

BTI 2010 | El Salvador Country Report

Status Index	1-10	7.14	# 32 of 128	
Democracy	1-10	7.35	# 34 of 128	➔
Market Economy	1-10	6.93	# 30 of 128	➔
Management Index	1-10	6.30	# 24 of 128	

scale: 1 (lowest) to 10 (highest) score rank trend

This report is part of the Transformation Index (BTI) 2010. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 128 transformation and developing countries are evaluated.

The BTI is a joint project of the Bertelsmann Stiftung and the Center for Applied Policy Research (C•A•P) at Munich University.

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Key Indicators

Population	mn.	6.1	HDI	0.75	GDP p.c.	\$	6514
Pop. growth	% p.a.	0.4	HDI rank of 182	106	Gini Index		49.7
Life expectancy	years	71	UN Education Index	0.79	Poverty ²	%	20.5
Urban population	%	60.4	Gender equality ¹	0.53	Aid per capita	\$	12.9

Sources: UNDP, Human Development Report 2009 | The World Bank, World Development Indicators 2009.

Footnotes: (1) Gender Empowerment Measure (GEM). (2) Percentage of population living on less than \$2 a day.

Executive Summary

In 2007 and 2008 the government of El Salvador made great progress in consolidating its free market economy, but little was achieved in the context of necessary political or social reforms that might help deepen democracy. In the economic realm, El Salvador has established itself as one of Latin America's most open environments for trade and investment. International observers such as the OECD particularly commend the progress made in the country's competition policy, citing it as an example for other nations. Despite strong ties to global financial markets cemented as El Salvador maintained and promoted numerous free trade agreements, the impact of the global financial crisis on its economy was moderate as of early 2009. Although headline inflation was subject to partly significant fluctuations throughout 2008, and growth rates were estimated to have dropped towards the end of 2008 after a record high in 2007, the country's macroeconomic fundamentals have overall been solid and its banking sector has remained highly liquid.

On the other hand, the Salvadoran government has done little to pursue political or social reforms which would address persistent problems such as corruption within state agencies, high rates of poverty and crime, or gross socioeconomic inequalities. Human rights observers particularly criticized the inappropriate use of the Special Law against Acts of Terrorism to charge 13 people following protests against the privatization of water services in Suchitoto in July 2007. In the months leading up to the 2009 elections, defamation-based electoral campaigns exacerbated the pronounced left-right cleavage in Salvadoran society, and thereby contributed to numerous instances of political violence. While the legislative elections on 18 January 2009 were generally free and fair, several irregularities in the electoral process occurred. The most momentous incident of attempted electoral fraud even led to the rescheduling of voting in the municipality of San Isidro. By failing to implement residential voting nationwide for the 2009 elections due to the lack of funds, the state authorities neglected necessary electoral reforms which would deepen democracy in El Salvador by enabling more political participation.

Although 50% of interviewees preferred democracy to any other form of government according to Latinobarómetro 2008, the level of consent to democratic norms fell as low as 38% in 2007, indicating the occurrence of another crisis of faith in democracy. In light of these issues, the greatest challenge for El Salvador's political leadership is the need for substantive political and social reforms in order to become a fully consolidated socially responsible free-market democracy.

History and Characteristics of Transformation

El Salvador's rather lengthy democratization process started at the end of the 1970s and beginning of the 1980s, when a group of young, radical reformist officers overthrew the government in 1979, and civilian presidents were elected to rule the country from 1984 on. A decisive step in the country's transformation process was taken when a peace agreement in 1992 officially ended the civil war that had lasted from 1980 to 1991. Approximately 75,000 individuals are estimated to have fallen victim to this intrastate conflict, and several thousand people who "disappeared" are still missing today. Competitiveness in the presidential elections as well as the extent of presidential powers increased from 1984 onwards. While the presidential powers of José Napoleón Duarte (1984 – 1989) were still strongly restricted by the military, his successors' powers became significantly greater. Duarte's successors in office were Alfredo Cristiani (1989 – 1994), Armando Calderón Sol (1994 – 1999), Francisco Flores (1999 – 2004) and Elías Antonio Saca (2004 – 2009). Except for Duarte himself, who was a member of the Christian Democratic Party (Partido Demócrata Cristiano, PDC), all presidents since the end of the civil war have been candidates of the right-wing Nationalist Republican Alliance (Partido Alianza Republicana Nacionalista, ARENA). ARENA's main opposition party has been the Farabundo Martí National Liberation Front (Frente Farabundo Martí para la Liberación Nacional, FMLN), a left-wing guerilla movement that was successfully transformed into a major political party.

The deep polarization and distrust between the two major parties, ARENA and FMLN, reflects a deep division within society along the ingrained socioeconomic cleavage of rich and poor, and has quite substantially hindered the development of a more democratic political culture. Seventeen years after the official end of the Salvadoran civil war, this polarization remains strong, as the results of the legislative elections in January 2009 show: In a close contest, FMLN and ARENA won the largest number of seats, respectively with 35 and 32 out of a total of 84. El Salvador seems to have entered a new phase of its political development in March 2009, as – for the first time since the beginning of the transformation process – the candidate of the left-wing FMLN, journalist Mauricio Funes, won the presidential elections over ARENA rival Rodrigo Ávila.

The ARENA-led governments have consistently pursued a process of economic transformation marked by privatization and liberalization since 1989. These policies were applied to the former public service sector from 1996 onwards. Nowadays, the Salvadoran economy is one of the most open in Latin America and is among the best performing in Central America. High rates of poverty and gross socioeconomic inequalities nevertheless remain, due to the lack of coherent anti-poverty policies. A small, oligarchic business elite thus benefits the most from El Salvador's transformation toward a free market economy.

Transformation Status

I. Democracy

1 | Stateness

While the state's monopoly on the use of force covers the entire territory of El Salvador and is not threatened by any major guerilla or paramilitary group, high crime rates continue to pose a challenge to the state's authority. Despite a 10.29% drop from 3235 registered murder victims between January and November 2007 to 2902 in the same period of 2008 according to the Central American Observatory of Violence (Observatorio Centroamericano Sobre Violencia), the number of homicides saw renewed growth towards the end of 2008 when 49 people were killed during the last four days of December alone. El Salvador remains one of the most dangerous countries in Latin America, with an average of 8.7 homicides per day and an especially high concentration of crime in the metropolitan area of San Salvador.

Monopoly on the use of force

According to findings from a Brazilian research group, the murder rate is particularly severe among young Salvadorans aged between 15 and 24. With 92.3 young murder victims per 100,000 people, El Salvador has the highest rate of youth homicides in Latin America. Findings from the National Commission for Citizen Security and Social Peace furthermore indicate that reported killings of women have increased by 50% since 1999.

Among the reasons quoted for El Salvador's vulnerability to crime are the prevalence of criminal gangs (maras), the continuous lack of consequences for perpetrators of criminal activities, the country's geographic placement as a key drug transit route, poverty and socioeconomic inequalities. Prior to the drop in the homicide rate between January and November 2008, government policies such as Mano Dura ("Strong Hand," implemented in 2003) and Super Mano Dura ("Super Strong Hand," implemented in 2004) as well as individuals such as Rodrigo Ávila, former director of El Salvador's National Police and presidential candidate for ARENA in 2009, had been repeatedly criticized for an inability to deal effectively with the challenge posed to the state's authority by high levels of crime.

According to the constitution, all Salvadorans over the age of 18 are considered citizens of the state. Nobody is formally denied civic rights on the grounds of belonging to particular religious, political or ethnic groups, or on the basis of gender or sexual orientation. The state's constitution is recognized by a majority of the Salvadoran population: According to Latinobarómetro, 63% of respondents supported the constitution in 2008. This is a slight increase compared to 60% in 2006, but remains underneath the value of 66% in 2004. The legitimacy of the nation-state is not questioned in principle.

State identity

The constitution explicitly recognizes the juridical status of the Catholic Church and establishes the right of all other churches to be officially acknowledged. According to a March 2008 survey by the Public Opinion Center of the Technological University of El Salvador, 52.5% of Salvadorans identify themselves as Roman Catholic. Protestant believers constitute the largest religious minority, comprising 27.6% of the population. Throughout 2007 and 2008, President Saca attended a variety of religious ceremonies in order to promote interfaith understanding. In April 2007, the Legislative Assembly voted unanimously to amend Article 296 of the Penal Code to impose criminal sentences of six months to two years on those who publicly offend or insult the religious beliefs of others, or who damage or destroy religious objects. Sentences increase to one to three years in prison if such acts are carried out for the purpose of publicity, while repeat offenders face prison sentences of three to eight years.

No interference of religious dogmas

Church and state are nevertheless widely separate, and religious dogmas have no noteworthy influence on politics or the law. President Saca's refusal to sign the Ibero-American Convention on the Rights of Youth (ICRY) in October 2008 was interpreted by Christian pro-life groups as rejection of the convention's provisions on abortion and homosexuality. However, this interpretation contradicts the government's official statement that its objections to the ICRY were based on concerns about clauses that would allow youths to evade military service, and that would forbid capital punishment of adults under the age of 24. Religious issues play no role in the electoral campaigns of the country's two major parties, the right-wing ARENA and the left-wing FMLN. Article 82 of the constitution prohibits persons who hold religious offices from belonging to political parties or running as electoral candidates for positions of political power.

