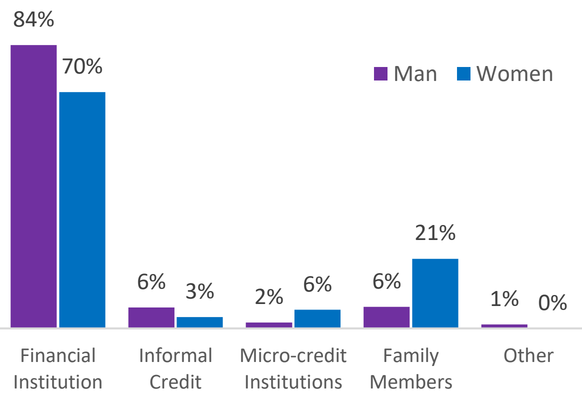
118. **Women are taking a stronger and more robust role in starting new businesses, though they still lag significantly behind men in access to financial or social capital resources**. In Colombia, the total early-stage entrepreneurial activity (TEA) is slightly behind the LAC region, however for each 100 male who are either a nascent entrepreneur or owner-manager of a new business just 88 women are[169]. This relation, although has risen during the last years, remain below some OECD countries. Moreover, according to the 2017 Enterprise Survey, less than one in five firms have a female manager or owner (slightly below the regional average), although Colombia exceeds the regional average in the share of firms with female participation in ownership. The vast majority of female-led micro-business have used their own resources or family loans (62 percent and 11 percent for women, respectively; in contrast to 65 percent and 7 percent for men, respectively) to finance their entrepreneurial endeavors[170]. Lack of access to credit banks is still a gender gap factor, while 70.4 percent of informal women request and get credit approval in financial institutions, 84.4 percent of men do. However, an even higher proportion of women turn to family, or micro-credit institution loans than men (Figure 11). In addition, women have lower access to the benefits that derive from social capital: merely 3 percent of women owners of a microentrepreneur in Colombia are part of organizations such as business or community associations in contrast to 7 percent for men, posing barriers in access to networks that can undermine their business opportunities.

119. **Finally, women were more affected by the pandemic than men in terms of employment loss and poverty.** While employment has recovered for both men and women (at a slower pace for women), a gender income recovery gap remains (Figure 12). Of the women's jobs lost in 2020, 76 percent correspond to positions in micro and small companies. It is estimated that the COVID-19 shock has led to 1.55 million new poor women (1.44 million men); is also estimated that poverty for women will increase by 6.4 percentage points, 0.5 percentage points more than men (Figure 12). The focus on addressing barriers to female entrepreneurship through efforts to promote, support and finance entrepreneurship, formalization and business development of women, can not only have positive broad economic effects from a more efficient use of the country’s talent pool, but can benefit households through increased opportunities for female income generation. In fact, 26 percent of the poverty reduction in Colombia in a decade (2008-2018) was due to female employment and earnings (World Bank, LAC Equity Lab).

[169] Own calculations based on Global Entrepreneur Monitor (2019)

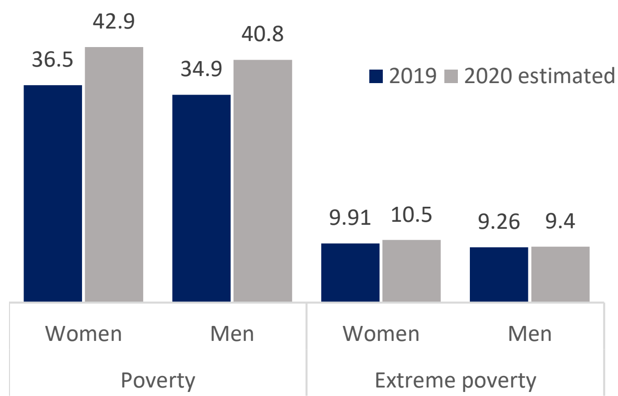
[170] Own calculations based on Microentrepreneur Survey, DANE (2019). Female/male TEA is defined as percentage of female 18-64 population who are either a nascent entrepreneur or owner-manager of a new business, divided by the equivalent percentage for their male counterparts.

