IV. TRADE POLICIES BY SECTOR

(1) OVERVIEW

1. Since the last El Salvador trade policy review, the importance of the manufacturing sector has increased appreciably in terms of its contribution to GDP and foreign trade. This is mainly due to the expansion of the industries operating under special regimes such as free zones and outward processing warehouses. With the notable exception of some agro-industrial activities, El Salvador has made only limited use of trade policy measures as instruments of industrial policy and the level of tariff protection accorded to the manufacturing sector is relatively low.

2. Although manufacturing may have grown more rapidly than agriculture, the agricultural sector continues to be important in terms of its contribution to value added and national employment, as well as in terms of its ability to generate foreign exchange. The Government has defined a specific agricultural trade policy whose general objective is to create favourable conditions for Salvadoran agricultural producers that help to make them more competitive and facilitate their integration into the national production chains and the world market by ensuring an adequate domestic supply and promoting their participation in the growth of exports. To this end, it has undertaken a review of the tariff structure for "sensitive" agricultural products, a review which by the end of 2002 had resulted in an increase in the tariffs applicable to imports of cheese, rice, white corn and pig meat. The two main agricultural exports, coffee and sugar, have been exposed to adverse market conditions, including a collapse in international prices.

3. Since 1996, there have been considerable changes in the services sector, especially in the area of telecommunications and financial services. These have made possible significant advances in the process of modernizing sectors of fundamental importance for national development. At the same time, the electrical sector has been extensively reformed to ensure the greater participation of the private sector and greater efficiency in the generation, distribution and marketing of electrical power. With respect to multilateral commitments, El Salvador has participated in the negotiations on financial services as well as in the GATS negotiations on basic telecommunications and has accepted both protocols.

(2) AGRICULTURAL SECTOR

(i) Market structure and results

4. The economic importance of the agricultural sector has declined since the last El Salvador trade policy review, although the sector continues to exert considerable influence in terms of contribution to value added and national employment. The sector's contribution (including hunting, forestry and fishing) to total GDP fell from 13.5% in 1996 to 12.3% in 2001. This contribution rises to more than 20% if the agro-industrial sector (food, beverages and tobacco) is included (Table IV.1). The importance of the agricultural sector for El Salvador's social development is reflected in the fact that the rural population accounts for more than 40% of the total population and more than 35% of the labour force; moreover, the highest concentration of poverty-stricken households is to be found in the rural areas.[1]

5. According to the Salvadoran Foundation for Economic and Social Development (FUSADES), the loss of dynamism in the agricultural sector during the second half of the nineties can be attributed

[1] FUSADES (2001), *The State of our Economy: 2000-2001*, Department of Economic and Social Studies.

to a number of factors and in particular to adverse weather conditions, low levels of productivity (especially in the case of sugar and basic grains), insufficient business training and poor infrastructure. FUSADES also mentions the lack of a legal and institutional framework for promoting and protecting free competition, as well as the deterioration of the environment. With respect to the environmental problems that the country is experiencing, it should be noted that in 1998 the Legislative Assembly adopted an Environment Law (Decree No. 233 of 2 March 1998, published in Official Journal No. 79, Volume 339 of 4 May 1998) intended to ensure the protection, conservation and recovery of the environment and the sustainable use of natural resources, as well as to regulate environmental management, both public and private. A year before the Law was adopted, the Ministry of the Environment and Natural Resources was set up and made responsible for monitoring compliance with the environmental protection legislation in El Salvador.

Table IV.1
Contribution of the agricultural and agro-industrial sector to GDP, 1996-2000[a]
(%)

	1996	1997	1998	1999	2000
Agriculture, hunting, forestry and fishing	13.51	13.01	12.45	12.96	12.28
Coffee, "oro"	3.13	2.81	2.48	2.77	2.31
Basic grains	2.71	2.48	2.2	2.53	2.27
Sugar cane	0.61	0.73	0.81	0.76	0.73
Other agricultural products	2.29	2.25	2.21	2.2	2.19
Livestock farming	2.16	2.24	2.2	2.18	2.18
Poultry farming	1.37	1.39	1.45	1.51	1.59
Forestry	0.76	0.74	0.71	0.7	0.69
Hunting and fishery products	0.48	0.36	0.39	0.31	0.29
Agro-industry[a]	8.01	8.16	7.96	7.99	8.17

a Includes the food industry (meat and meat products, dairy products, processed fish products, milling and bakery products, sugar, other processed food products, beverages, processed tobacco).
Data at constant prices.

Source: Central Reserve Bank of El Salvador.

6. Between 1996 and 2001, on average, the area reserved for growing the main crops (coffee, sugar cane and basic grains) amounted to some 710,000 hectares; however, this area fluctuated sharply reaching a peak of some 762,000 hectares in 1997 and a minimum of barely 678,000 hectares in 2000. The two main crops in terms of cultivated area are maize and coffee; whereas the area planted with maize fluctuated considerably during the period under review, the area planted with coffee remained more or less constant. In this connection, the authorities have noted that in El Salvador there are no legal or *de facto* restrictions to prevent the coffee-growing areas from being expanded or reduced. Apart from maize, the main crops for domestic consumption are sorghum and beans; for these two products the cultivated area (and production) have followed opposing trends. Whereas the area planted with beans has increased by more than 25%, that planted with sorghum has receded by a little over 18%. Likewise, the indicators for rice point to a considerable contraction, in terms of both cultivated area and production, over the last two years. During the same period, the figures for the main fruit crops remained relatively constant (Table IV.2).

Table IV.2
Main crop production indicators, 1996-2001
(Thousands of hectares and tonnes)

	1996	1997	1998	1999	2000	2001
Traditional						
Green coffee						
Cultivated area	163.9	164.2	162.0	162.1	162.2	162.2
Production	148.9	124.2	117.2	160.8	114.1	112.2
Cane sugar						
Cultivated area	55.8	69.9	74.9	77.1	75.3	64.4
Production	4.908.5	5.169.9	4.966.2	5.306.6	5.071.2	4.589.5
Basic grains						
Maize						
Cultivated area	279.1	306.1	295.4	263.4	259.3	294.1
Production	630.0	507.7	563.1	659.8	583.0	565.0
Sorghum						
Cultivated area	119.4	124.4	109.3	106.4	93.9	97.5
Production	182.0	199.7	168.6	139.5	149.0	148.8
Beans						
Cultivated area	67.7	83.0	78.1	74.4	79.0	85.2
Production	59.1	67.5	46.6	66.5	68.2	74.1
Rice						
Cultivated area	10.7	14.9	10.3	10.9	8.2	6.3
Production	55.3	66.1	51.4	57.4	47.2	37.3
Fruit						
Bananas						
Cultivated area	6.4	6.4	6.4	6.5	6.0	6.0
Production	40.9	70.0	70.0	70.0	65.0	65.0
Oranges						
Cultivated area	4.9	5.6	5.1	4.9	5.2	5.2
Production	33.0	36.3	26.1	37.0	37.3	37.3
Avocados						
Cultivated area	4.2	4.2	4.3	4.3	4.0	4.0
Production	41.5	42.0	42.5	42.5	40.0	40.0
Lemons						
Cultivated area	2.7	2.7	2.7	2.7	2.8	2.8
Production	23.5	23.5	23.5	24.0	25.0	25.0
Mangoes						
Cultivated area	2.7	2.7	2.7	2.7	2.5	2.5
Production	17.9	17.9	17.9	18.0	17.5	17.5

Source: WTO Secretariat, based on FAOSTAT data.

(a) Coffee

7. Up to the year 2000, coffee's contribution to El Salvador's agricultural value added was about 20% and its contribution to total merchandise exports about 10% (Table IV.3). The coffee sector has traditionally been one of the principal generators of jobs in El Salvador's rural areas: during the nineties, the sector employed, on average, 155,000 people each year, about 17% of the rural labour

force. Accordingly, the crisis through which the sector has been passing since 1997 has had a considerable economic and social impact on the rural areas of the country. During this period, Salvadoran producers have not only suffered losses due to various natural phenomena, including the earthquakes which shook the country at the beginning of 2001 and which cost the sector more than US$600 million, but have also had to confront a collapse in prices on the world market to levels of less than 50 dollars per quintal (one quintal is equal to 45 kg).[2]

Table IV.3
Volume and value of coffee and sugar exports, 1996-2000

	1996	1997	1998	1999	2000	2001[a]
Coffee						
Volume (thousands of tonnes)	138.2	166.4	101.5	113.9	150.4	92.1
Value (millions of US$))	339.0	520.5	323.7	245.1	297.9	115.1
% of total exports	19.0	21.5	13.3	9.8	10.1	4.0
Sugar						
Volume (thousands of tonnes)	97.6	174	245.5	219.3	256.5	310.4
Value (millions of US$)	36.6	56.1	67	46.5	39.9	70
% of total exports	2.0	2.3	2.7	1.9	1.4	2.4

a Preliminary figures.

Source: WTO Secretariat, based on figures published by the Central Reserve Bank of El Salvador.

8. According to a study by the Salvadoran Coffee Council (*Consejo Salvadoreño del Café*), during the last four years the trend in coffee prices has reflected the surplus in world supply relative to consumption.[3] In particular, the study mentions the entry into the world market of Vietnam, a country which increased its share of the global supply from 4% in 1995 to 13% in 2001, as well as the sharp increase in the productive capacity of Brazil in recent years, as two of the factors that have contributed to the sharp growth in world supply.

9. In the case of El Salvador, the fall in coffee prices has been translated into significant decreases production, which declined from an average of 3.1 million quintals of "*ora-uva*" in the nineties to 2.4 million during the 2000-2001 and 2001-2002 seasons. In terms of the income generated by coffee exports in the five-year period 1994-1998, during the period 1999-2001 El Salvador lost on average US$138 million a year.

10. According to the estimates of PROCAFE and the Salvadoran Coffee Council, for the 2000-2001 season the losses of the Salvadoran coffee producers amounted on average to 12 dollars per quintal.[4] The fall in prices had the greatest impact on the profitability of the cooperatives and micro-producers (those with less than seven hectares under cultivation). Faced with this drastic decline in profitability, the producers have been reducing their investment in inputs for the maintenance of the coffee plantations, sowing and re-sowing, pest control and fertilization, so that during the 2000-2001 season investment in each of these activities fell by between 26 and 90% relative to the average for the period 1995-1999. If this trend continues, it will have an adverse

[2] Economic Commission for Latin America and the Caribbean (ECLA) (April 2002), *Central America: The impact of the fall in coffee prices* (Mexico-United Nations).

[3] Salvadoran Coffee Council, The Coffee Market in 2002 (copy supplied by the authorities), undated.

[4] Estimates cited in ECLA (2002).

impact on the future productivity of the Salvadoran coffee plantations. The current crisis has also affected other activities linked with coffee, particularly transport.

11. The abandonment of numerous plantations as a result of the crisis in the sector has led to a considerable increase in unemployment in the countryside and a reduction in the income of many rural workers, whose numbers fell to 96,000 in the 2001-2002 season. It is estimated that in 2002-2003 the demand for labour will fall by an additional 35%. According to UNICEF, as a result of the growing unemployment and the lack of alternative sources of income for many of the families that depend on coffee, in some municipalities up to 80% of the children are suffering from malnutrition.[5]

12. In response to the crisis in the sector, in July 2001 the Government established the Environmental Trust for the Conservation of the Coffee Forest (*Fideicomiso ambiental para la conservación del bosque cafetalero* - FICAFE), to which the coffee debt portfolios of seven banks have been transferred. At the same time, the sector's 20-year credit was restructured and the farmers were granted loans partially guaranteed by the Government. Although these measures are bringing short-term relief, given the high levels of indebtedness in the sector (about 3,540 dollars per worker), in the medium and long-term the survival of many coffee-growers will depend on the trend in world prices and their ability to develop products that earn them higher profit margins in international markets.

13. Recognizing this, the Government has been promoting the cultivation of specialty (gourmet and organic) coffees by granting a subsidy equivalent to 6% of the total value of exports (Chapter III.3 (vi)). In recent years there has been an extraordinary increase in the demand for these coffees in the mature markets (mainly the United States and the European Union). Nevertheless, even though coffees already grown in El Salvador predominate in the specialty coffee blend, at present exports of gourmet and organic coffees amount to less than 2% of total Salvadoran coffee exports.