The state infrastructure and its powers extend beyond maintaining law and order, but severe deficits with regard to administrative structures remain, particularly in rural areas. Despite the conduct of pilot projects in 2006, the Voto Residencial ("residential vote") has not been fully implemented for the 2009 elections due to a lack of funds. The only area to exclusively offer residential voting in 2009 was the department of Cuscatlán. This failure to operate the Voto Residencial nationwide undermined hopes to enable more political participation, particularly among the

Basic administration

rural population, by reducing sometimes extensive travel distances to polling stations.

The overcrowding of prison facilities, the lack of basic sanitation and poor supply of drinking water for the country's poorest populations are still among the country's most severe problems and have not been adequately addressed. Occupancy levels of prison facilities have been increasing steadily since 2000, reaching an unprecedented 199.2% in December 2007. Journalists and human rights observers relate the numerous prison riots in 2007 directly to harsh conditions for detainees. According to a World Bank report published in December 2008, access to basic sanitation for El Salvador's poorest populations needs to be further improved. Although considerable progress has been made compared to the 1990s, only 66.5 out of 100 rural communities have access to drinking water, of which only 33.2 receive water seven days a week.

2 | Political Participation

The Constitution of the Republic of El Salvador and its electoral code establish that elections are to be free, direct and equal, with anonymous voting. According to international observers, the legislative and municipal elections on January 18, 2009, were free and fair overall despite several irregularities in the electoral process. While the months leading to the elections were marked by numerous instances of political violence, the day of the election itself proceeded in a largely peaceful manner. Due to difficulties in calculating the number of eligible voters, official data on voter turnout levels has yet to be published. However, several sources confirm that turnout was at a record high. Shortcomings in the electoral process range from administrative deficiencies to attempted electoral fraud. They include technical problems with the newly implemented quick-count system for election results; the inclusion of 100,000 deceased persons in the voter registries; the movement of voters within the country to vote in municipalities other than the ones they reside in; voter manipulation through party transportation to the polling station and the display of party symbols by staff in the polling stations; irregularities relating to DUIs (the Salvadoran ID cards required to vote) such as individuals possessing multiple DUIs; vote-buying and the placement of voting booths within viewing distance of active partisan observers. The most momentous incident of attempted electoral fraud occurred in San Isidro in the Cabañas department, where voting had to be rescheduled to 25 January 2009 after a group of foreigners illegally attempted to vote. While San Isidro was the only municipality to close voting, other municipalities also reported that foreigners attempted to vote using false identification.

Free and fair
elections

The fact that Salvadorans living abroad at times of elections are not allowed to vote seriously limits the democratic character of the Salvadoran elections, as more than

2.5 million Salvadorans are currently living and working in other countries, mainly in the United States. The failure to implement the Voto Residencial nationwide for the 2009 elections particularly disadvantaged individuals living in rural areas, as extensive travel distances to polling stations make it difficult for them to vote. Representatives of the FMLN moreover complained that defamation of their candidates during the electoral campaign undermined the free and fair competition between political parties, citing accusations by ARENA, the right-wing media and United States representatives alleging links between the FMLN and the Revolutionary Armed Forces of Colombia (Fuerzas Armadas Revolucionarias de Colombia, FARC) as being particularly harmful to the vote. The fact that ARENA claimed victory in the capital city of San Salvador before the publication of the official end result led to suspicions of electoral fraud, as the Supreme Electoral Tribunal (Tribunal Supremo Electoral) alone has the authority to declare the official election outcome. The reputation of the Tribunal was further undermined by criticisms that its members were politically biased and that they had intentionally impaired the transparency of the electoral process.

Since the successful reform of the military and the police forces in the 1990s, there have been no significant veto powers or political enclaves constraining elected rulers in their effective power to govern. However, civil society organizations continue to criticize the disproportionate political influence exercised by business oligarchies and U.S.-based multinational enterprises.

Effective power to govern

The constitution establishes the right for independent political and civic groups to associate and assemble freely in accordance with the law. This right is generally respected and numerous civil society groups operate in El Salvador without disturbance by the state authorities. However, concerns about constraints on the freedom of association have been growing in recent years due to the inappropriate use of the 2006 Special Law against Acts of Terrorism (Ley Especial Contra Actos de Terrorismo). Following protests against the privatization of water services in Suchitoto in July 2007, 13 people were charged under the anti-terrorism law, which carries a potential sentence of up to 60 years in prison. In response to domestic and international pressure, the charges against the "Suchitoto-13" were reduced from terrorism to public disorder before being completely dismissed in February 2008. Human rights experts have declared that the Special Law against Acts of Terrorism is "too confusing," and have raised concerns that it is being employed to repress left-leaning social movements rather than to target actual crimes.

Association / assembly rights

In addition, organizations with particular human rights or political agendas, such as those advocating on behalf of gays, lesbians and transgender persons, have continued to experience delays in the approval of their legal status. Likewise, workers have submitted several complaints to the International Labor Organization (ILO) Committee on Freedom of Association, as they have faced problems forming unions due to excessive formalities used as justification to deny applications for

legal standing. In October 2007, the Supreme Court of El Salvador ruled against the adoption of ILO Convention 87 on the freedom of association and protection of the right to organize, as it would contradict the constitution's prohibition on the formation of trade unions in the public sector.

The freedoms of opinion and of the press are guaranteed under the Salvadoran Constitution and generally respected in practice. The media realm is rather pluralistic and dominated by private operators. International media can operate freely in El Salvador and access to the Internet is not restricted. There have been no instances of censorship by the state authorities, and the media freely and routinely criticize the government. In March 2007, following public pressure, the Legislative Assembly (Asamblea Legislativa) of El Salvador withdrew its request to use a polygraph test to identify employees who provided the media with information about a salary increase for legislators.

Freedom of
expression

Reasons for concern about the freedom of expression in El Salvador include continued practices of self-censorship among journalists, irregular access to information at state agencies, particularly at the Supreme Court, and the failure of the National Police to investigate death threats against broadcasters at Radio Cadena mi Gente, a recently founded independent media outlet. Human rights activists furthermore criticized the arrest of freelance journalist María Haydee Chicas together with the "Suchitoto-13" under the Special Law against Acts of Terrorism in July 2007, as well as the lack of investigation into the 1997 killing of journalist Lorena Saravia, who had been reporting on narcotics trafficking that allegedly involved members of the armed forces. In the period leading up to the 2009 elections, tensions rose between media outlets and political parties, particularly officials of left-wing party FMLN.

3 | Rule of Law

The separation of powers in El Salvador is formally recognized but constrained in practice due to structural deficits of the legislative and the judiciary. Despite efforts by the World Bank-financed Judicial Modernization Project to improve the performance of El Salvador's justice system, inefficiency and corruption have continued to undermine the strength of the judiciary, and have frequently led to a lack of appropriate legal consequences for people who belong to economically or politically influential networks.

Separation of
powers

The judiciary's independence is constitutionally recognized, but persistent dysfunctions continue to undermine its impartiality in practice. Numerous reports about inefficiency and corruption within El Salvador's justice system indicate that major effects of the World Bank-financed Judicial Modernization Project remain to be seen. This project aimed to address the structural deficits of the Salvadoran judiciary, but ended in December 2008.

Independent
judiciary

Corrupt practices frequently lead to a lack of enforcement of civil and criminal laws. According to a report in the Miami Herald, Salvadoran officials failed to enforce a U.S. court judgment against textile and telecommunications magnate Oscar Safie Zacarias due to his family's influence over El Salvador's Supreme Court. Judicial delays, inadequate government funding of the National Police, the intimidation and killing of victims and witnesses, and the failure to remove unqualified and corrupt judges despite hundreds of complaints from private citizens have all contributed to the public's loss of confidence in the justice system. Polls by the Public Opinion Center of the Technological University of El Salvador show that 39.9% of the population believes the implementation of justice worsened in 2008, compared to 31.7% of interviewees in 2007.

Though El Salvador is perceived to be one of the cleanest Latin American countries in terms of corruption, reports on corrupt practices within state agencies, in particular the judiciary and the National Police, persisted throughout 2007 and 2008. NGOs such as the Salvadoran Foundation for Economic and Social Development (Fundación Salvadoreña para el Desarrollo Económico y Social) and the Human Rights Institute of the University of Central America (Instituto de Derechos Humanos de la Universidad Centroamericana) maintained their criticism that too few efforts had been made to remove corrupt officeholders. In a survey by the Public Opinion Center of the Technological University of El Salvador, 50.3% of respondents said they believed the degree of corruption had increased under Elías Saca's presidency.