Figure 11. Credit accepted for informal microenterprises by gender



Source: Own estimations based on Microenterprise Survey (DANE, 2019).

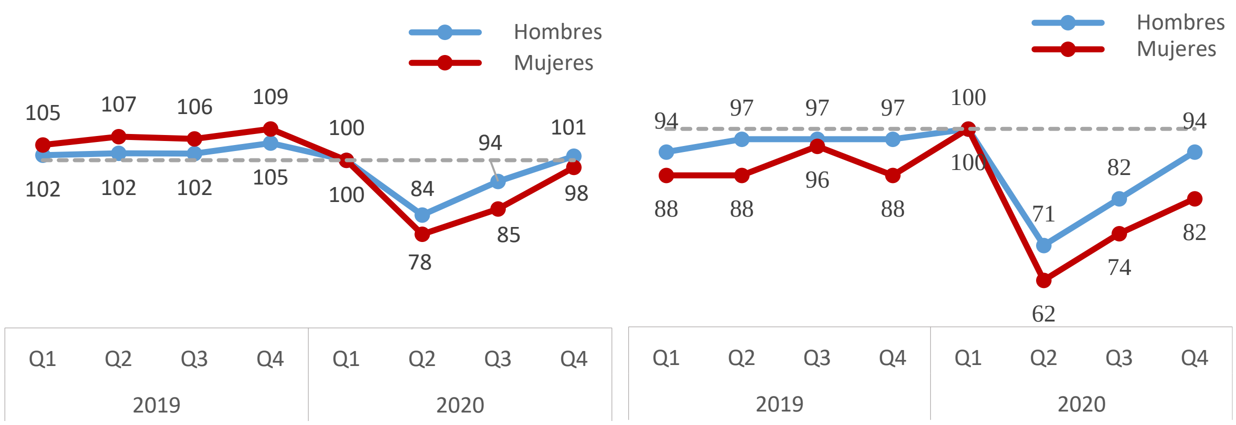
Figure 12. Poverty gender effect of pandemic crisis



Source: Microsimulation based on GEIH-2019 (DANE).

Figure 13. Labor market evolution 2019-2020, by gender

Panel A. Ratio of number of employed compared to Q1 2020 **Panel B. Ratio of median income compared to Q1 2020**



Source: GEIH 2019-2020 (DANE).

Prior Action #10. *The Republic of Colombia has adopted measures aimed at reducing the cost and time for firms to trade and facilitate their integration in global value chains through the extension of the Authorized Economic Operator Program (AEO) to operators of port installations, as evidenced by Resolution No. 48 dated May 15, 2020, published in the Official Gazette on November 4, 2020.*

120. **Measure aimed at reducing cost and time to trade and promoting exports is expected to have not significant direct effects in poverty reduction in the short run, its contribution to welfare will depend on sectors and occupations for which impacts will be concentrated.** Internationalization plays a key role in increasing innovation and productivity. Certification of importers and exporters through AEO program that provides a list of security, tax, and customs requirements can improve the risk management capacities at the borders, limiting the shipment submitted to inspections and hence reduce clearance

costs and time. Trade regulations is a major constrain, mainly for small businesses. As a matter of fact, small businesses spend near 15,5 days to clear direct exports, in comparison to medium and large firms in Colombia which expend 5,7 and 2,9 days more, respectively; and 5,9 days more than small enterprises of LAC region (Figure 14). Moreover, 27 percent of small firms identify customs and trade regulations as a major constraint (Enterprise Survey 2017), higher than for medium and large firms. For firms with a female manager this reaches 30 percent.