(b) Sugar

14. In volume terms, sugar production has fluctuated considerably since 1996. After recording an increase of almost 7% in 1999, production fell by more than 30% in the two following years, reaching its lowest level since 1996 (Table IV.2). Meanwhile, there was a clear upward trend in the volume of sugar for export. This rose from less than 100,000 tonnes in 1996 to more than 310,000 tonnes in 2001 (Table IV.3).

15. The sugar sector benefits from a high level of protection with nominal tariffs of 40%. According to a study published by the Central Reserve Bank of El Salvador (BCR), the level of protection is even higher because "in order to import sugar it is necessary to obtain the approval of the Ministry of the Economy which is only granted if it considers sugar to be in 'short supply'".[6] The Member countries of the CACM apply a technical standard which requires sugar for the domestic market to be fortified with vitamin A, as a means of counteracting malnutrition, especially among children (Chapter III.2 (x)).

16. At the end of the year 2000, the sector found itself faced with a series of difficulties including, in particular, according to FUSADES, a fall in the world price of the product and non-compliance

[5] United Nations Radio, “Cases of child malnutrition in El Salvador increasing because of the coffee crisis”, 22 October 2002, available at www.un.org/spanish/news/audiovis/radio/02/oct/02102200.htm.

[6] Lazo, Carmen A. and Manuel Sánchez Masferrer, The protection of the sugar market in El Salvador,” in Central Reserve Bank of El Salvador, Economic Bulletin 145, July-August 2001.

with domestic sales quotas on the part of one mill, which helped to depress the domestic price.[7] In response to this situation, Parliament passed the El Salvador Sugar Agro-Industry Production, Industrialization and Marketing Law, promulgated in Legislative Decree No. 490, published in the Official Journal, Volume 352 of 17 August 2001. The purpose of this law is to regulate the relations between sugar mills and between the latter and the sugar cane producers. Accordingly, it authorizes the Ministers of the Economy and Agriculture to establish maximum domestic sugar and honey prices on the basis of a technical, economic and social analysis.

17. The Sugar Agro-Industry Production, Industrialization and Marketing Law also set up a Salvadoran Sugar Agro-Industry Council (*Consejo Salvadoreño de la Agroindustria Azucarera*) composed of the Ministers of the Economy and Agriculture, three representatives of the sugar mills and three representatives of the producers' associations. On the basis of each mill's historical share of sugar production and estimates of the domestic and foreign demand, the Council allocates the amount of sugar that can be sold each year by each of the mills on the domestic and preferential markets. The law does not provide for the allocation of quotas to foreign sugar producers for supplying the domestic market.

18. At the same time, the process of privatization which began with the entry into force of the 1994 Law on the Privatization of Distilleries has been considerably extended. The Privatization Law granted credit facilities to enable workers and cane growers linked to the distilleries to purchase shares in the latter. However, the workers who benefited from these credits were unable to fulfil their obligations within the time limits laid down by the Privatization Law.[8] In view of this situation, on 29 July 2002, the Legislative Assembly adopted Decree No. 928 enabling the Salvadoran Investment Corporation (*Corporación Salvadoreña de Inversiones*, CORSAIN), the entity to which the accounts payable in connection with the privatization of the distilleries had been transferred, to offer the debtors new payment options.

(ii) Policy objectives and instruments

19. Within the framework of the agricultural policy formulated for the period 1999-2004, the Ministry of the Economy, in close coordination with the Ministry of Agriculture and Livestock (MAG), has defined an agricultural trade policy whose general objective is to provide favourable conditions for Salvadoran agricultural producers that help to make them more competitive and facilitate their integration into the national productive chains and the world market, by ensuring an adequate domestic supply and promoting their participation in the growth of exports. According to the authorities, the interests of the consumers are also being taken into account in formulating specific measures within the context of agricultural trade policy.

20. For the purpose of achieving the general objective of agricultural trade policy, at the end of 2002, the tariffs applicable to "sensitive" agricultural products were being reviewed. "Sensitive" products are those "with unstable and distorted international markets important for the creation of agricultural jobs and value added".[9] This exercise has resulted in increases in the tariffs applied to

[7] FUSADES (2001), *The State of our Economy: 2000-2001*, Department of Economic and Social Studies.

[8] See recital IV of Legislative Decree No. 928, of 29 July 2000, and recital II of Legislative Decree No. 674, of 28 July 1999.

[9] Ministry of Agriculture and Livestock of El Salvador, *Agricultural Policy and National Agrarian Management 1999-2004*, San Salvador, 4 May 2000.

imports of cheese, rice, white maize and pig meat. The authorities have pointed out that, with the exception of pig meat, the increase in the tariffs on these products is also subject to the process of tariff harmonization initiated in connection with the establishment of a customs union between El Salvador and Guatemala.

21. The Government has established an Interministerial Agricultural Trade Commission (*Comisión Interministerial de Comercio Agropecuario*) composed of representatives of the Ministries of the Economy, Agriculture and Livestock, and Finance. One of the main tasks of this Commission is to guide and advise agricultural producers on matters relating to trade, tariff, fiscal and agricultural health policy, as well as on any other matter of interest that requires technical recommendations for decision-making at ministerial or presidential level. For its part, the MAG, in collaboration with the Ministry of Finance, has implemented the International Agricultural Product Price Information System (*Sistema de Información de Precios Internacionales de Productos Agropecuarios*). Through this system the MAG regularly transmits to the Directorate-General of Customs Revenue (*Dirección General de la Renta de Aduanas*, DGRA) a list of "ordinary competitive prices" for imports, so that the DGRA can detect possible underinvoicing or undervaluation. In addition, it has set up a Consultative Commission on the Management of Donations (*Comisión Consultiva sobre el Manejo de Donaciones*) which analyses and approves any food donations and agricultural inputs that the country may receive with a view to preventing distortions of the local market due to the entry of these products. A Technical Quotas Commission (*Comisión Técnica de Contingentes*), which specializes in making recommendations on the opening and administration of quotas, has also been established.

22. Agricultural trade policy also includes measures to improve market access for Salvadoran agricultural products. To this end, the MAG provides support for the efforts of the Ministry of the Economy in negotiating trade treaties. In addition, several of the specific programmes administered by the MAG as part of the scheme Agricultural Policy and National Agricultural Management 1999-2004 are intended to acquire a larger share of the international market for Salvadoran agricultural products. At the end of 2002, there were specific programmes in such areas as research and technology transfer, promotion of agri-business development, development of the physical support infrastructure for productive activities, agricultural education, agricultural health and security of tenure.

23. As far as financing is concerned, in addition to the loans offered by the banks of the national financial system and under the programmes described in Chapter III (Section (4) (v)), the agricultural and agro-industrial sector has access to public resources channelled through special funds. These funds include the Environmental Loan Fund (*Fondo de Crédito para el Medio Ambiente*, FOCAM), which has about 20 million dollars available for promoting productive environmental conservation activities and the Special Agricultural Development Trust (*Fideicomiso Especial de Desarrollo Agropecuario*, FEDA), whose resources of approximately 45 million dollars are intended for financing investment in medium- and long-term research into various agricultural activities. Both programmes offer preferential terms for users. The Government has pointed out that the guidelines for granting loans under these programmes are being reviewed in order to make the funds more accessible. At the same time, the Government is continuing to support the agricultural sector through funds for refinancing the debts of those affected by natural phenomena, such as the Agricultural Sector Finance Fund (*Fondo de Financiamiento para el Sector Agropecuario,* FINSAGRO), whose resources amount to 34 million dollars.

(iii) Support indicators

24. El Salvador's notifications to the Committee on Agriculture indicate that since 1997 no export subsidy has been granted and no domestic support measure in favour of agricultural products has been

introduced.[10] The tariff protection granted to agricultural products (defined on the basis of Annex I of the WTO Agreement on Agriculture) continues to be appreciably greater than that granted to industrial products (Chapter III.2 (iii)). However, there are no indicators, such as, for example, PSE estimates, that would make it possible to assess the net global impact, on the sector and on specific products, of the various protection and promotion measures.

25. Public expenditure on the agricultural sector has remained relatively constant in nominal terms since the last El Salvador trade policy review. However, as a proportion of total public sector expenditure, public expenditure on agriculture has displayed a clear downward trend, falling from 2.5% of total public expenditure in 1996 to about 2% in 2000 (without taking into account the transfer of US$47 million from the MAG to the Agricultural Development Bank in 2000 to strengthen the latter's position). According to the information provided by the authorities for the period 1996-2000, out of the US$20 million disbursed on average each year for the benefit of the agricultural sector 70% was for productive development, which includes the development of irrigation and drainage systems, market improvement and development, and institutional reform programmes to encourage good management, innovation, environmental regeneration and sustainable agriculture.

(3) MANUFACTURING INDUSTRY

26. Since last El Salvador trade policy review, the manufacturing sector has performed strongly, growing on average at rates higher than those for total GDP. As a result, the manufacturing sector's contribution to the economy has increased significantly, rising from 21.5% of GDP in 1996 to 23.5% in 2001. In terms of employment, the manufacturing sector employs 17.4% of the labour force. Moreover, the sector has played an important role as a generator of foreign exchange, especially the *maquila* industry which in 2001 generated exports worth more than US$1,650 million (equivalent to 57.6% of the total value of Salvadoran exports). However, the value of net *maquila* industry exports was much lower, about US$490 million, since the industry's imports increased to a little over US$1,160 million.

27. On average, during the period 1997-2001, the items making the greatest contribution to manufacturing production were as follows: basic and processed chemicals with 9.8% of manufacturing GDP; milling and bakery products (9.8%); beverages (9.7%); sugar (7.9%); other processed food products (7.1%); and textiles and made-up textile articles (6.9%).[11] At the same time, the most dynamic branches were the rubber and plastics industry, with an average annual growth rate of 9.2% between 1997 and 2001; transport equipment and miscellaneous manufactures (7.6%); paper, board and paper and board products (6.4%); basic and processed metal products (6.2%); and the beverage industry (6.1%) (Table IV.4).

[10] WTO documents G/AG/N/SLV/13 and G/AG/N/SLV/14, of 20 August 2002.

[11] The manufacturing GDP figure used to calculate the weight of these sectors does not include industrial *maquila* services.