Prosecution of
office abuse

The civil rights of certain societal groups have been violated over protracted periods of time, with state authorities failing to hold perpetrators sufficiently accountable. Discrimination against women, homosexuals, indigenous people and persons with disabilities remained widespread throughout 2007 and 2008. Due to the judiciary's inefficiency and corruption, civil rights violations have been dealt with only inadequately or not at all. Consequently, many victims believe their cases to be unlikely to be prosecuted and do not sue their perpetrators.

Civil rights

Human rights groups were particularly alarmed by the continuously worsening conditions in prison facilities, by reports detailing police brutality and by a constantly growing trend in violence against women. Statistics by the Salvadoran Institute for the Development of Women (Instituto Salvadoreño para el Desarrollo de la Mujer) show that domestic violence against women increased from 4,792 reported cases in 2006 to 5,777 in 2007. According to human rights observers, neither cases of domestic violence nor incidents of rape are effectively prosecuted and continue to be underreported due to ineffective and unsupportive responses by the authorities towards victims. Additional problems as yet insufficiently addressed by state agencies include poor working conditions and the prevalence of child labor. Despite numerous labor inspections on behalf of the Ministry of Labor, and various

civil society collaborations, child labor laws are not effectively enforced and child labor activities go frequently unpunished.

Human trafficking for the purposes of commercial sexual exploitation and forced labor has also remained a serious problem, despite an increase in government attempts to combat the practice in 2007 and 2008. These efforts included international cooperation with the governments of Guatemala, Nicaragua, Belize and the United States on transnational trafficking cases, assistance with repatriation efforts, widespread training of law enforcement personnel and nationwide awareness campaigns.

Human rights groups have raised growing concerns about the military's involvement in the fight against gang violence. In August 2008, 700 troops were newly deployed to provide support to the National Police in their fight against crime, joining the 1,300 already so assigned. Reports by civil society organizations describe the emergence of unofficial death squads and vigilante groups in recent years, linking them to the police and army. In 2007, the National Police presented evidence that some officers were moonlighting as hired assassins.

Only sparse progress has been made by the Salvadoran state with respect to prosecution of human rights violations during the civil war. In January 2007, the Legislative Assembly approved an annual day of remembrance in commemoration of children who disappeared during El Salvador's civil war, in accordance with a ruling by the Inter-American Court of Human Rights (IACHR). However, the majority of IACHR recommendations have not been followed up, including those regarding the 1980 killing of Archbishop Oscar Romero and the 1994 killing of Mauricio Garcia Prieto. Despite domestic and international demands for the abolishment of abolish the 1993 General Amnesty Law for the Consolidation of Peace (Ley de Amnistía General para la Consolidación de la Paz), the government has persisted in its objection to investigations of past injustices. As a result, human rights violations during the Salvadoran civil war are frequently prosecuted by foreign courts, such as the 1989 "Jesuits Massacre" case officially opened by Spain's National Court in January 2009. While the FMLN until recently pleaded for the repeal of the General Amnesty Law, it received widespread criticism from human rights observers when its presidential candidate for the 2009 elections, Mauricio Funes, declared in September 2008 that the party would no longer aim to abolish the law.

4 | Stability of Democratic Institutions

Democratic institutions in El Salvador fulfill their functions in principle, but inefficiency, corruption and the lack of administrative resources in some rural areas continue to constrain their effective performance. While political decisions are, as a rule, prepared, made and implemented in legitimate procedures, circumvention of

Performance of
democratic
institutions

formal procedures is particularly frequent within the judiciary. This leads not only to insufficient prosecution of civil rights violations, but also undermines horizontal accountability among state institutions, thereby considerably restraining the polity's effective and democratic performance. Following the funds-related failure to implement the Voto Residencial nationwide for the 2009 elections, the Supreme Electoral Tribunal was criticized for neglecting necessary electoral reforms which would deepen democracy in El Salvador by enabling more political participation.

During the 2009 electoral campaign, government members including President Saca, along with a variety of media outlets, questioned the FMLN's democratic credentials by accusing it of supporting violence and terrorist activities, in part because of alleged links with Colombia's FARC and funding by Venezuela's president Hugo Chavez. Despite such accusations, which are rather characteristic of defamation-based electoral campaigns in El Salvador, there are no relevant political or social players that oppose democracy in El Salvador.

Commitment to democratic institutions

On the other hand, civil society organizations such as the Committee in Solidarity with the People of El Salvador (CISPES) report a recent increase in the number of apparently politically motivated killings. In 2008 alone, more than half a dozen left-wing activists were assassinated, including Wilber Moises Funes, the FMLN mayor of Alegría, in January 2008. In April 2008, two municipal officials from Alegría were charged with conspiring to arrange murder. While these killings raise serious concerns about the commitment of some politicians to the principles and procedures of democracy, there have been no attempts by potential veto players such as the military or the police force to replace the democratic system as such.

5 | Political and Social Integration

The 2009 legislative elections highlighted the persistence of a strongly polarized two-party system in El Salvador: Out of 84 seats in the Legislative Assembly, the right-wing ARENA won 32, thus decreasing its number of seats from 34 in the 2006 – 2009 legislative term. The left-wing FMLN won 35 seats in 2009 compared to 32 in 2006, while the strength of the three center parties in the Legislative Assembly – the Christian Democratic Party (Partido Demócrata Cristiano, PDC), Democratic Change (Cambio Democrático, CD) and the Party of National Conciliation (Partido de Conciliación Nacional, PCN) – barely changed. The 2009 election results for these parties were: 11 seats for the PCN, five seats for the PDC, one seat for the CD (as compared to 2006, when the PCN won 10 seats, the PDC six seats and the CD two seats). Following El Salvador's Electoral Code, the Democratic Revolutionary Front (Frente Democrático Revolucionario, FDR), which was founded by defectors from the FMLN in 2005 but failed to win at least one parliamentary seat or 50,000 valid votes in the 2009 elections, was deregistered as a political party.

Party system

The results of the 2009 legislative elections indicate that, 17 years after the end of the civil war in 1992, politics in El Salvador remain polarized, as the two main political parties, ARENA and FMLN, obtained the largest number of seats in a close contest but neither of them an absolute majority. The polarization of El Salvador's party system is paralleled in its civil society, and was evident in numerous manifestations organized by left-wing and right-wing sympathizers in the months leading to the elections, confirming the strong social roots of the Salvadoran political parties. The de facto two-party system has proven to be stable, having been in place since the end of the civil war (regardless of internal splits in the major parties ARENA and FMLN). However, despite the strong societal roots of the party system, voter volatility tends to be rather high, amounting to as much as 30% of the electorate according to a statement by PCN representative Dagoberto Marroquín in March 2008.

Numerous interest groups and associations with diverse societal agendas operate in El Salvador, and generally coexist peacefully despite competing programs. International observers praise the fact that the Salvadoran civil society has been growing in strength and become more close-knit in recent years. This has been illustrated by the multitude of demonstrations, seminars, press conferences and awareness campaigns that were initiated or hosted by civil society organizations. For instance, leaders of trade unions and other interest groups were actively involved in the extensive protests against the privatization of water services and the planned mining activities in the department of Cabañas in 2007 and 2008. However, interest representation remains skewed to the disadvantage of organizations with particular political or human rights agendas, such as workers' unions or associations that campaign for the rights of homosexuals. This asymmetric representation of interests is mainly due to persistent resistance on the part of state authorities, which takes the forms of delays or denials of applications for legal standing.

Interest groups

The degree of popular consent to democracy in El Salvador has been subject to significant fluctuations in the last two years. According to Latinobarómetro, only 38% of interviewees in 2007 preferred democracy to any other form of government, the second-lowest value since the survey was first conducted in the country in 1996. These results indicate that in 2007 a "crisis of faith" in democracy similar to the one in 2001 occurred, when only 25% of interviewees supported the democratic system. By 2008, however, levels of consent to democratic norms recovered somewhat, increasing to 50%, or one percentage point beneath the value for 2006. These developments confirm a trend of partly radical yet short-lived changes in the attitudes towards democracy in El Salvador throughout the 2000s. Nevertheless, there have been no political protests calling the constitutional framework into question.

Consent to democratic norms

According to the 2008 survey by Latinobarómetro, the Salvadoran population has Latin America's lowest level of faith in the practical effects of popular protests and

Associational activities

demonstrations. Only 40% of interviewees consider public manifestations to be indispensable for the realization of their demands, indicating low levels of confidence in the efficacy of protest politics. On the other hand, numerous civic associations with diverse agendas operate in El Salvador despite continued hardships posed by the state authorities, including excessive formalities which delay applications for legal standing. The web of autonomous, self-organized groups is robust and becoming more closely knit in recent years. International observers interpret cooperative efforts such as a 2008 protest by a variety of community associations against the construction of a garbage dump in Cutumay Camones as evidence for the growing strength of voluntary networks.

Similarly, trust among the Salvadoran people has slightly increased. According to *Latinobarómetro*, 20% of interviewees in 2007 believed they could trust a majority of the population, compared to 17% in 2006. These results put El Salvador in Latin America's top 10 countries with respect to levels of interpersonal trust.