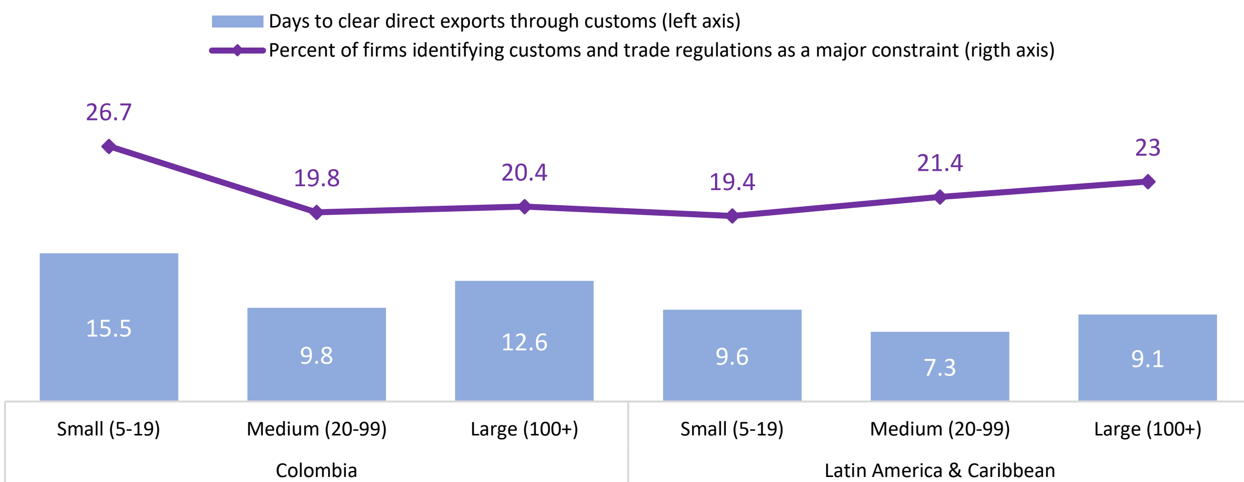
121. Reducing trade barriers aimed at facilitating development of trade may have positive effects on firm productivity, and potentially job creation for certain sectors. This is particularly the case in a recovery process, from a shock that has affected dramatically trade by temporary sealing borders and locking downs economies, that has transmitted to most sectors in the economy. Our estimates suggest that the new poor in Colombia were employed in the commerce (49.7 percent) and services sectors (26 percent) pre-pandemic.[171] However, while it is true that trade brings overall gains to households and is critical for lowering poverty, impacts differ over time and regions, depending on the speed of the adjustment process, geographically concentration and certain sectors and occupations for which impacts may be concentrated. For instance, gains can be limited to sectors that employ a larger proportion of skilled workers, but constrains related to geography, the market power of intermediaries and the structure of domestic markers can be critical to not bring benefits from lower consumer prices.[172] On the other hand, the distributional impacts depend on the nature of sectors benefited by the program, geographical characteristics, or skill level of workers. It is crucial to quote the importance of complementary policies because trade liberalization alone can perpetuate historical disparities[173], specially between regions. Without complementary policies, the gains could be concentrated in most urban areas or be limited. Recent work by Kugler et al (2020) shows that policies toward strengthening Global Value Chains (related to fall in barriers for seamless business logistics, reductions in tariffs, and lower barriers to foreign direct investment) have very modest impacts on poverty and inequality; this limited impact is partly related to the fact that there are relatively few direct jobs created to benefit households with low levels of human capital and the suboptimal positioning of Colombian firms to latch onto GVCs.

[171] Microsimulation model of Global practice of Poverty and Equity of the World Bank for Colombia, estimating impacts on labor market in poverty an inequality based on data from GEIH-2019.

[172]World Bank, 2021. Distributional impacts of trade, empirical innovations, analytic tools, and policies response.

[173] Wage distribution in Colombia were affected by tariff reduction between 1980s and 1990s. Mainly three channels explain that change. Skill premium return driven by skilled-biased technological change, changes in industry wages with negative impacts on sectors with lower wages and unskilled concentration of workers, and changes in worker towards informal sector. Attanasio, O., Goldber, P., and Pavnik, N. (2004). Trade reforms and wage inequality in Colombia. Journal of Development Economics. V. 74. PP 331-366.

Figure 14. Days to clear direct export and percent of firms identifying trade regulations as a major constraint in Colombia and LAC region



Source: Enterprise Survey, World Bank, 2017.