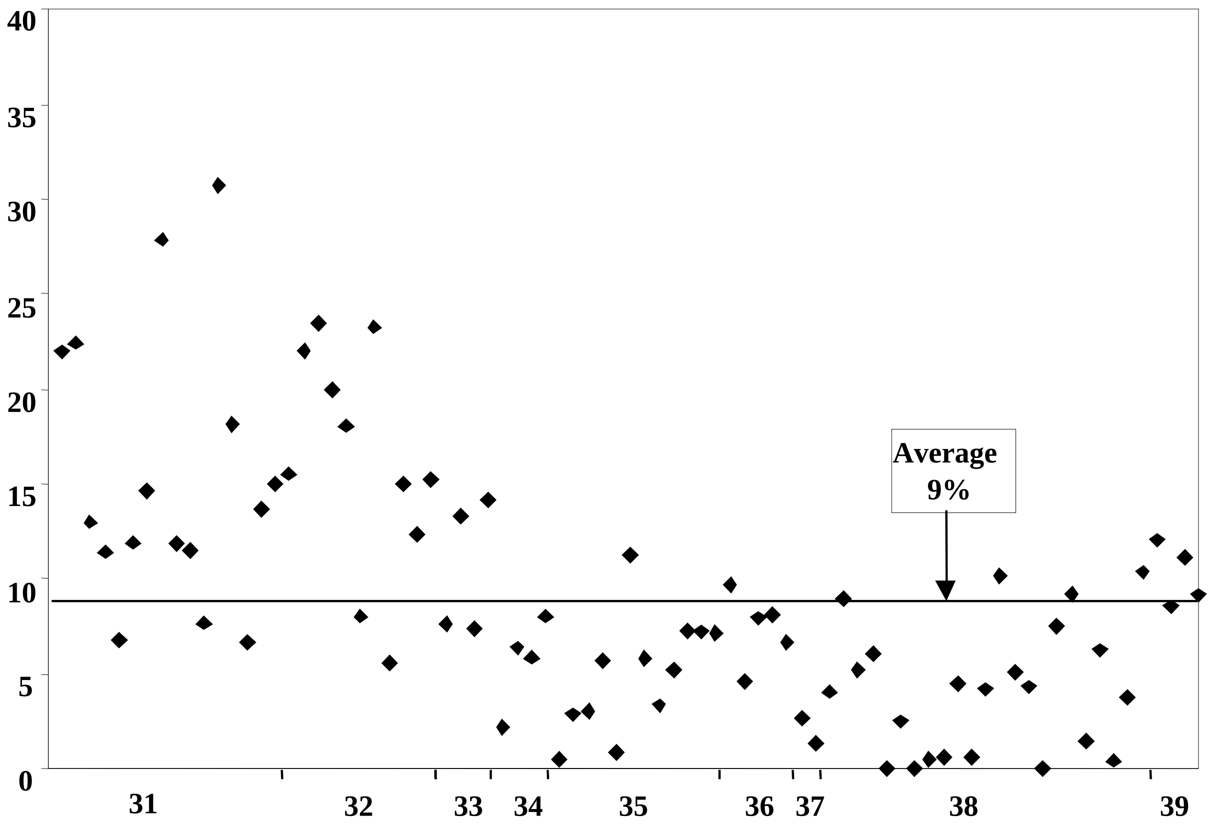
Table IV.4
Breakdown of industrial sector value added, 1996-2001
(%)

	1996	1997	1998	1999	2000	2001
Manufacturing industry (% of total GDP)	21.0	21.0	21.4	22.6	23.1	23.0
Food products	26.5	26.8	27.9	27.5	26.7	26.4
Beverages	7.6	7.7	6.8	6.7	6.5	9.0
Tobacco, processed	1.9	1.5	0.0	0.0	0.0	0.0
Textiles and made-up textile articles (exc. clothing)	6.2	6.7	6.8	7.4	6.6	5.8
Clothing	3.7	3.6	3.5	2.8	2.7	1.8
Leather and leather products	4.9	4.3	5.0	4.2	4.0	3.7
Wood and wood products	2.0	2.2	1.9	2.0	1.9	1.2
Paper, board and products thereof	3.3	3.4	3.3	3.3	3.4	2.7
Products of the printing and allied industries	5.4	5.6	5.2	4.8	4.9	4.5
Basic and processed chemicals	7.3	6.5	7.6	8.1	7.3	8.5
Products of oil refining	6.7	6.1	5.4	6.1	7.1	5.0
Rubber and plastics products	2.1	2.1	2.2	2.1	2.2	2.7
Processed non-metallic mineral products	3.8	4.0	4.4	4.0	3.8	4.3
Basic and processed metal products	4.3	4.4	4.5	4.3	4.7	4.7
Machinery, equipment and supplies	4.4	3.6	3.6	3.5	3.4	3.1
Transport equipment and miscellaneous manufactures	3.6	3.6	4.0	4.5	5.0	3.5
Industrial *maquila* services	6.3	8.0	8.1	8.6	9.9	13.3

Source: Central Reserve Bank of El Salvador

28. In 2000, the main products exported by non-*maquila* manufacturing industry were: chemical products (medicaments and cleaning products); textile products (underwear, clothing, bed, table and kitchen linen, cotton yarn); metal products (rolled iron and steel products and manufactured aluminium goods); and electrical machinery and equipment.

Chart IV.1
Tariff protection in the industrial sector, 2002[a]
(%)



31	Manufacture of food products, beverages and tobacco
32	Textile, clothing and leather industries
33	Wood and wood products industry, including furniture
34	Manufacture of paper and paper products; printing and publishing
35	Manufacture of chemicals and chemical products derived from petroleum and carbon, rubber and plastics
36	Manufacture of non-metallic mineral products, except for petroleum and carbon derivatives
37	Basic Metal Industries
37	Manufacture of metal products, machinery and equipment
38	Other manufacturing industry

a By 4-digit ISIC heading.
Source: WTO Secretariat estimates based on data supplied by the Salvadoran authorities.

29. El Salvador has made only limited use of trade policy measures as instruments of industrial policy, with the notable exception of some agro-industrial activities and the use of special export procedures (Chapter III(3)(vi) and (vii)). The level of tariff protection accorded to the industrial sector is relatively low; in 2002 the average tariff in the manufacturing sector amounted to 7.5% (estimate based on the ISIC classification).[12] However, some industrial activities continue to benefit from levels of tariff protection much higher than the sector average. In addition to some branches of the food industry (ISIC 31), the textile, clothing and leather industry (ISIC 32) and the wood industry continue to enjoy a level of tariff protection above the average for the manufacturing sector (Chart IV(1)). Other industrial sector promotion measures include support programmes for research (Chapter III(4)(vi)) and various specific financing programmes generally focussed on small and medium-sized enterprises (Chapter III(4)(v)).

30. Moreover, Salvadoran industry as a whole, and especially the textile and clothing *maquila* industry, benefits from preferential access conditions under various unilateral concession arrangements such as the Generalized System of Preferences and the Caribbean Basin Initiative (Chapter III(3)(x) and Chapter II(4)(iii)).

31. There has been a considerable increase in the part played by the *maquila* industry in the national economy. Sector exports rose from US$646.6 million in 1995 to 1,651.6 million in 2001, a figure equivalent to slightly more than 57% of total Salvadoran exports for that year. Another development that reflects the dynamism of this sector is the marked increase in the number of free zones, which totaled 15 in July 2002 and occupied about 595,000 square metres of industrial floor space, more than twice the figure for 1996.

32. El Salvador's *maquila* industry specializes in the assembly of clothing. In 2001, approximately 95% of exports from the country's free zones were items of clothing and made-up textile articles, while the remaining 5% consisted mainly of electronic products, although refrigerators, cookers, sewing machines and plastic sheeting were also exported.[13] The experience of other countries suggests that the concentration of *maquila* production on textiles and clothing is hampering the establishment of links between the free zones and Salvadoran enterprises, which is resulting in low levels of local value added.[14] The exports of the Salvadoran *maquila* sector are highly concentrated not only in terms of production but also with respect to their geographical destination, since almost all the sector's exports are destined for the United States.

33. As the authorities have pointed out, one of the main benefits to be derived from the free zones has been job creation. In 2001, the free zones employed 81,220 workers, almost 20% of total manufacturing industry employment. Moreover, almost another 38% of manufacturing jobs in El Salvador are indirectly related with the free zones.

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[12] According to the WTO definition of agricultural products, the average tariff for the non-agricultural sector is 6.7%.

[13] BCR (2002), Quarterly Review, January-March.

[14] Jenkins, Mauricio; Gerardo Esquivel and Felipe Larraín B. (1998), "Export Processing Zones in Central America," *Development Discussion Paper* No. 646, Harvard Institute for International Development, August.

(4) ELECTRICAL SECTOR

34. It is estimated that the contribution of the electrical sector to GDP is 0.6%. Until the middle of the nineties, the Salvadoran electrical sector was dominated by a single State enterprise, the Rio Lempa Hydroelectric Executive Commission (*Comisión Ejecutiva Hidroeléctrica del Río Lempa*, CL). In 1996, new laws were approved. This led to the restructuring of the industry and the breakup and partial privatization of this public enterprise. The new legislative framework for the electrical sector includes the following laws and regulations: the General Electricity Law (Legislative Decree No. 843 of 21 October 1996, published in Official Journal No. 201 of 25 October 1996); its Regulations (Executive Order No. 70 of 25 July 1997); the Law establishing the General Superintendency for Electricity and Telecommunications (SIGET) (Legislative Decree No. 808 of 12 September 1996, published in Official Journal No. 189 of 9 October 1996); the Regulations applicable to electrical energy marketing activities (Executive Decree No. 90, 1 November 2000); SIGET's standards and decisions; the Regulations of the Transactions Unit (*Unidad de Transacciones*) and the Regulations for the Operation of the Transmission System and the Wholesale Market, SIGET Decision No. E-13-99 of 19 July 1999, published in Official Journal No. 138 of 23 July 1999.

35. This legislative framework provides for the separation of the electrical industry into four parts (generation, transmission, distribution and marketing), the introduction of competition into the power generation and heavy consumption market (wholesale electricity market or WEM), and competition at the retail level through the action of marketers. Sector policies are formulated by the Electrical Energy Directorate of the Ministry of the Economy. SIGET is responsible for monitoring compliance with the provisions of international treaties on electricity and telecommunications and the laws that regulate these sectors. In particular, SIGET's responsibilities include: reviewing the terms, conditions and maximum prices of the tariff schedules applicable to the end user; establishing technical standards for the generation, transmission and distribution of electricity; examining the granting of concessions for the exploitation of hydroelectric and geothermal resources; issuing technical standards applicable to the sectors under its supervision; carrying out technical audits of the generation, transmission and distribution systems; and promoting competition.

36. Generation and distribution are open to private investment. To generate electrical energy from hydroelectric and geothermal resources it is necessary to obtain a concession from SIGET. The General Electricity Law places no limitations on the nationality or nature of the concessionaires who may therefore be foreign private investors. No concession is required for generation using other resources or for transmission, distribution and marketing activities; the enterprises merely have to be registered in SIGET's Register of Electricity Sector Operators. Transmission is currently a monopoly operated by the State-owned *Empresa Transmisora de El Salvador*. The private sector plays a part in marketing, which, however, is mainly concentrated in the hands of the State.

37. At the end of 2002, the Salvadoran electrical industry had: thirteen generating enterprises; one enterprise devoted to transmission; five distribution enterprises; four marketers of electricity; and three heavy consumers in the WEM. Moreover, the sector included one independent private entity, the Transactions Unit (UT) responsible for coordinating and operating the WEM. Its shareholders are all operators (involved in generation, transmission or distribution) and end users participating directly in the WEM. At the end of 2002, four generators, the transmission company, four distribution operators and two end users were participating in the UT.

38. Each of the distributors covers a geographical area but none of them has an exclusive supply concession. Of the five distributors (CAESS, DELSUR, AESCLESA, EEO and DEUSEM) four were privatized in 1998 with the participation of Venezuelan, Chilean and United States capital; DEUSEM was privatized at a later date. The distributors are also exporters and importers of electricity.

39. In 2001, total electrical energy production on the wholesale market was 3,647 GWh, of which 31% was generated by public enterprises and 69% by private generating companies; the net demand for electrical energy amounted to 3,956 GWh, which exceeded domestic production, the national supply being supplemented with imports from Guatemala equivalent to 309 GWh (Table IV.5). In terms of installed capacity, that same year, the private enterprises (exclusively thermal generation) exceeded the installed capacity of the public enterprises (hydroelectric and geothermal generation), bringing total installed capacity to 1,118 MW distributed as follows: thermal generation 50%; hydroelectric generation 36%; and geothermal generation 14%.

Table IV.5
Main indicators for the electrical sector, 1994-2002

	1994	1995	1996	1997	1998	1999	2000	2001	2002[a]
Installed capacity (MW) [b]	818	909	943	943	943	988	1,101	1,118	1,133
Public (%)	100	90	85	85	85	54	50	50	51
Private (%)	0	10	15	15	15	46	50	50	49
Maximum demand (MW)	566	592	626	666	694	718	758	734	748
Net demand for energy[c] (GWh)	3,064	3,236	3,361	3,636	3,775	3,889	4,074	3,956	1,942
Production (GWh)	3,075	3,271	3,340	3,548	3,737	3,638	3,377	3,647	1,811
Public (%)	100	94	80	74	75	64	56	31	31
Private (%)	0	6	20	26	25	27	44	69	69
Net imports[d] (GWh)	-11	-35	21	88	38	250	696	309	131
Average price, residential sector (US$/kWh)	0.070	0.072	0.080	0.081	0.123	0.116	0.126	0.134	0.132

a On 30 June.
b Wholesale market.
c Sum of local production and net imports of electrical energy.
d Negative net imports represent exports to neighbouring countries.

Source: Information provided by the Salvadoran authorities.