II. Market Economy

6 | Level of Socioeconomic Development

El Salvador's economy is the third largest in Central America. However, persistently high levels of poverty, long-term ingrained socioeconomic inequalities and practices of social exclusion are among the greatest challenges to El Salvador's socioeconomic development, not least due to their direct association with high levels of crime and low levels of schooling. Official state data indicates that the number of households living underneath the national poverty line increased from 30.7% in 2006 to 34.6% in 2007. Poverty is more pronounced in rural areas (with 49.8% of people living in poverty) than in urban areas (where 28.5% of people living in poverty). Studies by the ILO and World Bank report that high poverty rates have led to the dominance of a majority of the agricultural and non-agricultural sector by subsistence production. Remittances contribute to the income of Salvadoran households and play an important role in reducing poverty and socioeconomic hardships. According to the Central Reserve Bank of El Salvador (*Banco Central de Reserva de El Salvador*), the quantity of remittances amounted to \$3.7 billion in 2007 and increased to \$3.8 billion in 2008 despite the global financial crisis.

Socioeconomic
barriers

El Salvador's HDI score is 0.735, ranking 103rd out of 177 countries, making it a country of medium human development. The country's Gini coefficient of 52.4

(reference year 2002) highlights the fact that socioeconomic inequalities pose a serious challenge to state authorities. Likewise, problems of social exclusion remain prevalent, as women and indigenous people in particular continue to face discrimination in educational and economic opportunities, especially with respect to hiring and salaries. The UNDP Human Development Report 2007/2008 ranks El Salvador 92nd out of 157 countries with a Gender-related Development Index score of 0.726.

Economic indicators		2004	2005	2006	2007
GDP	\$ mn.	15798.3	17070.2	18653.6	20372.6
Growth of GDP	%	1.9	3.1	4.2	4.7
Inflation (CPI)	%	4.5	4.7	4.0	4.6
Unemployment	%	6.8	-	6.6	6.4
Foreign direct investment	% of GDP	2.3	3.0	1.2	7.5
Export growth	%	5.7	3.8	8.1	3.9
Import growth	%	4.1	5.0	8.4	8.1
Current account balance	\$ mn.	-627.7	-568.5	-676.9	-1118.8
Public debt	\$ mn.	4858.0	4775.2	5587.3	5443.9
External debt	\$ mn.	8400.0	8455.4	9218.5	8808.8
Total debt service	% of GNI	6.4	5.0	6.3	5.3
Cash surplus or deficit	% of GDP	-3.3	-4.4	-3.2	0.8
Tax Revenue	% of GDP	11.0	12.5	13.4	14.0
Government consumption	% of GDP	9.6	9.6	9.6	7.4
Public expnd. on edu.	% of GDP	-	2.7	3.0	3.0
Public expnd. on health	% of GDP	3.5	3.7	4.1	-
R&D expenditure	% of GDP	-	-	-	-
Military expenditure	% of GDP	0.7	0.6	0.6	0.6

Sources: The World Bank, World Development Indicators 2009 | UNESCO Institute for Statistics | International Labour Organization, Key Indicators of the Labour Market Database | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security.

7 | Organization of the Market and Competition

The rules for market competition are well established and guaranteed by the state, contributing to El Salvador's attractiveness for investment. The fundamentals of the country's competition policy are laid down in its constitution. While Article 102 guarantees economic freedom and Article 110 bans monopolistic practices, Article 101 requires the state to promote economic and social development by means such as the increase of productivity and the defense of consumer interests. Additionally, the 1 January 2006 implementation of El Salvador's first competition law, the Competition Law (*Ley de Competencia*), rendered a series of anticompetitive practices and the abuse of dominant market positions illegal. The law also provided for the creation of the Superintendency of Competition (*Superintendencia de Competencia*) which aims to abolish monopolistic practices and achieve a more efficient and competitive economy. The law was amended in 2007 to set higher maximum fines for especially harmful conduct and to give new means of enforcement to the Superintendency. According to a 2008 report by the OECD, El Salvador's competition policy has been off to an excellent start and can serve as example for other countries. Among the competition agency's greatest achievements is the development of supporting regulations and guidelines to complete the structure provided by the law.

Market-based
competition

Despite protests by certain parts of the Salvadoran civil society, the government under President Saca (2004 – 2009) continued to pursue policies of market liberalization and privatization as means to foster economic growth and development. The state does not intervene in market processes, and opportunities afforded to all market participants are largely equal. The 1999 Investment Law (*Ley de Inversiones*) grants equal treatment to foreign and domestic investors, establishes procedures to settle disputes between foreign investors and the government, and created the National Investment Office at the Ministry of Economy, whose main function is to facilitate the registration of new investments in the country. There are no restrictions on using or transferring profits. According to the U.S. Department of Commerce, there are no controls or requirements on current transfers, access to foreign exchange or most capital transactions. The country's tax burden is among the lowest in the region. Tariffs are relatively low and were further reduced by the implementation of the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA) in March 2006. As a result of these different factors, El Salvador was listed as Central America's most open trade and investment environment by the 2008 and 2009 editions of the Heritage Index of Economic Freedom, and was surpassed in Latin America only by Chile. The informal sector in El Salvador is comparatively small.

However, despite the establishment of a generally appropriate and efficient institutional framework for economic policy, two major challenges for market-based competition in El Salvador persist in the lack of a competition culture and inefficiency in the enforcement of commercial law. While the latter is due to deficiencies in the Salvadoran judiciary, the OECD has criticized the lack of public understanding of competition policy and of appreciation for the mission of the competition agency.

In 2006, the new Competition Law took effect in El Salvador. Besides rendering anticompetitive practices such as rigged bids and the abuse of dominant market positions illegal, this law also provided for the creation of the Superintendency of Competition which aims to abolish monopolistic practices and achieve a more efficient and competitive economy. One of the features distinguishing the Salvadoran Competition Law from its counterparts in other Latin American countries is its provisions on merger control. In 2007, the Competition Law was amended in order to set higher maximum fines for especially harmful conduct and to give new means of enforcement to the Superintendency, including the powers to conduct dawn raids and to create a leniency program.

Anti-monopoly
policy

A 2008 OECD report praised the Superintendency's recent accomplishments. These include the development of a five-year operations plan, the issuance of guidelines for merger notifications, the conduct of numerous sector studies and the signing of several cooperation agreements with other Latin American competition agencies. However, progress in targeting hard-core cartels has been rather slow, and international as well as domestic actors criticize the persistent, disproportionate influence of a few business oligarchs over the Salvadoran economy. According to an article in the left-wing journal Raices, the eight business conglomerates which dominate economic life in El Salvador are Grupo Cuscatlán, Banagrícola, Banco Salvadoreño, Banco de Comercio, Grupo Agrisal, Grupo Poma, Grupo de Sola and Grupo Hill. The slow and uncertain process of judicial review of the Superintendency's decisions contributes to problems in combating the monopolistic practices of El Salvador's oligarchs. Appeals of these cases are made directly to the Salvadoran Supreme Court, none of which has been resolved since the Superintendency's creation.

Foreign trade is mostly liberalized and there is no fundamental state intervention in free trade. The government under President Saca continued its efforts to establish and deepen bilateral and multilateral free trade agreements, emphasizing privatization and liberalization as means for achieving economic growth and development. Trade statistics indicate that the United States is El Salvador's leading trade partner, accounting for 35.6% import market share in December 2007 and serving as the destination for 50.8% of Salvadoran exports. By the end of 2007, a total of 13 free zones were operating in the country, of which 12 were used by maquila textile businesses. According to the U.S. Department of Commerce, these

Liberalization of
foreign trade

firms are mostly owned by Salvadoran, United States, Taiwanese and Korean investors, and collectively employ approximately 58,000 people.

El Salvador is also a member of the WTO, an active participant in the Summit of the Americas process and a signatory to free trade arrangements with Colombia, Taiwan, Mexico, Chile and the Dominican Republic. Negotiations on the establishment of a free trade agreement with Canada took place in 2007 and 2008, as were discussions on a new Association Agreement with the European Union which would include the establishment of a free trade area. The implementation of DR-CAFTA in March 2006 granted El Salvador preferential access to U.S. markets and further liberalized trade among the Central American countries.

The Salvadoran banking system remains one of the most advanced and strongest in the region, and has shown great resilience in light of the global financial crisis. El Salvador's banks are among the largest in Central America, and remain highly liquid with liquidity ratios above 34% according to a 2008 report by the IMF. With the acquisition of Banco Cuscatlán by Citigroup and Banco Agrícola by Bancolombia in 2007, about 90% of banking system assets are now foreign owned. The banking system's total assets as of November 2007 amounted to \$12 billion. While there has been robust growth in deposits and domestic assets in recent years, the ratio of non-performing loans has also been on an upward trend since 2006.

Banking system

According to reports by the IMF, the OECD and the U.S. Department of Commerce in 2008, the Salvadoran banking system is sound and in general well managed and supervised. El Salvador is officially dollarized and has no domestic currency or monetary policy. Foreign banks are afforded national treatment under the 1999 Banking Law (Ley de Bancos) and amendments made in 2002. This law helped the Salvadoran banking system to achieve international standards, strengthened supervisory authorities, provided more transparent and secure operations for customers and banks, sharply limited bank lending to shareholders and directors, and increased the minimum capital reserve requirement for a bank to 100 million colones (\$11.4 million). Foreign investors may obtain credit in the local financial market under the same conditions as local investors, with accounting systems generally being consistent with international norms. Oversight in the financial system is provided by the Superintendent of the Financial System. Interest rates are set by the market and have decreased significantly since the dollarization. The organization, operation and activities of microfinance institutions is regulated by the Non-Bank Financial Intermediaries Law (Ley de Intermediarios no Bancarios). According to the Law Against the Laundering of Money and Assets (Ley Contra el Lavado de Dinero y Activos), financial institutions are required to report suspicious transactions to the Attorney General and the Superintendent of the Financial System.

In order to reduce future effects of the global financial crisis on El Salvador's banking system, the government requested an \$800 million precautionary standby arrangement from the IMF that was approved in January 2009, and negotiated loans with the World Bank and the IDB for budget support and to increase the supply of bank credit.

8 | Currency and Price Stability

The passage of the Monetary Integration Law (Ley de Integración Monetaria) in November 2000 established the U.S. dollar as legal tender in El Salvador alongside the colon, with a fixed exchange rate of 8.75 colones per U.S. dollar beginning on 1 January 2001. The power of the Central Reserve Bank to issue new colones or coins ceased on the same date. The Monetary Integration Law also established the U.S. dollar as the unit of account for the financial system, and granted the freedom to contract in any currency. The U.S. dollar now freely circulates in El Salvador and is valid in all transactions, while the colon is used only in isolated rural areas.

Anti-inflation /
forex policy

Representatives of the IMF commend El Salvador's real effective exchange rate – which fell from -0.2% by the end of 2006 to -0.8% by the end of 2007 – as being broadly in line with economic fundamentals. Likewise, the IMF's mission chief for El Salvador describes the country's inflation rate as generally low and stable, although it has been subject to somewhat significant fluctuations in recent years. Headline inflation increased from 4.9% (year-on-year) in December 2007 to 9.9% in August 2008, but fell again to 5.3% in November 2008. The main contributing factor to these fluctuations was the volatility of global commodity prices, particularly for food and fuel. According to *The Economist*, food prices in El Salvador rose by 11.7% in 2008 compared to 2007, while transport prices increased by 9.1% due to rising energy costs. The Salvadoran government responded to rising prices with a \$15 million cut in its administrative expenditure in 2008, which included the suspension of extras such as bonuses and a freeze on new hiring in all government departments except public security and health.

The Central Reserve Bank is an autonomous entity, which is not allowed to grant loans to the government.

President Saca's government followed a consistent stability policy throughout his term, based on fiscal consolidation and the pursuit of trade and private investment as essential means to economic growth. As a result, international organizations such as the IMF have commended El Salvador's macroeconomic fundamentals for their solidity in recent years, citing prudent policies and well-oriented structural reforms. The government's fiscal deficit targets of 2.3% of GDP in 2008 and 2.2% in 2009

Macrostability

are consistent with its objective of maintaining fiscal restraint. Medium-term fiscal policy is anchored by the goal of reducing public debt to approximately 30% of GDP by 2013, while increasing spending on infrastructure and well-targeted social programs such as Red Solidaria. Although El Salvador's financial condition was subject to some fluctuations in 2007 and 2008 due to high fuel prices on energy subsidies, government actions to mitigate the impact of food prices and the U.S. slowdown, the country did not face any balance of payments pressures.

Despite strong economic fundamentals and a moderate public debt-to-GDP ratio, the Salvadoran government negotiated loans with the World Bank and the IDB as well as a precautionary standby arrangement with the IMF in 2008 and early 2009. This additional financing is intended to reduce the impact of the global financial crisis, the U.S. recession and election-related uncertainty on the economy.

9 | Private Property

Property rights and the regulation of the acquisition of property are well defined in terms of acquisition, benefits, use and sale, but only moderately well protected. El Salvador is a signatory of the Bern Convention for the Protection of Literary and Artistic Works; the Geneva Convention for the Protection of Producers of Phonograms Against Unauthorized Duplication; the Paris Convention for the Protection of Industrial Property; the Rome Convention for the Protection of Performers, Phonogram Producers and Broadcasting Organizations; the World Intellectual Property Organization (WIPO) Copyright Treaty; and the WIPO Performance and Phonograms Treaty. In December 2005, state authorities revised several laws to comply with DR-CAFTA's provisions on intellectual property rights, including the Intellectual Property Promotion and Protection Law and the Law of Trademarks and other Distinctive Signs. Among other changes, these reforms extended the copyright term from 50 years to 70 years and made piracy punishable by a jail sentence of two to six years. Although Article 106 of the Salvadoran Constitution allows the state authorities to expropriate private property for reasons of public utility and social interest, there have been no recent cases of expropriation. There are minor restrictions on land ownership and the exploitation of underground resources. Since the Investment Law states that these latter resources belong to the state, concessions for mining are compulsory. With respect to land ownership, no single natural or legal person, either Salvadoran or foreign, may own more than 245 hectares. Rural lands cannot be acquired by foreigners from countries where Salvadorans do not enjoy the same right.

Despite these generally well-defined property rights and the overall sound regulation of the acquisition of property, the high crime rate, including criminal acts such as robbery and theft, and the state's incapability to deal with this challenge effectively, serve as a de facto restraint on the assurance of private property.

Property rights

International observers such as the U.S. Department of Commerce and the Heritage Index of Economic Freedom criticize inefficiency and corruption within the judicial system as among the main constraints on doing business in El Salvador, as they lead to the often slow and unproductive enforcement of property rights.

Private companies are permitted, and the privatization of the Salvadoran economy has been consistent with market principles. The privatization process began with the banking sector in 1989, while other public services such as electrical energy distribution, telecommunications and pensions followed suit in the mid- and late 1990s. Throughout its tenure, President Saca's government repeatedly declared that it regarded privatization and market liberalization as most important means to guarantee economic growth and development in El Salvador. International observers commend recent reforms as having enhanced business opportunities for private enterprises, including the introduction of an online license application system and the reduction of days required to start a business from 115 to 26 in 2006. Consequently, the World Bank's Doing Business Report named El Salvador as one of the most successful reformers worldwide in 2007, 2008 and 2009. Likewise, a 2008 report by the OECD praises the efforts of the Superintendency for Competition in enhancing competition between enterprises and abolishing monopolistic practices in the Salvadoran market.

Private enterprise

According to the U.S. Department of State and the Heritage Foundation, privatization has played an important role in attracting foreign investment, particularly in the electricity, telecommunications and pension funds sectors. Nevertheless, some civil society organizations continue to argue that privatization has strengthened the power of the oligarchy rather than increased the wealth of all Salvadorans. The water decentralization plan announced by President Saca in July 2007 triggered extensive protests on the part of a variety of communities, which demanded that their rights be protected against the government's privatization policies.

10 | Welfare Regime

April 2008 marked the tenth anniversary of El Salvador's private social security system. Newspapers such as *El Diario de Hoy* praise the success of the pension system, noting that the combined savings of Salvadoran workers now represent 21.5% of the country's GDP. However, a 2008 OECD report showed that the volume of private pension assets, valued at \$3.96 billion in 2007, was still relatively low compared to other Latin American countries.

Social safety nets

During the transition from the pay-as-you-go pension system to fully funded private accounts in 1998, the government created five privatized pension funds, which subsequently consolidated to just two, one owned by Banco Cuscatlán, the other by

Banco Agricola. Following the acquisition of the latter by Bancolombia and of the former by Citigroup in 2007, these funds are now entirely foreign controlled. While insurance companies operating in El Salvador have shown strong financial performance during the last years, human rights observers note that a high number of individuals, particularly in rural areas, and including those who work in hazardous activities, remain without health, accident and life, pension or unemployment insurance.

In response to high commodity prices, the government has committed itself to increase social spending by expanding the coverage of Red Solidaria (a conditional cash transfer program) to the 100 poorest municipalities. Further measures include a selective rise in the wages of low-income public servants and an increase in allowances for a tax credit program aimed at middle-income families. Additionally, a \$461 million anti-poverty compact intended to stimulate economic growth and reduce poverty in El Salvador's northern region entered into force in September 2007, based on a 2006 agreement between the Salvadoran government and the Millennium Challenge Corporation (MCC). While the future effects of these measures remain to be seen, recent statistics indicate that the government's poverty reduction strategy has to date seen little success. According to official data, the number of households living beneath the national poverty line increased from 30.7% in 2006 to 34.6% in 2007. Family, friendship or neighborhood ties cannot compensate effectively for the prevailing gross socioeconomic inequalities, which are reflected in a Gini coefficient of 52.4.