40. With regard to generation per operator in the WEM, in 2001 the State enterprise CL covered 29% of the demand, followed by the enterprises Gesal (with Italian capital) and Nejapa (United States capital) with 23 percent each, Duke (regional private enterprise) with 16%, and the Salvadoran cement producer CESSA with 1%. With respect to hydroelectric and geothermal energy there are only two generators in operation: the former State monopoly CL, which controls most of the production, and the Salvadoran enterprise *Geotérmica Salvadoreña, S.A. de C.V.* However, in October 2002, concessions were granted to four other private enterprises which are not yet in operation.

41. El Salvador is participating in the SIEPAC Project (Electrical Interconnection System for Central America) which involves the establishment and implementation of a Central American wholesale electricity market and the development of the first regional transmission system. El Salvador, together with Guatemala, Honduras, Nicaragua, Costa Rica and Panama, have approved and ratified the Framework Treaty on the Central American Electricity Market, signed in December 1996 and in force since January 1999, which is aimed at the establishment of a Regional Electricity Market (REM). The Framework Treaty opened up the national markets to the regional market for the transmission and buying and selling of electricity and created a Regional Electrical Interconnection Commission (*Comisión Regional de Interconexión Eléctrica*, CRIE), responsible for ensuring the implementation of the principles of the Framework Treaty and subsequent regulations, and a Regional Operating Body (*Ente Operador Regional*, EOR), responsible for the technical operation and commercial aspects of the regional market. Both these entities were formally set up in 2000; in October 2002, it was decided that the EOR's permanent headquarters should be in El Salvador and those of the CRIE in Guatemala.

42. The Framework Treaty grants a concession for the network-owning enterprise (*Empresa Propietaria de la Red*, EPR) to build and operate the first regional transmission system known as the SIEPAC Line. Six public electricity enterprises from each of the member countries are participating in the EPR, together with the Spanish enterprise *ENDESA*. The line will be 1,830 km long and should be completed in 2006; the estimated cost is US$320 million, 75% of which will be financed by a loan from the Inter-American Development Bank, the rest being contributed by the partners. At the end of 2002, there were interconnections between El Salvador and Guatemala and between El Salvador and Honduras.

43. The principal instrument used for regulating activity in the distribution branch is the retail end consumer tariff. For this purpose, the distribution network operators who act as marketers in the geographical area in which their networks are situated must each year submit to SIGET, for approval, a tariff schedule containing the prices and conditions of electrical energy supply according to voltage level, season and time of day. The tariff schedule fixes approved maximum prices. For this purpose, the prices are broken down into three kinds of charges: a charge for energy consumption, a charge for use of the network and a charge for customer service. SIGET regulates these two latter charges; however, the charge for energy consumption, which according to the authorities represents 70% of the price, is not regulated but determined on the wholesale market.

44. The legislative framework for the sector does not include provisions concerning end-consumer subsidies; however, the Government does grant direct subsidies focused on low-income users. In view of the shortage of resources, up to March 2001 the revenues of the public enterprise CL were indirectly tapped through discounts granted by that enterprise on invoices for energy sales to distributors. Since April 2001, these subsidies have been covered by the State through the National Electricity and Telephony Investment Fund (*Fondo de Inversión Nacional en Electricidad y Telefonía*, FINET) (see Section (iii)).

45. At present, government policy involves targeting subsidies and State resources on the expansion of coverage and on low-income consumers. The following tariff subsidies are in place: a residential consumption subsidy for monthly consumption of less than 99 kWh; a subsidy on the pumping of water for the consumption of the State enterprise ANDA and rural cooperatives. According to information provided by SIGET, in 2001, subsidies worth a total of US$26.3 million were received by 551,000 users, while the implicit ANDA subsidy amounted to some US$18 million and the subsidy on the consumption of energy for pumping water to some US$2.5 million. The tariffs for these consumers have remained unadjusted, the difference being paid by the State through FINET. According to an ECLA report, the subsidies represented a reduction of up to 76% in the electricity bill for smaller consumers and, during the period 1998-2001, total subsidies amounted to some US$167 million.[15] However, the authorities have pointed out that subsidies were reduced by more than 50% in 2001 as compared with 2000, totalling US$27 million.

(5) SERVICES

(i) Main characteristics

46. Since the previous Secretariat report there have been considerable changes in the services sector, particularly in the areas of telecommunications and financial services. In 2001, the services sector made a contribution of about 62% to total GDP. According to the breakdown of the national

[15] ECLA (2002), Central American Isthmus: the Regulation of the Distribution of Electrical Energy in Countries with Private Enterprises: the cases of El Salvador, Guatemala, Nicaragua and Panama. Available at the following address: http://www.eclac.cl/publicaciones/Mexico/6/LCMEXL536/L536.pdf, 28 August 2002.

accounts by the Central Reserve Bank, in 2001 the principal services subsectors in terms of contribution to total value added were, in decreasing order of importance: commerce; rental housing; transport and storage; construction; and financial services (Table IV.6).

Table IV.6
Contribution of the principal services sectors to GDP, 1996-2001

	1996	1997	1998	1999	2000	2001[a]
Electricity	0.3	0.3	0.3	0.3	0.3	0.6
Water and sewage	0.3	0.3	0.3	0.3	0.3	0.3
Construction	3.7	3.8	4.0	3.8	3.6	3.9
Commerce	16.7	16.7	16.8	16.5	16.7	16.7
Restaurants and hotels	3.1	3.1	3.2	3.1	3.1	3.1
Transport and storage	5.6	5.7	5.8	5.7	5.8	5.8
Communications	1.9	2.0	1.9	2.4	2.7	2.8
Banks, insurance and other financial institutions	3.0	3.2	3.4	3.7	3.8	3.8
Real estate and business services	3.3	3.3	3.4	3.2	3.2	3.2
Rental housing	9.0	8.8	8.7	8.4	8.4	8.0
Community, personal and social services	3.6	3.6	3.5	3.4	3.4	3.4
Domestic services	1.9	1.8	1.7	1.7	1.7	1.6
Government services	5.8	5.8	5.6	5.5	5.4	5.4
Industrial and *maquila* services	1.6	2.1	2.4	2.5	3.0	3.1
Total	59.8	60.5	61.0	60.5	61.4	61.7

a Preliminary figures.

Source: BCR.

47. El Salvador's Schedule of Specific Commitments under the WTO's General Agreement on Trade in Services (GATS) includes commitments relating to six of the twelve categories of services (Table IV.7).[16] As regards horizontal commitments, the Schedule of Specific Commitments establishes the following limitations applicable to foreign investment: net profits obtained in each financial year from commercial and services activities may be remitted abroad in amounts of up to 50% of the registered investment; and payments for rights to use foreign trademarks and patents, technical assistance and other similar services may be remitted freely, provided the value does not exceed 10% of net sales. Moreover, in accordance with the provisions of the Investment Law (see Chapter II(3)), the Schedule stipulates that small-scale trade, industry and provision of services are reserved exclusively for persons who are nationals of El Salvador by birth, and foreigners may not hold the positions of administrator, director, manager or representative of such enterprises. In addition, unless specially authorized by the Ministry of Labour and Social Security, every employer must employ Salvadoran nationals in a proportion of at least 90% of the personnel of his enterprise, and the amount of wages received by Salvadorans may not be less than 85% of the total wages paid.

48. The authorities have pointed out that the limitations on the repatriation of foreign capital and the prohibition on foreign investors holding directorships contained in El Salvador's Schedule of Commitments corresponded to the legislation in force at the time that the Schedule was negotiated and were expressly abolished by the 1999 Investment Law.

49. El Salvador's Schedule of Specific Commitments includes MFN exemptions for all sectors in favour of the member countries of the Central American Common Market (CACM). Moreover, for financial services, El Salvador incorporated exemptions from MFN treatment in favour of Honduras and Nicaragua on the basis of the Convention on Facilitating the Financial Integration of Countries of the Central American Isthmus.[17]

[16] WTO document GATS/SC/29 Supp.1 and 2, of 11 April 1997 and 26 February 1998, respectively.

[17] WTO document GATS/EL/29, of 15 April 1994.

Table IV.7
Summary of El Salvador's commitments under the GATS[a]

	Market access				National treatment			
Modes of supply:								
Cross-border supply	**1**				**1**			
Consumption abroad		**2**				**2**		
Commercial presence			**3**				**3**	
Presence of natural persons				**4**				**4**
Commitments (■ full; ◨ partial; □ no commitment; - does not appear in Schedule)								
Horizontal[b]	□	□	◨	◨	◨	◨	◨	◨
Sector-specific commitments								
1. Business services								
A. Professional services								
a. legal [c]	■	■	■	◨	■	■	■	□
b. accounting [c]	□	□	■	□	□	□	■	□
c. tax advisory [c]	□	□	■	□	□	□	■	□
d. architectural [c]	■	■	■	□	■	■	■	□
e. engineering [c]	■	■	■	□	■	■	■	□
B. Computer and related services, solely:								
c. data processing [c]	■	■	■	□	■	■	■	□
C. Research and development services	–	–	–	–	–	–	–	–
D. Real estate services	–	–	–	–	–	–	–	–
E. Rental/leasing services without operators								
c. rental/leasing of vehicles [c]	□	■	■	□	□	■	■	□
F. Other business services								
a. advertising [c]	□	□	■	□	□	□	■	□
2. Communication services								
A. Postal services	–	–	–	–	–	–	–	–
B. Courier services	–	–	–	–	–	–	–	–
C. Telecommunications services, solely:								
a. voice telephony	■	■	◨	■	■	■	■	■
b. packet-switched data transmission	■	■	◨	■	■	■	■	■
c. circuit-switched data transmission	■	■	◨	■	■	■	■	■
d. telex	■	■	◨	■	■	■	■	■
e. telegraph	■	■	◨	■	■	■	■	■
f. facsimile	■	■	◨	■	■	■	■	■
g. private leased circuits	■	■	◨	■	■	■	■	■
o. other [c]	■	■	◨	■	■	■	■	■
D. Audiovisual services	–	–	–	–	–	–	–	–
3. Construction services	–	–	–	–	–	–	–	–
4. Distribution services	–	–	–	–	–	–	–	–
5. Educational services	–	–	–	–	–	–	–	–
6. Environmental services [c]	□	□	◨	□	□	□	□	□
7. Financial services								
A. Insurance and related services	–	–	–	–	–	–	–	–
B. Banking and other financial services, solely:								
a. Acceptance of deposits and other funds [c]	□	□	◨	□	□	□	□	□
b. Loans of all types [c]	□	□	◨	□	□	□	□	□

	Market access				National treatment			
Modes of supply:								
Cross-border supply	**1**				**1**			
Consumption abroad		**2**				**2**		
Commercial presence			**3**				**3**	
Presence of natural persons				**4**				**4**
C. Other	□	□	◨	□	□	□	□	□
8. Health and social services	–	–	–	–	–	–	–	–
9. Tourism and travel related services								
A. Hotels and restaurants								
a. Hotel and other lodging [c]	□	■	■	□	□	■	■	□
b. Meal serving [c]	□	■	■	□	□	■	■	□
B. Travel agencies and tour operators [c]	□	□	■	□	□	□	■	□
C. Tourist guides services	□	□	■	□	□	□	■	□
D. Other	–	–	–	–	–	–	–	–
10. Recreational and sporting services	–	–	–	–	–	–	–	–
11. Transport services								
A. Maritime	–	–	–	–	–	–	–	–
B. Inland waterway	–	–	–	–	–	–	–	–
C. Air								
d. Maintenance and repair services	■	■	◨	□	■	■	■	□
D. Space	–	–	–	–	–	–	–	–
E. Rail	–	–	–	–	–	–	–	–
F. Road	–	–	–	–	–	–	–	–
G. Pipeline	–	–	–	–	–	–	–	–
H. Auxiliary	–	–	–	–	–	–	–	–
I. Other	–	–	–	–	–	–	–	–
12. Other services	–	–	–	–	–	–	–	–

a The only authentic source of information concerning these commitments is El Salvador's Schedule of Specific Commitments as set out in documents GATS/SC/29 (15 April 1994), GATS/SC/29/Suppl.1 (11 April 1997) and GATS/SC/29/Suppl.2 (26 February 1998).
b Applicable only to the services included in El Salvador's Schedule of Commitments.
c Not applicable to all the subdivisions of the category (for more details see El Salvador's Schedule of Commitments).

Source: WTO Secretariat.

(ii) Financial services

(a) Structure and performance

50. In 2001, the financial services sector (including insurance services) made a contribution of 3.8% to total GDP.[18] The sector is composed of entities distributed among the following categories: commercial banks; stock market entities (securities exchanges, stockbrokers, and companies specializing in the deposit and custody of securities); foreign exchange dealers; forecasting entities; public warehouses; financial intermediaries (cooperatives, federations, and savings and loan societies); public credit institutions; and insurance and guarantee entities.

[18] Preliminary estimate published by the Central Reserve Bank (2002), Quarterly Review, October-November-December 2001.

51. The financial system is supervised by the following bodies: the Financial System Superintendency (*Superintendencia del Sistema Financiero*, SSF); the Securities Superintendency (*Superintendencia de Valores)*; and the Pensions Superintendency (*Superintendencia de Pensiones*). The functions of the SSF include: ensuring compliance with the laws, regulations and other legal provisions applicable to the Central Reserve Bank of El Salvador and other entities under its supervision; issuing rules governing the functioning of the institutions under its control; authorizing the establishment, operation and closure of the banks, insurance companies and other financial entities designated by law; ensuring the transparency of information; applying sanctions; and intervening in financial sector entities in difficulty. The Securities Superintendency is responsible for overseeing compliance with the provisions applicable to stock market entities and facilitating the development of the securities market, while the Pensions Superintendency oversees the pension system. At the same time, the Central Reserve Bank is responsible for ensuring that the payment systems function normally.

(b) Multilateral commitments

52. El Salvador participated in the financial services negotiations and accepted the Fifth Protocol annexed to the GATS, incorporating it into its legislation by means of Legislative Decree No. 653 of 13 March 1999, published in Official Journal No. 97 of 26 May 1999. There are some differences between the scope of the commitments undertaken on the basis of these negotiations and those undertaken in the context of the Uruguay Round. For example, with respect to commercial presence in the banking sector, in the Uruguay Round El Salvador undertook to grant access to foreign financial institutions through the establishment of branches or participation in the ownership of domestic banks and finance houses limited to a maximum of 50%. In the new offer this level was increased to 75% for prime foreign financial institutions subject to prudential regulation and supervision in their countries of origin. However, the maximum percentage that foreign natural persons may acquire was reduced from 50 to 25%. Moreover, the initial Schedule limited the holding of shares by a natural or legal person to a maximum of 5% of the capital per institution, whereas in the new Schedule this requirement was eliminated and replaced with a provision allowing a natural or legal person to hold shares representing more than 1% of the capital of a financial institution only with the approval of the SSF.[19] At the same time, the most recent Schedule only includes commitments with respect to measures of the type specified in Article XVI:2 (f) of the GATS (limitations on the participation of foreign capital) and does not explicitly include the possibility of access through branches.

53. El Salvador did not include insurance services in its GATS commitments resulting from either the Uruguay Round or the Fifth Protocol negotiations.

(c) Banking

Characteristics and performance

54. On 30 June 2002, the Salvadoran banking sector consisted of 13 operating banks (including a subsidiary of a foreign bank, two State banks and two branches of foreign banks) and one finance house authorized to accept funds from the public.[20] Of the shareholders in the entities covered by the Banks Law established in El Salvador (that is to say, excluding the two branches of foreign banks)

[19] WTO document GATS/SC/29/Suppl.2 of 26 February 1998.

[20] In addition to the entities mentioned, there is a bank in process of liquidation, *Banco CREDISA*, which has not been included in the figures given in this Section.

52% were Salvadoran natural or legal persons, 31% were Central American persons and 17% were persons from other countries, among which the largest investors were banks from Canada, the United States and Germany. Four banking entities were controlled by foreign shareholders: two by Nicaraguan shareholders, one by Canadian shareholders and another by Panamanian shareholders. In 2001, under cover of the new Banks Law, the establishment or regularization plans for the adaptation of a number of financial conglomerates, as defined in the new Law (see below), were approved.

55. In addition to the entities authorized to accept funds from the public, the Salvadoran financial sector includes entities authorized to carry out active operations; on 31 December 2001, these entities included four branch offices of foreign institutions, operating as information centres or placing funds in El Salvador in the form of loans or investments, and 11 public credit institutions.

56. On 30 June 2002, the total assets of the banking system amounted to US$9,082 million mainly distributed among loan portfolios (57.6% of total assets), financial investments (19%) and liquid assets (12.64%); liabilities amounted to US$8,278 million and were mainly distributed between deposits (77.8% of total liabilities) and loans (15.3%).

57. Since 1998, the banking sector's loan portfolio has not been very dynamic, especially since 2001, despite the fall in interest rates (Table IV.8). Deposits increased in line with the trend in economic activity up to 2001, but then declined in the first half of 2002, in line with the banks' increasing interest, following the entry into force of the Law on Monetary Integration, in raising funds abroad (see below).

Table IV.8
Evolution of net loan portfolio and deposit taking, 1997 – June 2002
(US$ million)

	1997	1998	1999	2000	2001	2002 (June)
Loans	4,556	5,052	5,132	5,120	5,118	5,229
Deposits	5,083	5,481	5,894	6,189	6,503	6,435

Source: Financial System Superintendency (2002), Statistical Bulletin: Banks, April - June 2002. Available online at the following address: http://www.ssf.gob.sv/.

58. Although the volume of credit increased slightly in the first half of 2002, the increase (2.2% relative to December 2001) was modest considering the substantial reduction in interest rates which, as a result of the Law on Monetary Integration, fell, in the case of loans with a term of up to one year, from 9.6% in June 2001 to 6.9% in June 2002 and, in the case of loans with a term of more than year, from 11.4 to 8.2%. The banks are therefore in a very liquid situation, which has led them to place funds abroad in the form of loans and investments in foreign government sovereign bonds.[21] The SSF notes that the banks are seeking new users via regional expansion through financial conglomerates and the opening of representative offices in other countries.

59. Despite the fall in interest rates, the sluggish domestic credit market, together with the dollarization of the economy, has also led the banks to raise long-term funds more cheaply on the international market and to take less interest in attracting savings on the domestic market. Another consequence of the weakness of the demand for credit has been that the banking system has built up unnecessarily large reserves of liquidity. At the end of June 2002, reserves totaled US$1,384.7 million, as compared with required reserves of 1,367.9 million.

[21] Financial System Superintendency (2002), Statistical Bulletin: Banks. Available at the Internet address http://www.ssf.gob.sv/.

60. According to a study published in 2000, between 1987 and 2000 the credit asset quality indicators for the Salvadoran banking industry tended to deteriorate, in particular as a result of the operations of the State banks, especially the Agricultural Development Bank.[22] In order to improve the solvency of the Salvadoran banking system, the new Banks Law (see below) established stricter solvency requirements. In principle, the banks must always maintain a ratio of at least 12% between their capital base and their total risk-weighted assets. In practice, to meet this solvency requirement, provision has been made for a transition period with an interim target of 9.6% for the year 2000 and a series of further increments until the objective of 12% is achieved in 2005.

61. The Salvadoran banking system has made considerable progress towards this goal. On 30 June 2002, the base capital requirement with respect to the system's weighted assets was 11.85%, i.e. above the legal limit of 10.5% for 2002. On the same date, loans in default amounted to US$211.8 million or 3.9% of the total, an improvement on the levels for December 2000 due to the fall in interest rates and the rescheduling of coffee sector debt (see below).[23] The bad debt provisions are sufficient to provide more than 100% cover.

62. With respect to the situation at the Agricultural Development Bank, the authorities have pointed out that at present it is under the disciplines of the Banks Law and is completing the process of transition from being a bank that receives a certain amount of State support into a bank that has to compete with others. The transition process includes cutbacks in personnel and the number of branches and the sale of assets. However, on 30 June 2002, the percentage of delinquent loans (23.8%) was still high and the cover (58.7%) low. In 2002, the Agricultural Development Bank began granting loans again.

63. In recent years, an important aspect of financial policy was the establishment, in 2001, of the Environmental Trust for the Conservation of the Coffee Forest (FICAFE). The participating banks: Agrícola, Cuscatlán, Salvadoreño, Comercio, Hipotecario and the Agricultural Development Bank have contributed US$250.2 million of loan portfolios to the Trust in exchange for bonds. FICAFE has a US$40 million government guarantee. Through the Trust and thanks to the government guarantee, the loans have been restructured so as to offer longer terms and considerably lower interest rates. In June 2002, total coffee sector debt amounted to US$273.3 million. Although the creation of FICAFE constituted a form of risk reduction for the financial system, the persistently low level of international coffee prices, far below that envisaged when the Trust was set up, has increased the probability of some of the loans being written off.

Legislative framework

64. Since the last El Salvador trade policy review, the Salvadoran financial system has undergone substantial changes, especially in the legislative area, with the adoption of the new Banks Law and the Non-Banking Financial Intermediaries Law (Table IV.9). Another significant development was the entry into force, in 2001, of the Law on Monetary Integration which paved the way for the transition to a dollarized economy (Chapter I).

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[22] Lemus Gómez, R. (2000), The banking industry in the nineties, Research Series No. 2000-1, FUSADES, 2000.

[23] In December 2000, delinquent loans totalled US$268.6 million or 5% of total loans. In December 2001, total delinquent loans had fallen to US$216.9 million or 4.2% of total loans. Financial System Superintendency, Financial Accounts and Indicators December 2001. Available at the Internet address http://www.ssf.gob.sv/cont/pub/anuariob01/iii.doc.

65. The Banks Law stipulates that all banks established in El Salvador must be organized and operate as closed-end public limited companies with their capital divided into registered shares held by not less than ten shareholders. At least 51% of the shares must be owned by investors of the following types: Salvadoran or Central American natural persons; Salvadoran legal persons whose shareholders or majority members are Salvadoran or Central American natural persons or other Salvadoran legal persons; foreign banks and other financial institutions which are subject in their country of origin to prudential regulation and supervision in accordance with international practice and are classified as prime names by internationally recognized rating agencies. The SSF maintains a Register of Prime Foreign Banks and Financial Institutions which, in the second half of 2002, was made up of 50 banks from Canada, Chile, Costa Rica, Germany, Guatemala, Italy, Netherlands, Panama, Spain, Switzerland, United Kingdom, United States and Venezuela.[24]

Table IV.9
Main financial system legislation

Title of law	Date of entry into force (publication)	Description
Non-Banking Financial Intermediaries Law	31 March 2001	Regulates the organization, operation and financial intermediation activities of cooperative savings and loan societies and associations which accept funds from the public, as well as Federations.
Law on Monetary Integration	1 January 2001 (22 December 2000)	Makes the US dollar unlimited and unrestricted legal tender and fixes the colon-dollar exchange rate at 8.75.
Banks Law	8 October 1999 (30 September 1999)	Establishes the legal framework for the operation of the banks based on international principles of banking regulation and supervision. Also establishes mechanisms for the consolidated supervision of financial conglomerates. Creates the Deposit Guarantee Institute (*Instituto de Garantía de Depósitos*).
Organic Law of the Pensions Superintendency	1 January 1997	Creates the public law institution responsible for supervising and monitoring compliance with the legal provisions applicable to the operation of the pensions savings system, the public pensions system and the pensions system for the administrative institutions.
Pension Savings System Law	1 January 1997 (23 December 1996)	Creates the pensions savings system for administering the funds for paying benefits to members to cover the risks of disability, old age and death.
Insurance Companies Law	5 December 1996 (4 November 1996)	Regulates the establishment and operation of insurance companies and the participation of intermediaries.
Organic Law of the Securities Superintendency	13 October 1996 (4 October 1996)	Creates the specialized public law institution responsible for overseeing and regulating the securities market and its various participants.
Multisectoral Investment Bank (BMI) Establishment Law	5 June 1994 (27 May 1994)	Establishes the BMI as a public credit institution with legal personality and its own resources to promote the development of private sector investment projects by providing medium and long-term financing.
Securities Market Law	30 April 1994 (21 April 1994)	Establishes the legal and institutional framework for the operation of the securities market.
Organic Law of the Central Bank of El Salvador	12 May 1991 (3 May 1991)	Grants the Central Reserve Bank institutional autonomy and assigns it, *inter alia*, the priority tasks of ensuring the normal operation of the payment systems and fostering a competitive and solvent financial system.
Organic Law of the Financial System Superintendency	19 December 1990 (10 December 1990)	Regulates the activities of the Superintendency in its capacity as overseer of the financial system and grants it administrative and budgetary autonomy in the performance of its functions, while investing it with powers to regulate the system and sanction non-compliance.
Foreign Exchange Dealers Law	15 April 1990 (6 April 1990)	Regulates the authorization and operations of companies routinely engaged in the buying and selling of foreign currencies, while granting the Central Bank powers to authorize their operations and the SSF powers to oversee them.
Small-Enterprise Finance Company and Guarantee Fund (FIGAPE) Law	16 June 1973 (7 June 1973)	Creates an autonomous credit and guarantee institution for small traders and manufacturers.
Social Fund for Housing Law	15 June 1973 (6 June 1973)	Establishes the Social Fund for Housing as a credit institution.