There are no institutions to compensate for gross social differences. Recent investments in public services for El Salvador's poorest populations, such as the 2007 MCC Compact, have had only marginal effects on persistent socioeconomic barriers. Although the Salvadoran Constitution stipulates that basic education and that of children with special needs have to be free, some public schools have continued to charge fees, effectively preventing poor children from attending school. Moreover, major disparities in the provision of schooling remain between rural and urban areas, as rural areas have failed to provide the mandated education to all eligible students. This is mainly due to a lack of funds, and because rural parents frequently withdraw their children from school to work.

Likewise, discrimination against homosexuals, persons with disabilities, women and indigenous people has persisted. The latter two groups in particular have continued to be disadvantaged with respect to educational and economic opportunities, in particular hiring and salaries. According to recent data by the Bureau of Democracy, Human Rights, and Labor of the U.S. Department of State, women's average wages are approximately half those of men. International observers such as the U.N. Committee on the Elimination of Discrimination against Women criticize the Salvadoran government for not doing enough to promote equal opportunities.

Equal opportunity

11 | Economic Performance

While El Salvador's economy used to rely heavily on agriculture, it is now much more diverse. By the end of 2008, agriculture accounted for approximately 10% of GDP, industry approximately 29% and services approximately 61%. The country's principal export goods are coffee and the output of the maquila industry. Remittances traditionally contribute to the income of Salvadoran households, and increased from \$3.5 billion in 2006 to \$3.7 billion in 2007 (i.e., 18% of El Salvador's GDP). Despite the global financial crisis, and in contrast to the experience of other Latin American countries, the quantity of remittances further rose to \$3.8 billion in 2008. According to the Heritage Foundation's 2009 Index of Economic Freedom, overall tax revenues represent 13.3% of GDP. Although the volatility of commodity prices led to fluctuations in headline inflation – rising to 9.9% in August 2008, but falling again to 5.3% in November 2008 – the end-of-period inflation rate remained relatively low at 4.9% in 2007 (as in 2006) and 5.5% in 2008. The unemployment rate decreased by 0.5% from 189,000 unemployed workers in 2006 to 188,000 unemployed workers in 2007. Official data on unemployment in 2008 were not yet available at the time of writing, but are expected to have increased only slightly. El Salvador's trade balance and public sector debt also remained relatively solid in recent years: The trade deficit grew from 19.0% of GDP in 2006 to 20.0% of GDP in 2007 and shrunk marginally to an estimated 19.9% of GDP in 2008. End-of-period public sector debt fell from 41.9% of GDP in 2006 to 40.8% of GDP in 2007 and reached an estimated 41.7% of GDP in 2008.

Output strength

On the other hand, levels of gross domestic investment declined from 16.1% of GDP in 2006 and 2007 to an estimated 15.4% of GDP in 2008. This reduction in investment, along with the tightening of external financing conditions due to international financial turmoil, had a negative effect on El Salvador's growth rates. While real GDP growth in El Salvador rose to a record high of 4.7% in 2007 from 4.2% in 2006, it decelerated to an estimated 3.2% in 2008. According to the Economist Intelligence Unit, El Salvador's budget balance improved from a deficit of 1.1% of GDP in 2006 to a deficit of just 0.3% of GDP in 2007, before falling to a deficit of 1.3% of GDP in 2008.

Taking all these figures into account, the impact of the global financial crisis has thus been moderate so far, despite the country's strong ties to global financial markets. As a result, international observers such as the IMF have commended the Salvadoran economy for its solidity and resilience in recent years.

12 | Sustainability

Despite certain improvements in natural resource management, environmental concerns continue to be subordinated to growth efforts in El Salvador. On the one hand, ecological standards were enhanced for 20,000 hectares by the end of 2008 thanks to successful coffee plantation innovations aimed at conserving biodiversity. Moreover, the Salvadoran Ministry of Environment and Natural Resources launched the Protected Areas Consolidation and Administration Project (PACAP) in May 2007. Financed by a \$5 million grant from the Global Environment Facility provided through the World Bank and \$2.6 million counterpart funds from the Salvadoran government, the PACAP aims to strengthen the Natural Protected Areas System in El Salvador which has been severely threatened by the conversion of forests, pollution and overexploitation of natural resources.

Environmental
policy

However, sparsely enforced environmental policies and violations of voluntary agreements in the context of international environmental law continue to raise concerns about the government's commitment to environmental protection. Domestic and international observers have noted critically that multinational corporations operating in the country frequently violate ecological standards, and rarely face any penalty imposed by the Salvadoran state authorities. A particular cause for concern is the insufficient enforcement of regulations on mining companies' reprocessing of water. In May 2008, the Catholic Church published a document which criticized the use of poisonous substances such as cyanide for mining activities as leading to extensive water pollution. United Nations human rights representatives in El Salvador have warned that short-term economic benefits can not compensate for the probably irreparable damages caused by ecologically harmful business activities, and have urged the Salvadoran government to make greater efforts to enforce environmental policies.

Public spending on education in El Salvador remains rather low, amounting to an average of 2.8% of GDP between 2002 and 2005, a slight drop as compared to an average of 2.9% of GDP between 2000 and 2002. Serious inconsistencies remain across the country with regard to institutional provisions for education, training, and research and development, as few schools are established in rural areas, and poor children are effectively prevented from attending school due to the persistence of illegal school fees. According to a 2008 report by the U.S. Department of State, children receive schooling for an average of approximately 5.5 years. The fact that rural parents frequently withdraw their children from school by the sixth grade to work contributes to this small number.

Education policy /
R&D

Similarly, insufficient investments in research and development – which were as low as 0.1% of GDP according to the UNDP Human Development Report 2007/2008 – have led to severe inconsistencies regarding the programs of study

offered by Salvadoran universities. A lack of funds also contributes to the universities' underperformance in terms of innovation and scientific publication. According to a 2007 report by the Association of Universities and Other Higher Education Institutions in Germany, this inconsistency and underperformance can be observed in both public and privately sponsored universities.

In light of the shortcomings in the nationwide system of education and training, the Salvadoran government has made significant efforts in recent years to expand educational opportunities. These include the implementation of a long-term educational development plan called Plan 2021, and a \$461 million anti-poverty compact by the MCC which entered into force in September 2007 and will be used, among other things, for investments in education in the country's northern region. Plan 2021 aims to improve the quality, access and relevance of secondary and primary education, and is scheduled to last from 2005 to 2021. However, the effects of these efforts to improve education in El Salvador have yet to be seen, particularly as the World Bank – one of the three project sponsors in addition to the IDB and the Central American Bank for Economic Integration – cancelled its contribution to Plan 2021 in December 2007.

Transformation Management

I. Level of Difficulty

The political leadership's governance capacity is severely constrained by several factors. Poverty rates are persistently high, with official data by the Salvadoran state authorities indicating that the number of households living underneath the national poverty line increased from 30.7% in 2006 to 34.6% in 2007. These high levels of poverty, ingrained socioeconomic inequalities (with a Gini coefficient of 52.4), the deportation of Salvadorans with criminal records from the United States and the country's geographic placement as key drug transit route all contribute to its vulnerability to crime. Despite a decrease in the number of registered murder victims between January and November 2008, El Salvador remains one of the most dangerous countries in Latin America with an average of 8.7 homicides per day.

Structural
constraints

Chronic childhood malnutrition and high school dropout rates are widespread, particularly in rural areas where the country's poorest populations live. Infrastructural deficiencies such as shortcomings in the provision of basic sanitation and the supply of drinking water are particularly pronounced in rural communities. International observers such as the U.S. Department of Commerce identify the relatively poorly educated labor force as being among the main obstacles to business opportunities in El Salvador. In the UNDP Education Index 2007/2008, El Salvador received a score of 0.772, confirming that its labor force is one of the least educated in Latin America.

While the Salvadoran economy has so far shown great resilience in weathering the effects of the global financial crisis, the country's high dependence on workers' remittances (reaching a total of \$3.8 billion in 2008), exports concentrated in coffee and textiles, and high gross external financing needs all add to the country's vulnerable external position. Regarding foreign constraints on El Salvador's political leadership, representatives of the FMLN and left-wing civil society organizations have alleged that representatives of the U.S. government distorted political competition in El Salvador by accusing the FMLN of links with Venezuela's President Chavez and Colombia's FARC.

Civil society traditions in El Salvador are weak, but do exist. Though a relevant political actor at the beginning and end of the civil war, civil society lost

Civil society
traditions

prominence in the 1990s. However, civil society has grown significantly in strength during the last decade, as evidenced by the establishment of various new associations and a multitude of demonstrations, seminars, press conferences and awareness campaigns initiated or hosted by civil society organizations. According to the president of environmental organization Salvadoran Ecological Unity (Unidad Ecológica Salvadoreña, UNES), social and ecological issues have been the central topics serving to mobilize Salvadoran civil society in the 2000s. This has been illustrated by the active involvement of trade unions and other interest groups in the extensive protests against the privatization of water services and the planned mining activities in the department of Cabañas in 2007 and 2008.