[24] Information available online at: http://www.ssf.gob.sv/.

Title of law	Date of entry into force (publication)	Description
Agricultural Development Bank Law	4 May 1973 (25 April 1973)	Creates the official credit institution known as the Agricultural Development Bank, whose fundamental objectives are to create, promote and maintain financial facilities for contributing to agricultural development and to act as financial agent for the organizations responsible for implementing rural welfare and agrarian structural reform programmes.
Commercial Code	1 April 1971 (31 July 1970)	Regulates the activities of traders, commercial transactions and commercial affairs, thus constituting the basis of the financial legal system and, ultimately, one of the main pieces of supplementary legislation.

Source: Central Reserve Bank of El Salvador, available at www.bcr.gob.sv/finan002.htm.

66. No natural or legal person, either directly or through an intermediary, may hold shares in a bank that represent more than 1% of the institution's capital, without the prior authorization of the SSF. The minimum capital required to establish a bank in El Salvador is US$11 million.

67. Subject to authorization by the SSF, foreign banks may establish branches in El Salvador to carry out the same operations as domestic banks. Likewise, subject to authorization, foreign banks may open offices to serve as information centres for their customers or for placing funds in the country in the form of loans or investments, without engaging in deposit operations in the national territory. In both cases, authorization is granted for a period of two years which can be extended for further identical periods. Under the Law, depositors and creditors domiciled in El Salvador have preferential rights over assets owned by a foreign financial institution in El Salvador.

68. With respect to national treatment, the Banks Law stipulates that, except where the law provides otherwise, the branches and offices of foreign financial institutions operating in El Salvador shall enjoy the same rights and privileges, be subject to the same laws and be governed by the same rules and regulations as apply to domestic banks. The authorities have pointed out that at present there is no legislation providing for the non-application of national treatment to foreign institutions.

69. The Banks Law also establishes mechanisms for the consolidated supervision of financial conglomerates by the SSF. A financial conglomerate is defined as a group of companies characterized by the fact that more than 50% of their shareholders' capital is owned by a holding company, which is also a member of the conglomerate. Nevertheless, the SSF may agree to a bank established abroad forming part of a conglomerate, provided that the holding company owns at least 45% of the shares of the bank in question and a number of specific prudential requirements are met.

70. The holding company may be a company whose exclusive purpose is to invest in more than 50% of the capital of financial entities, or a bank established in El Salvador. In the first case, the holding company may hold minority investments, totalling not more than 25% of its base capital, in the shares of Salvadoran institutions that administer pension funds. However, if the holding company is a bank, neither that bank nor its subsidiaries may invest in the share capital of pension fund administering institutions or of insurance companies. Holding companies are subject to supervision by the SSF, which is allowed access to their information for the purpose of supervising the conglomerate as a whole.

71. Apart from the holding company, a conglomerate may consist of a bank and one or more financial sector entities such as insurance companies, institutions that administer pension funds, stockbrokers, companies specializing in security deposit and custody, credit card companies, foreign exchange dealers, leasing companies, and public warehouses, including their subsidiaries, duly overseen by the SSF or by the appropriate supervisory body.

72. Salvadoran banks more than 50% of whose shares are owned by a foreign financial entity (banks or financial conglomerates) may only share names, assets and infrastructure or offer joint services to the public with other companies of the same conglomerate if the aforementioned entity establishes a subsidiary holding company in El Salvador. Foreign banks and financial institutions that establish agencies or branches in El Salvador and whose parent companies or companies of the financial conglomerate to which they belong own more than 50% of other financial sector companies in El Salvador, may operate in the same way as a financial conglomerate without having to establish a subsidiary holding company in the country.

73. Another important change introduced by the Banks Law was the creation of the Deposit Guarantee Institute to guarantee the public's deposits in the event of the winding up of a bank or its compulsory liquidation and to assist with the restructuring of banks with solvency problems. The Institute's assets consist mainly of a one-off contribution of 250 million colons from the Central Bank and the premiums paid by the member banks. The maximum cover for deposits is US$6,285; all private banks must be members of the Institute, with the exception of subsidiaries of foreign banks if the deposits are guaranteed in the country in which those banks are established. As far as State banks are concerned, the El Salvador Mortgage Bank (*Banco Hipotecario*) is subject to the same deposit insurance regime as a private bank, but in the case of the Agricultural Development Bank the guarantee is provided by the State.

74. Article 20 of the Law on Monetary Integration introduced, as from 1 January 2001, new provisions relating to the liquidity reserves that the banks must maintain. Under this Law, the SSF establishes a liquidity reserve which, in proportion to their deposits and liabilities, the banks have to maintain and which is administered by the Central Reserve Bank of El Salvador. For 2001 and 2002, the liquidity reserve of each bank may consist of US dollar deposits in the Central Reserve Bank or of securities issued by the latter in the same currency. From 2003 onwards, the reserve may also be invested abroad, in deposits with prime banks or in highly liquid low-risk securities. The Law stipulates that a weighted average of 20% of deposits must be maintained as a liquidity reserve, and that the average liquidity reserve should not be more than 25% of deposits.

75. The implementation of the liquidity reserve requirements is governed by Regulations NPB3-06 "Regulations for the Calculation and Use of the Liquidity Reserve on Deposits and Other Liabilities". The SSF is responsible for verifying compliance with the reserve requirements, as well as for determining the daily surpluses and shortfalls and providing the Central Reserve Bank with information on the liquidity situation of each bank. The liquidity reserve is deposited in the Central Reserve Bank, 50% in the form of a sight deposit and 50% of the form of investment in nonnegotiable securities issued by the Central Bank, and is remunerated. The Central Reserve Bank will receive a commission for administering this reserve. The first 25% of the funds maintained under the new reserve mechanism is available without the payment of interest, whereas the second tranche of 25% is subject to the collection of a fee proportional to the funds by the Central Reserve Bank. The disbursement of funds from the remaining 50% requires the approval of the SSF.

(d) Insurance

Characteristics and performance

76. On 30 June 2002, El Salvador had 20 insurance companies of which 18 were fully operational and two were in process of liquidation. The shares of these 20 companies were distributed as follows: 86.4% of the shares were owned by Salvadoran persons, 0.2% by persons from countries in the Central American area, and the remaining 13.4% by persons from other countries, among which the biggest investors were Spain with 7.9% and the United States with 3.5%. Only two of these

enterprises were controlled by foreign investors. The State does not participate in the insurance sector. In October 2002, after the two companies mentioned above had been liquidated, the number of insurers fell to 18.

77. According to the SSF, in 2002, the solvency situation of the insurance system, even though it had experienced a number of difficulties, was acceptable.[25] Despite the claims which it had had to pay out for the earthquakes that occurred at the beginning of 2001, the sector's profits were 18.4% higher than those for the previous year, while the profits recorded in the first half of 2002 were one-third higher than those for the same period of the previous year. The insurance companies received claims for US$328.5 million for the total losses caused by the earthquakes of 2001.[26] By 30 June 2002 almost 95% of these claims had been paid. According to information provided by the SSF, the resulting loss for the insurance system was of the order of US$6.4 million.

78. Despite the fact that the sector's losses were limited, one negative effect of the earthquakes was an increase in the price of international reinsurance and a reduction in the coverage and exclusion of some risks. This was reflected in a generalized increase in premiums, which in its turn led to a fall in the number of customers and a decline in policy renewals. Overall, the rise in premiums offset the fall in volume and made possible an increase in profits.

79. As a result of the legislative changes introduced with respect to financial conglomerates, the structure of the insurance sector has changed considerably through a process of acquisitions and mergers and conglomerate formation. In May 2002, the SSF approved the acquisition of a majority of the shares in the companies Seguros Universales, S.A. Seguros de Personas and Compañía Mundial de Seguros, S.A. by the company Corporación Excelencia, S.A. of C.V.

Legislative framework

80. Insurance activities are regulated by the Insurance Companies Law of 1997. This Law requires insurance companies established in El Salvador to be organized and to operate in the form of closed-end public liability companies of indefinite duration with their capital divided into registered shares. As distinct from the banks, the Law does not require a minimum number of shareholders. However, no natural or legal person may, either directly or through an intermediary, own shares in an insurance company that represent more than 1% of the company's capital, without the prior authorization of the SSF.

81. At least 75% of the shares of insurance companies must be held, individually or collectively, by the following classes of persons: Salvadoran or Central American natural or legal persons, or Central American or other foreign insurance or reinsurance companies. Foreign companies outside the Central American area must have prime ratings as established by the SSF on the basis of the ratings awarded by internationally recognized rating agencies. The cross-border supply of insurance services is not permitted.

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[25] According to information provided by the SSF, based on a risk analysis by two international risk classifiers, the Salvadoran insurance companies fall between categories EAA (very high capacity to meet their obligations on the terms and within the periods agreed, strong protection factors and modest risk) and EBBB- (adequate payment capacity, adequate protection factors).

[26] Financial System Superintendency (2002), Statistical Bulletin: Insurance, April-June 2002. Available at the following address: http://www.ssf.gob.sv/.

(iii) Telecommunications

82. The telecommunications sector has undergone considerable changes in recent years, especially since the privatization of the State-owned company National Telecommunications Administration (*Administración Nacional de Telecomunicaiones*, ANTEL) and the adoption of a new legislative framework. The privatization of ANTEL was regulated by the Law Privatizing the National Telecommunications Administration (Decree No. 53 of 24 July 1997, published in Official Journal No. 143 of 7 August 1997). ANTEL was divided into two entities, the Telecommunications Company of El Salvador (*Compañía de Telecomunicaciones de El Salvador*, CTE), devoted mainly to wire-based telephone services, and the International Telecommunications company (*Internacional de Telecomunicaciones*, INTEL), devoted mainly to wireless telephone services. Control of CTE was acquired by *France Telecom* at auction; the State continues to hold the equivalent of 43% of the company's share capital. The authorities have pointed out that the aim is to privatize the enterprise completely. For its part, INTEL was acquired at auction by a consortium led by *Telefónica de España*.

83. From the outset, both companies have had to compete with other operators in the market. In May 2002, El Salvador had 9 fixed line operators (AESTEL, Cablevisa, CTE, EMETEL, GCA, SALNET, SALTEL, Telefónica and Telemóvil) and four mobile telephone operators (CTE Personal, Telefónica, Telemóvil and DIGICEL). CTE controlled 90% of the fixed telephone lines, while in mobile telephony the principal operator was Telemóvil (45% of subscribers) followed by Telefónica (29%), CTE Personal (23%) and DIGICEL (3%).

84. Communications sector value added increased considerably in real terms between 1998 and 2001; in terms of contribution to total value added, the telecommunications sector, together with the postal services sector, contributed 2.8% in 2001 as compared with 1.9% in 1998. With respect to infrastructure, the trend in the indicators has likewise been accelerating: the number of fixed lines rose from some 387,000 in 1988 to more than 709,000 in May 2002; meanwhile, the number of subscribers to the cellular mobile telephone system rose from 137,000 to about 908,000 during the same period. Moreover, the standard-of-service indicators provided by the Electricity and Telecommunications Supervisory Authority (SIGET) point to an improvement in the situation. However, the tariffs have increased for both local and national calls in the case of fixed telephony and have remained unchanged since 1999 in the case of mobile telephony. At the same time, the tariffs for long-distance calls have fallen considerably in recent years (Table IV.10).

Table IV.10
Telecommunications indicators

Size and quality of the telephone network	1998	1999	2000	2001	2002[d]
Telephone lines in operation	386,659	495,340	625,785	649,879	709,394
Total capacity of local telephone exchanges (number of users)	523,294	603,761	711,737	2,945,774	..
Main lines connected to digital exchanges (%)	84	88	100	100	..
Number of coin-operated public telephones	4,926	..	..	1,754	..
Number of prepaid card-operated public telephones	..	21,715	22,075	16,916	..
Number of subscribers to the cellular mobile phone system	137,114	511,365	743,628	857,782	908,227
Number of telex subscriber lines	467	358	393	1,079	..
Number of leased circuits	..	60	190	184	..
Subscribers to public data networks	..	500	1,865	2,131	..
Standard of service					
Outstanding applications for residential telephone lines	174,163	103,617	72,566	37,991	..
Outstanding applications for business telephone lines	..	..	..	256	..
Telephone service faults repaired the next working day (%)	..	..	76	79	..

Size and quality of the telephone network	**1998**	**1999**	**2000**	**2001**	**2002[d]**
Number of telephone service faults reported by users	..	..	..	234,073	..
Peak-hour calls not completed (%)	..	..	5	11	..
Operator services responding within 15 seconds (%)	..	..	91	87	..
Traffic[a]					
Local telephone traffic[b]	45,947	2,787,143	3,3345,513	3,492,329	..
National telephone traffic[b]	9,170	313,617	474,282	814,111	..
International telephone traffic (incoming)	223,524	398,284	710,330	801,918	..
International telephone traffic (outgoing)	38,843	53,562	138,815	157,673	..
Tariffs[c] (US$)					
Charge for installing telephone service	335,77	335,77	335,77	335,77	..
Basic monthly charge, residential	6,84	7,13	7,13	8,12	9,43
Basic monthly charge, business	13,69	14,21	14,21	14,21	16,14
Cost per local minute (US cents)	1,94	2,01	2,29	2,29	2,65
Cost per national minute (US cents)	3,23	3,36	3,82	3,82	4,45
Cost per minute for calls from fixed to mobile	0,02	0,23	0,23	0,23	0,23
Cost per minute for international calls (United States only) during business hours	0,80	0,48	0,25	0,25	0,25
Investments					
Total annual investment in telecommunications, including land and buildings (US$ million)	477	711	877	163	..

.. Not available.

a In thousands of minutes.
b Not including CTE traffic for 1998.
c VAT included (tariffs applied by the responsible operator).
d Data obtained up to May 2002.

Source: Electricity and Telecommunications Supervisory Authority, Telecommunications Manager's Office, Indicator Handbook. Available at the following address: http://www.siget.gob.sv/, 29 July 2002.

85. The legislative framework for the telecommunications sector consists mainly of the following laws and regulations: the Telecommunications Law (Legislative Decree No. 142, of 6 November 1997, published in Official Journal No. 218, of 21 November 1997), its amendments (Legislative Decree No. 87, of 27 April 2001, published in Official Journal No. 90 of 16 May 2001) and its Regulations (Legislative Decree No. 64 of 15 May 1998); the Law Establishing the General Superintendency for Electricity and Telecommunications (Legislative Decree No. 808, of 12 November 1996, published in Official Journal No. 189, 9 October 1996), its amendments (Legislative Decree No. 175, of 4 December 1997, published in Official Journal No. 239 of 22 December 1997) and its Regulations (Executive Decree No. 56 of 13 May 1998, published in Official Journal No. 88 of 15 May 1998); and the Law on the National Electricity and Telephony Investment Fund (Legislative Decree No. 354 of 29 July 1998, published in Official Journal No. 142 of 29 July 1998) and its amendments (Legislative Decree No. 859 of 30 May 2002, published in Official Journal No. 115 of 24 June 2002).

86. The Ministry of the Economy is responsible for formulating telecommunications policy, while the General Electricity and Telecommunications Superintendency (SIGET), an autonomous entity assigned to the Ministry of the Economy, is the institution responsible for applying and monitoring compliance with the sector's rules and regulations. SIGET is also responsible for administering, managing and overseeing the radio-frequency spectrum, which is owned by the State.

87. The Law on Telecommunications (LT) applies to the activities of the telecommunications sector and, in particular, the regulation of the public telephone service, the use of the radio-frequency

spectrum, access to essential resources and the numbering system, including the allocation of codes for accessing the multi-carrier system. The objectives of the LT include: facilitating access to telecommunications for all sectors of the population; protecting the rights of users and providers of telecommunications services; ensuring the rational and efficient use of the radio-frequency spectrum; and developing a competitive telecommunications market at all levels.

88. The LT requires the prices and conditions of telecommunications services to be negotiated freely between operators, except as regards access to essential resources. Operators interested in providing public telephone services must apply to SIGET for a concession to operate the service, which, provided that they comply with the registration requirements laid down, will be automatically granted, once they are registered, for a period of 30 years without any limitation as to number or location, it being possible for there to be more than one concession in the same geographical area.

89. The maximum public telephone service tariffs are determined and approved by SIGET in accordance with the provisions of the LT. The latter provides for the maximum access charges to be those applied by the operators the day before the entry into force of the LT and stipulates that from that date up to and including the year 2002 these prices may be adjusted annually by SIGET by the same percentage as the Consumer Price Index (CPI) published by the Ministry of the Economy. The Law also provides that up to 2002, inclusive, telephone network operators that control less than 10% of a particular market or service and are not linked by crossholdings with any other operator, may opt to request SIGET to approve their own maximum tariffs on the basis of their real costs or accept the maximum tariffs that SIGET has approved for other operators.[27] Starting in 2003, SIGET was to have adjusted the maximum telephone tariffs on the basis of an index that depended 50% on the CPI and 50% on the rate of depreciation of the colon in relation to the dollar.[28] This ceased to apply with the Law on Monetary Integration although, according to the competent authority, the indexation mechanism which will be used to replace it is still being studied.

90. To encourage investment in new telephone lines, the LT authorized SIGET to conclude five-year investment contracts with the access network operators controlling more than 10% of the market in which targets for the installation of new lines are agreed. In return, when the maximum tariffs for national services are approved, tariff adjustments additional to those previously mentioned may be introduced. In this connection, it is provided that, from the beginning of the investment contract, SIGET may approve an additional percentage increment for the maximum charges for access and additional telephone services equal to the growth of the telephone network of the operator concerned, up to a maximum of 15% in the first year, and 20% in each of the remaining four years, subject to certain time limitations. A contract of this type was signed with CTE in 1998 and was in force at the end of 2002. The authorities have pointed out that, in practice, under these arrangements tariffs increased by an amount less than that permitted by the LT.

[27] Information on the maximum tariffs applicable in the current year is available online at SIGET's Internet address: http://www.siget.gob.sv/.

[28] Up to 2002 the following adjustment formula was applied: $P_1 = (P_0) \cdot (IPC_1/IPC_0)$, while from 2003 the formula will be: $P_1 = (P_0/2) \cdot ((IPC_1/IPC_0) + (XR_1/XR_0))$, where: P_1 is the value of each maximum charge from the date of indexation; P_0 is the value of the same maximum charge corresponding to the reference date or the immediately preceding indexation date; IPC_1 is the consumer price index from the first day of indexation; IPC_0 is the consumer price index on the immediately preceding indexation date; XR_1 and XR_0 are the exchange rates for current money in El Salvador against the US dollar from the first day of indexation and on the immediately preceding indexation date, respectively. From 2001, under the Law on Monetary Integration, the value of the ratio XR_1/XR_0 was statutorily fixed at 1.

91. The radio-frequency spectrum is owned by the State and, in accordance with the LT, is classified as for free use, official use, and regulated use. No concession is needed to exploit the free-use spectrum. To exploit part of the regulated-use spectrum it is necessary to ask SIGET for a concession, which is granted for a period of 20 years. Concessions have been awarded mainly on the basis of auctions, by means of which the Government collected US$221.4 million between 1998 in 2001. The base price for a concession to exploit the radio-frequency spectrum is determined in accordance with a formula which takes into account the total transmission and reception bandwidth, the base unit price of the spectrum, and the target population. A concession may be revoked if it is not used within two years of being granted.

92. Satellite communications system operators that transmit from the national territory must, among other things, have rights to use the spectrum clearly established by international conventions, treaties or agreements signed and ratified by El Salvador or by obtaining a concession to use the spectrum granted by SIGET.

93. The services deemed to be essential include interconnection, at all levels, for the purpose of terminating telecommunications or transferring telecommunications originating in the network of one of the parties to another network selected by the end user; signaling; the handover of automatic identification of the number of the user originating the communication; billing data; the portability of the user's telephone number; and the recording of users in the telephone directory. Under the LT, every commercial telecommunications network operator must provide access to essential resources to any operator that asks for them, subject to appropriate payment and without discrimination of any kind.

94. The prices and technical conditions for access to essential resources are negotiated between the parties; if agreement cannot be reached on any or all of the points, the parties may call on SIGET to settle the dispute. The LT also stipulates that network interconnection may be freely negotiated except as regards access to the above-mentioned essential resources.

95. The LT incorporates safeguards against anti-competitive practices, in particular, it prohibits operators from concluding any type of agreement on fixing, raising, concentrating or manipulating the prices they charge for selling or leasing their services to third parties or end users, as well as distribution agreements. Cross subsidies in connection with services offered in competition with other operators are also prohibited.

96. Finally, the LT establishes a special regime for the telecommunications activities of operators providing the following services: free-reception sound broadcasting; free-reception television; sound broadcasting by subscription via cable or radio; and television broadcasting by subscription via cable or radio. The services require concessions which are granted for a period of 20 years. Only natural persons Salvadoran by birth or Salvadoran legal persons (entities with at least 51% of the capital in Salvadoran hands) may obtain concessions for providing free-reception broadcasting services.

97. The National Electricity and Telephony Investment Fund (FINET) was established for the purpose of facilitating access to electricity and telephone services for rural communities and low-income families. FINET's functions include subsidizing telephone infrastructure and the supply of telephone services (and of electrical energy, see Section 4) in rural and low-income areas, provided that they benefit the community.[29] The Law provides for the Fund to subsidize these activities using

[29] Electricity consumption associated with water extraction and pumping projects and with buildings used for providing educational and health services, if community owned or administered, are considered to be of benefit to the community.

the income obtained as a result of investing its resources. The assets of the Fund consist mainly of contributions from the State, 98.5% of the resources generated by granting concessions to use the radio-frequency spectrum, and all the resources produced by concessions for generating geothermal and hydroelectric power. In January 2002, 18 FINET-funded projects awarded by auction, with a total value of US$1.64 million, were in progress, together with 57 projects awarded by competition for funds (*concurso de fondos*), with a total value or US$5.54 million.

98. El Salvador bound the level of market access provided for by its legislation in its Schedule of Commitments agreed during the GATS Negotiations on Basic Telecommunications.[30] During those negotiations, El Salvador significantly increased its commitments with respect to its 1994 offer, binding services provided at national and international level via public and non-public basic telecommunications networks for all modes of supply and with respect to both market access and national treatment.[31]

(iv) Transport

(a) Maritime transport

99. In October 2002, the Vice-Ministry of Transport, created in 1994 within the Ministry of Public Works, Housing and Transport, was the body responsible for regulating all maritime transport policy. This work was carried out through the Maritime Transport Directorate. The Vice-Ministry must also approve port charges and changes in those charges.