Social trust and trust in institutions alike are comparatively low. According to Latinobarómetro, only 20% of interviewees in a 2007 poll believed they could trust a majority of the population. One explanatory factor contributing to this relatively low level of social trust is the persistently high level of crime. A November 2007 survey by the Public Opinion Center of the Technological University of El Salvador showed that the most trusted institution in El Salvador was the Catholic Church (with 38.1% of interviewees stating that they trust it a lot), while only 14.3% of interviewees had a lot of trust in the central government and just 7.8% in the Legislative Assembly.

Protestant believers constitute the largest religious minority in El Salvador. Representing 27.6% of the population in 2008, their numbers are on the rise. Indigenous people comprise 1% of the Salvadoran population and frequently face discrimination in the economic sector, particularly with respect to hiring and salaries. Nevertheless, the salience of religious and ethnic cleavages in El Salvador is marginal, with a low risk that conflict will erupt along these lines. On the other hand, the Salvadoran society remains deeply divided by economic and social inequalities. Human rights observers have reported numerous instances of discrimination against the country's poorest populations in a variety of spheres. However, while the social divide between rich and poor has animated an increasing number of protests against policy programs which would harm the country's most vulnerable populations – the privatization of water services were a case in point – there have been no political actors trying to mobilize the poor parts of society into violent conflict.

Conflict intensity

II. Management Performance

14 | Steering Capability

President Saca's government repeatedly declared the establishment and maintenance of constitutional democracy and a socially responsible market economy to be strategic long-term aims. However, while progress has been made in furthering the development of El Salvador's market economy, little has been achieved in the context of political and social reforms. Rather, persistent problems such as poverty, socioeconomic inequalities and human rights violations have not been dealt with effectively. Moreover, by exacerbating the ingrained left-right cleavage by means of defamation-based campaigns in the months leading to the 2009 elections, the political leadership contributed to the deep polarization of the Salvadoran society and clearly prioritized short-term political gain over the long-term aim of democratic stability and political inclusion. However, international observers also charged that the steering capability of El Salvador's political leadership was constrained by foreign actors' intervention in the election campaign. While the U.S. ambassador in El Salvador blamed Venezuela for intervening in El Salvador's internal affairs, civil society organizations such as CISPES in turn criticized the United States for seeking to influence the Salvadoran political decision-making process. However, neither of these accusations can be substantiated with concrete evidence showing foreign constraints on the political leadership's steering capability.

Prioritization

International organizations such as the IMF have commended El Salvador's political leadership for successfully realizing a number of prudent and well-oriented structural reforms in the economic sector. This includes the government's efforts in pursuing and maintaining free trade arrangements as well as the progress made in the country's competition policy, such as the 2007 amendment of the Competition Law and the development of supporting regulations and guidelines to complete the framework provided by the law.

Implementation

On the other hand, there were certain shortcomings regarding the implementation of political reforms. The failure to implement the Voto Residencial nationwide for the 2009 elections received widespread domestic and international criticism. This shortcoming was seen as a neglect of necessary electoral reforms which would deepen democracy by enabling more political participation. Moreover, as shown by the increase in the share of households living beneath the national poverty line from 30.7% in 2006 to 34.6% in 2007, and by the persistent socioeconomic inequalities

(manifested in a Gini coefficient of 52.4), little has been achieved with respect to necessary social reforms. According to a May 2008 opinion poll by the Public Opinion Center of the Technological University of El Salvador, as many as eight out of 10 Salvadorans were dissatisfied with the leadership of President Sacá and ARENA.

There were limited signs of policy learning in 2007 and 2008. On the one hand, efforts to combat human trafficking intensified, and the government negotiated loans with international financial institutions – despite the country’s solid macroeconomic fundamentals – in order to reduce the impact of the global financial crisis. The administration showed good leadership skills in terms of finding new ways to address persistent human rights violations and preventing negative effects on the economy. Efforts to combat human trafficking include cooperative efforts with the governments of Guatemala, Nicaragua, Belize and the United States on transnational trafficking cases, assistance with repatriation efforts, widespread training of law enforcement personnel and nationwide awareness campaigns.

Policy learning

On the other hand, the political leadership’s inability to address prolonged problems such as poverty, discrimination against women and high school dropout rates indicates only little receptiveness to policy learning, at least in these areas. Likewise, the government showed little innovation in addressing the problem of high crime rates, but rather continued its rigid enforcement of the *Mano Dura* and *Super Mano Dura* strategies. The success of these policies is questionable, as the 10.29% drop in the number of registered murder victims between January and November 2008 as compared to the previous year was followed by a renewed increase toward the end of 2008.

15 | Resource Efficiency

The government has made efficient use of a majority of its economic resources. The economy has diversified significantly compared to the past, with agriculture accounting for about 10% of GDP, industry about 29% and services 61% by the end of 2008. Challenges for El Salvador’s trading position have been successfully met by reforming the export market, in which the principal export goods are coffee and the output of the maquila industry. The dollarization of the economy, a solid banking system, significant progress with respect to national competition policy following the implementation of the Competition Law in 2006, a low tax burden and low tariffs contribute to the country’s attractiveness for foreign investment. The Salvadoran government furthermore demonstrated efficient use of its budget resources in 2008 by responding to rising prices with a commitment to increase social spending while implementing a \$15 million cut in its administrative expenditure, which included the suspension of extras such as bonuses and a freeze on new hiring in all government departments except public security and health.

Efficient use of assets

However, the country's human resources are not used efficiently, due to number of factors including high school dropout rates, violations of workers' rights, a deficient infrastructure (particularly in rural areas), high levels of emigration and the related brain drain. The government does not deal effectively with malnutrition and other health risks, such as those related to working on coffee or sugar plantations, due to a lack of coherent policies and weak enforcement of the law. The failure to adequately address high levels of poverty and inequality also constrains business opportunities in El Salvador, in particular because these socioeconomic challenges are associated with high levels of crime. Likewise, the persistence of corrupt practices within state agencies, particularly the judiciary and the National Police, pose a significant challenge to the efficient use of organizational resources.

The government coordinates its policies effectively and acts in a coherent manner. There are no significant intragovernmental frictions, redundancies or lacunae. From 2006 until the general elections in early 2009, El Salvador was ruled by a form of divided government, with an ARENA-led presidency and the two major rival parties, FMLN and ARENA, holding the largest share of seats in the Legislative Assembly in a very close contest. Having respectively won 32 (FMLN) and 34 (ARENA) out of 84 seats in the 2006 elections, neither party was able to secure an absolute majority in the legislature. The legislative elections in January 2009 ensured that this close contest in the Legislative Assembly will continue, as the FMLN won 35 out of 84 seats and ARENA 32. However, despite the two major parties' conflicting policy objectives, particularly with regard to El Salvador's economic system, no major deadlock within the government in 2007 or 2008 emerged. On the contrary, the political agreement reached in order to ensure congressional approval to negotiate loans from the World Bank and the IDB in 2008 showed that compromise and policy coherence is possible in spite of fundamental ideological disputes between central political actors.

Policy
coordination

Corruption within the state authorities has reportedly been widespread and in some cases substantial, particularly with respect to the judiciary. NGOs such as the Salvadoran Foundation for Economic and Social Development and the Human Rights Institute of the University of Central America have persistently criticized the government for doing too little to remove corrupt officeholders. Supporting this criticism are survey results by the Public Opinion Center of the Technological University of El Salvador, which showed that 50.3% of interviewees believed that the degree of corruption increased under Saca's presidency. On the other hand, the implementation of the World Bank-financed Judicial Modernization Project, which had aimed to improve the performance of the Salvadoran justice system but ended in December 2008, shows that the political leadership is aware of the challenge posed by corrupt practices and is at least in principle willing to act on it. Further integrity mechanisms are either lacking, as in the case of a law on the declaration of party financing, or constrained, as seen in the delays in the release of information and public records by state authorities.

Anti-corruption
policy

16 | Consensus-Building

Despite irregularities in the 2009 elections, such as the movement of voters within the country to vote in municipalities other than the ones they resided in, and an apparent increase in the number of politically motivated killings in 2008 according to CISPES, there is fundamental agreement among all major political actors that democracy is a long-term strategic aim. There is less consensus among the two major political parties ARENA and FMLN regarding the country's economic system. While ARENA has emphasized the need to establish free-market policies as a long-term strategic aim in order to achieve economic growth and development, FMLN representatives have been critics of liberalization and privatization. However, despite this fundamental dispute, the political agreement reached in order to ensure congressional approval to negotiate loans from the World Bank and the IDB in 2008 showed that compromise on the issue of economic policy is possible. Similarly, an increasing number of social movements have protested against socially and environmentally damaging effects of privatization and liberalization policies, but this does not threaten the survival of the free-market economy in El Salvador. This ambiguous relationship of Salvadoran civil society to the free-market project has been illustrated by high levels of popular mobilization in demonstrations against the privatization of water services in 2007 and 2008 on the one hand, and 2008 survey results by Latinobarómetro on the other, which reveal that the country's levels of popular satisfaction with privatized services are among the highest in Latin America, with 47% of interviewees supporting privatization.