100. El Salvador's Port System comprises two commercial ports, the ports of Acajutla and Cutuco, both managed, at the end of 2002, by the Executive Autonomous Ports Commission (*Comisión Ejecutiva Portuaria Autónoma,* CEPA). The fishing ports are under the management of the Ministry of the Economy. Under its Organization Law, CEPA has exclusive responsibility for: the administration, exploitation, management and execution of the port operations of all Salvadoran port facilities not subject to a special regime, such as the custody, handling and storage of exports and imports. CEPA is also responsible for the facilities of El Salvador's International Airport (see Section (iv) (b)). CEPA may contract out certain tasks, but must retain direct management of the ports. At the end of 2002, the services subcontracted to private enterprises included, among other things: mooring, loading, transferring cargo from hold to wharf and vice versa, and storage.

101. In mid-2002, all maritime cargo was being handled in the Port of Acajutla, the Port of Cutuco being out of operation. In 1999, the Port of Acajutla handled 2.3 million tonnes of cargo; if the petroleum and petroleum derivatives moved in the vessels of the RASA refinery -- a private enterprise established by a consortium of the oil companies Esso and Shell -- are taken into account, the total cargo moved increases to a little over 4 million tonnes. Most of this volume (about 86%) corresponded to imports. With respect to previous years, it is possible to observe a slight increase in the volume of cargo handled in Salvadoran ports. Export volumes have been affected by the decline in coffee exports.

102. In October 2002, the Legislative Assembly approved the tendering procedure for giving out the management and operation of the Port of Acajutla on concession to the private sector.[32] The

[30] WTO document GATS/SC/29/suppl.1, 11 April 1997.

[31] In the case of market access through commercial presence, application must be made to the Electricity and Telecommunications Supervisory Authority for a concession or licence.

[32] Decree No. 1014 of 3 October 2002, published in the Official Journal.

concession will be granted for a period of 25 years and calls for a series of compulsory investments which have to be made in the course of the first 3 years following contract signature, for a minimum of US$10,875,000. Moreover, the concessionaire will have to make other investments totalling US$7,125,000.00 in the course of the first 10 years.

103. Until the latter part of 2002, there was no specific maritime transport law *per se*. The authorities noted the need for this type of legislation and a bill was drafted which led to the General Maritime Port Law, approved by the Legislative Assembly in Decree No. 994, published in Official Journal No. 187 of 1 October 2002, which entered into force on 1 November 2002. In October 2002, the new Law was still in the process of entering into force. It will regulate everything to do with maritime navigation and port services.

104. The General Maritime Port Law establishes a Maritime Port Authority (*Autoridad Marítima Portuaria*, AMP), a regulatory body with legal personality and administrative, technical and financial autonomy, for the technical and economic regulation of the maritime port transport subsector. The Law limits the jurisdiction of the Ministries of Public Works and Transport and of Housing and Urban Development to the formulation of subsectorial maritime port policy, the associated outline planning and the corresponding implementing regulations. The AMP is also responsible for representing El Salvador in international organizations and for participating in the negotiation of international treaties and conventions on ports and maritime issues, in coordination with the competent departments. The AMP's functions also include, *inter alia*, regulating port charges and establishing port charge adjustment mechanisms, supervising and monitoring the granting and execution of national port concession contracts, preventing anticompetitive and discriminatory practices among users of maritime and port services, and approving all legal documents relating to the transfer, extension, expiry and buy-back of concessions.

105. The General Maritime Port Law created a Managing Board of the Maritime Port Authority (*Consejo Directivo de la Autoridad Marítima Portuaria*, CDAMP), responsible for formulating policies, directives and guidelines for the effective exercise of the AMP's institutional powers. The administration of the AMP will be the responsibility of an Executive Manager. The AMP will be financed by: Government contributions; a percentage, not to exceed 6%, of the income derived from the charges for port services provided to ships and cargo in public-use or private ports; the fees for services provided by the AMP itself; the dues collected by the various registries operated by the AMP; the proceeds of the fines and economic penalties levied by the AMP; nonrecurrent receipts; and any other lawfully obtained income.

106. El Salvador does not have a national merchant fleet, but the new General Maritime Port Law makes provision for the registration of vessels. The Law establishes a Salvadoran Maritime Register (*Registro Marítimo Salvadoreño*, REMS), an integral part of the AMP, in which vessels and floating structures and transactions such as buying and selling, building, leasing, chartering and mortgaging must be registered. To be registered in the REMS, a vessel must meet certain requirements with respect to design and seaworthiness; moreover, its owner must be domiciled in the country or, in the case of a company, have been established in accordance with the laws of El Salvador, or if established abroad, have a branch office in El Salvador. A foreign vessel may be registered in the REMS only if its registration in the issuing country has previously been cancelled. The AMP will issue any vessel or floating structure registered in the REMS a registration certificate conferring Salvadoran nationality. To form part of the crew of vessels registered in the REMS or exercise any profession, office or occupation in the port jurisdiction or in an activity regulated or controlled by the AMP, it is necessary to obtain the latter's authorization and have it registered in the REMS.

107. The tariff or price policy for the port services provided by the public ports or public-use private ports operating in El Salvador will be formulated by the AMP in accordance with the Special Regulations for the Application of Port Services Tariffs, under which port operators must submit to the AMP, for its approval, a tariff schedule that includes the tariffs or prices for port services, the methodology used to calculate them and the way in which these tariffs or prices will be adjusted in the future. To prevent cross subsidization, port services operators must implement a system of cost accounting per activity. The AMP will be able to use several methods of determining tariffs: tariffs adjusted on the basis of inflation indices and operational improvements; tariffs by comparison with other competing ports; tariffs based on calculation of the return on investment; free market. Port tariffs approved by the AMP and changes in them must be registered and published in two national newspapers at least 10 calendar days before they enter into force.

108. The Law provides for the AMP to define the port services that will be deregulated, where the market is sufficiently competitive. The Law expressly prohibits any act the intention or result of which is improperly to restrict competition between ports and port services operators. It is stipulated that as long as the country lacks specific legislation in the field of competition policy, the Board of Directors of the AMP will ensure compliance with the relevant principles as far as maritime and port activities are concerned.

109. Ports, whether public or private, in operation on the date of entry into force of the Law, are subject to the AMP's regulatory regime, where applicable. The CEPA will be the local maritime port authority for the State commercial ports under its jurisdiction within which it will be competent for administration, operation, maintenance and conservation. At the CEPA's representation, this authority will be exercised by the port operator.

110. El Salvador is a signatory to a number of conferences administered by the International Maritime Organization but not to the United Nations Convention on a Code of Conduct for Liner Conferences. In the field of maritime transport, El Salvador has not made any commitments under the GATS.

(b) Air transport

111. Air transport policy is the joint responsibility of the Vice-Ministry of Transport, under the Ministry of Public Works, Housing and Transport, and of the Civil Aviation Authority (*Autoridad de Aviación Civil*, AAC). CEPA is responsible for air traffic control services.

112. El Salvador has two public airports, the El Salvador International Airport and Ilopango Airport, which has both military and civilian uses. The El Salvador International Airport concentrates all international traffic, both passenger and freight. The activity indicators for this airport reveal a significant increase in the number of landings and take-offs, mainly for passenger transport. Between 1996 and 2000, passenger traffic grew steadily at an average annual rate of 13.4%, reaching about 1.6 million passengers in the year 2000. The authorities have pointed out that there is capacity for handling up to 3.5 million passengers a year. The trend in freight traffic is less clear-cut; there was an appreciable increase in imports between 1996 and 2000, whereas exports declined (Table IV.11).

113. El Salvador International Airport is administered by CEPA, which is responsible for the management, administration, maintenance and expansion of all airport facilities (see also Section (iv) (a)). CEPA is in charge of the handling and storage of goods, but the possibility of contracting the provision of these services out to a private company is being considered. CEPA is also responsible for airport security, together with the national civilian police (*Policía Nacional Civil*, PNC), while

private companies supply other services such as cleaning, restaurant services, flight information and the maintenance of certain areas not connected with airport maintenance.

114. Since 1983, El Salvador International Airport has been the base for operations, reservations, maintenance and administration of TACA International Airlines, S.A., a company in which Salvadorans hold a majority interest. TACA International Airlines, S.A. maintains administrative and operational links with the flag carriers of other Central American countries in which it has acquired holdings. TACA International Airlines S.A. is by far the most important airline based in Central America. No other company domiciled in El Salvador offers commercial air services.

Table IV.11
Activity indicators for El Salvador International Airport, 1996-00

	1996	1997	1998	1999	2000
Passengers					
Arrivals	463,455	482,163	599,111	655,587	634,750
Departures	409,230	426,453	554,917	605,231	621,595
Subtotal	**872,685**	**908,616**	**1,154,028**	**1,260,818**	**1,256,345**
Transit passengers	32,095	21,480	26,491	111,349	85,360
Transfer passengers	60,735	30,511	23,006	188,782	256,636
Total	**965,515**	**960,607**	**1,203,525**	**1,560,949**	**1,598,341**
Aircraft[a]					
Commercial aviation	22,967	22,093	25,188	27,742	30,796
General aviation	1,124	1,058	1,202	2,124	1,042
National aviation	124	268	302	156	120
Air taxis	102	680	1,402	1,326	68
Total	**24,317**	**24,099**	**28,094**	**31,348**	**32,026**
Freight and mail (kg)					
Import freight	16,155,915	17,368,915	17,387,583	21,318,441	18,030,674
Export freight	16,510,552	14,350,104	13,792,576	14,651,080	14,437,271
Total freight	**32,666,467**	**31,719,019**	**31,180,159**	**35,969,521**	**32,467,945**
Arriving mail	..	227,676	267,028	211,310	223,044
Departing mail	..	92,060	104,747	71,924	103,643
Total mail	..	**319,736**	**371,775**	**283,234**	**326,687**
Total freight and mail	**32,666,467**	**32,038,755**	**31,551,934**	**36,252,755**	**32,794,632**

a Landings and take-offs.

Source: Executive Autonomous Ports Commission.

115. Legislative Decree No. 582 of 19 October 2001 approved the Civil Aviation Organization Law. The Law created the Civil Aviation Authority (AAC) and governs everything to do with the granting of licences, public and private air transport services, ancillary services, and infrastructure. The functions of the AAC include the regulation, supervision and control of all civil aviation activities relating to the authorization, modification, cancellation and revocation of operators' certificates and operating permits, air transit services, aeronautical communications, aeronautical meteorology services, aeronautical information services, aerial navigation services and facilities, and the registration, certification and supervision of aviation personnel, aircraft and other aeronautical infrastructure. Moreover, the AAC must ensure the maintenance of healthy competition in the civil aviation and air transport sector and guard against monopolistic practices. Thus, the AAC is

responsible for regulating the tariffs for airport, aeronautical, aerial navigation, air transit control and flight protection services which have monopolistic characteristics and might be exposed to the exploitation of a dominant position. The AAC is authorized to impose sanctions for non-compliance with the rules and regulations applicable to the civil aviation sector.

116. As far as the commitments assumed under GATS are concerned, El Salvador has bound repair and maintenance services with respect to market access and national treatment for the cross-border supply, consumption abroad and commercial presence modes. In this latter case, El Salvador's Schedule of Commitments stipulates that it is necessary to apply to the CEPA for a concession or licence to provide these services, with the requirement that the applicant be domiciled in El Salvador. The authorities have pointed out that, in the light of the new Civil Aviation Organization Law, a permit from the AAC is now required and that in recent years permits of this type have been issued.

117. There are no limitations on foreign investment for establishing airlines in El Salvador. Foreign investors receive national treatment in connection with investment in Salvadoran airlines and there are no limitations on market access under the commercial presence mode.

118. El Salvador has signed a freedom of the air (fifth and sixth freedoms) agreement with the United States.[33] It has also signed fourth freedom bilateral agreements with Chile, Spain and the United Kingdom.[34] Licences for landing slots are granted on the reciprocity principle in accordance with the Chicago Convention.

[33] Generally speaking, the fifth freedom grants an airline of one country the right to transport freight or passengers between two third countries provided that the flight originates or terminates in the carrier's flag state. The sixth freedom grants the right to transport freight or passengers between two third countries via the carrier's flag state.

[34] In general, the fourth freedom grants an airline of one country the right to transport freight or passengers from another country to its own flag state.

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