There are no significant anti-democratic veto actors in El Salvador.

The political leadership does not act consistently to prevent political cleavages from escalating into conflict. While there are no salient religious or ethnic cleavages in El Salvador, the society remains deeply divided by economic and social inequalities that translate into a polarized party system and civil society. During the period under review, the political leadership did not take adequate action to depolarize this division by compensating for gross social and economic inequalities or addressing poverty, malnutrition of children and the deficient infrastructure in rural areas. Rather, representatives of the state authorities tended to reinforce the dividing line between left- and right-wing groups in the Salvadoran society, which has contributed to the regular escalation of violence associated with electoral campaigns. An example of the conscious exacerbation of this right-left cleavage was government members' allegations of FMLN involvement in terrorist activities within El Salvador and elsewhere in Latin America. San Salvador's FMLN mayoral candidate, Violeta Menjívar, compared the violent attack by ARENA party activists against her campaign procession on 12 January 2009 to a "dirty war" carried out against left-wing politicians on behalf of the right-wing government. Nevertheless,

Consensus on goals

Anti-democratic
veto actors
Cleavage /
conflict
management

outside of the context of electoral campaigns, cleavage-based conflicts do not seem likely to escalate in the near future.

Several of El Salvador's international partnerships, such as those with the European Union or the Summit of the Americas, encourage the active participation of NGOs in the political decision-making process. However, despite these encouragements and the growing strength of Salvadoran civil society, civic organizations are rarely involved in the government's process of policy formulation. On the contrary, international and domestic observers have criticized the Salvadoran government for working closely with its traditional partner, the business sector, while hardly ever including non-business NGOs in its negotiations. Moreover, instead of attempting to overcome the polarization between left- and right-wing groups in El Salvador's civil society, the government has fueled the distrust between them. A case in point was accusations by ARENA representatives about the alleged involvement of the FMLN in terrorist activities. Associations with specific political and human rights agendas continue to face obstructions from state authorities, such as denials or delays in the approval of their legal standing. Journalists are frequently excluded from the political process due to irregular access to information at state agencies, or delays in the provision of public records.

Civil society participation

El Salvador's political leadership has made only sparse progress in addressing past acts of injustice, or initiating a process of reconciliation. Although state authorities complied with an IACHR ruling in January 2007 by approving an annual day of remembrance to commemorate the children who disappeared during El Salvador's civil war, most other recommendations have not been implemented. These additional recommendations include actions relating to the assassination of Archbishop Oscar Romero in 1980, the El Mozote massacre in the same year, and the murder of Mauricio Garcia Prieto in 1994. Moreover, despite domestic and international demands to abolish the 1993 General Amnesty Law, the government – supported in its position by the Roman Catholic archbishop of San Salvador – has continued to object to investigations into human rights violations during the civil war, arguing that the process would reopen wounds of the past. As a result, acts of injustice committed between 1980 and 1991 continue to be prosecuted by foreign courts, such as the case related to the 1989 murder of Jesuit priests that was officially opened by Spain's National Court in January 2009. The FMLN has traditionally sought repeal of the General Amnesty Law, but its presidential candidate for the 2009 elections, Mauricio Funes, declared in September 2008 that the party would no longer aim to abolish the law. Inefficient structures and corrupt practices within the judiciary contribute to the failure to address past acts of injustice or bring about a reconciliation process.

Reconciliation

17 | International Cooperation

The Salvadoran government makes efficient use of international partnerships to realize its domestic policy agenda, particularly in economic terms. In line with the government's objectives, El Salvador has actively pursued new trade agreements and built on existing ones as a means to promote economic growth and development. In 2007 and 2008, the government carried on negotiations regarding a free trade agreement with Canada as well as discussions on a new Association Agreement with the European Union which would include the establishment of a free trade area. El Salvador also benefited from the implementation of the DR-CAFTA in March 2006, which granted preferential access to U.S. markets and further liberalized trade among the Central American countries. Other free trade arrangements, including those with Colombia, Taiwan, Mexico and Chile, have been sustained. Additionally, the country's political leadership has negotiated loans with the World Bank and the Inter-American Development Bank, as well as a precautionary standby arrangement with the IMF designed to ameliorate any future effects of the global financial crisis.

Effective use of support

The Salvadoran government similarly uses international cooperation to pursue non-economic objectives. Such efforts include the World Bank-financed Judicial Modernization Project, aimed at improving the performance of El Salvador's justice system, and the Protected Areas Consolidation and Administration Project (PACAP), largely financed by the Global Environment Facility, which is meant to strengthen the country's Natural Protected Areas System.

These projects demonstrate the government's willingness to make use of international assistance for specific policy goals including economic and ecological standards. However, other recommendations from bi- or multilateral partners, such as the European Union's advice to include civil society organizations in the political decision-making process, have been largely ignored by the political leadership.

El Salvador has established itself as a credible and reliable partner in the international community, due to its engagement in economic and trade agreements such as DR-CAFTA, its commitment to political dialogue with other Central and Latin American countries in the framework of Central American Integration System (SICA), and by providing humanitarian and military aid on a global scale. Ties with the United States continue to be strong, in part because of trade relations and the substantial community of 2.5 million Salvadorans living in the United States. Troops from El Salvador remained in Iraq longer than those of any other Latin American nation, although President Saca announced in December 2008 that the country's soldiers would be withdrawn after the end of the year. In November 2007, the U.S.-based International Republican Institute (IRI) honored Saca with the 2007 Freedom Award for his leadership in promoting El Salvador's democratic and

Credibility

economic development, and praised his efforts to defend freedom at home and abroad. The European Union, El Salvador's third most important trading partner after the United States and the group of other Central American countries, has likewise commended the political leadership's constant efforts toward the establishment and maintenance of international partnerships.

The Salvadoran political leadership promotes and maintains stable economic and political relations with neighboring countries within the framework of trade agreements such as DR-CAFTA, and of international organizations such as the Central American Parliament (PARLACEN), SICA and the Conference of Central American Armed Forces (CFAC). El Salvador and Honduras enjoy normal diplomatic and trade relations despite persistent territorial disputes. The two countries reached a final agreement on the demarcation of their land border in 2006, following two rulings of the International Court of Justice (ICJ) and a survey by the OAS. Disputes over their maritime borders remain, as both El Salvador and Honduras claim the small Conejo Island in the Gulf of Fonseca, which was not explicitly mentioned in the ICJ decision.

Regional
cooperation

Strategic Outlook

El Salvador's transformation progress has been somewhat unbalanced, as major achievements towards a fully consolidated free market economy have been coupled with a lack of substantive social or political reforms which would help deepen democracy. Economically, the political leadership succeeded in establishing El Salvador as one of the most open trade and investment environments in Latin America, and as a reliable and credible partner in numerous free trade agreements. International observers such as the OECD and IMF particularly commend the progress in the country's competition policy and the solidity of its macroeconomic fundamentals despite the global financial crisis.

On the other hand, the Salvadoran government has failed to adequately address political and social issues which not only challenge the state's authority but also hinder the further deepening of democracy. These issues include corruption inside state agencies, high rates of poverty and crime, gross socioeconomic inequalities, a deficient infrastructure in rural areas and human rights violations. The exacerbation of the left-right cleavage by defamation-based electoral campaigns, the failure to implement the Voto Residencial nationwide for the 2009 elections and the political leadership's unwillingness to include civil society organizations in the political decision-making process are particularly concerning, as each has contributed to political alienation and disillusionment with democracy. This risk was illustrated by the 2007 "crisis of faith" in democracy, in which only 38% of survey respondents preferred democracy to any other form of government and by opinion polls from May 2008 which showed that as many as eight out of 10 Salvadorans were dissatisfied with the leadership of President Saca and ARENA.

The government of El Salvador needs to commit itself to substantive political and social reforms in order to overcome these challenges. It has to recognize that high rates of crime (which are directly associated with poverty and socioeconomic inequalities), low levels of schooling and an inefficient judiciary not only affect the social and political realm, but also create obstacles to the country's long-term economic development insofar as they constrain business and investment opportunities. The political leadership furthermore needs to distance itself from defamation-based electoral campaigns, as these conflict with the long-term aim of political inclusion and might even jeopardize democratic stability. To strengthen the population's trust in democratic institutions and moderate the apparent polarization between left- and right-wing groups, political office holders need to show more willingness to compromise. The Voto Residencial should be implemented as soon as possible in order to enable more political participation particularly among rural communities.

El Salvador's trading partners ought to contribute to the prioritization of social and political issues by putting greater emphasis on human rights and the participation of civil society organizations in the political decision-making process. Moreover, international actors should

encourage the establishment of welfare institutions that compensate for gross socioeconomic inequalities among the Salvadoran population.

With the victory of FMLN's candidate Mauricio Funes in the March 2009 presidential elections, El Salvador has now joined the recent wave of left-of-center governments in Latin America. The greatest challenge for this first left-wing presidency since the beginning of the Salvadoran transformation process will be to pursue relevant political and social reforms in order to overcome persistent socioeconomic problems, while at the same time deepening democracy.