

## ENVIRONMENTAL AND SOCIAL MANAGEMENT REPORT

### MACQUARIE MEXICAN INFRASTRUCTURE FUND

(ME-L1096)

- 1.1 **Description of the Fund.** The purpose of Macquarie Mexican Infrastructure Fund (Fund) is to make investments in a diversified portfolio of infrastructure-related projects and companies in Mexico. It is anticipated that the Fund will make between 10 to 15 investments, assuming the Fund reaches its target size, which will be in the form of debt, equity, equity-like or other investments in a diversified portfolio of infrastructure assets in Mexico (which may include sectors such as social infrastructure (hospitals, schools, etc), construction or modernization of toll roads, railroads, ports, airports, water and sewage infrastructure, and telecommunication), that, in the opinion of the Fund Manager (as defined below), are expected to generate predictable cash flows over the long term and exhibit sustainable competitive advantages. The Fund reached its initial closing in December 2009 with total commitments of approximately US\$410 million raised with Mexican pension funds, the Mexican National Fund for Infrastructure (Fonadin) and the Macquarie Group (Macquarie).<sup>1</sup> As of November 17, 2010, the Fund has made no investments and MMIF Compañía Controladora, S.A.P.I. de C.V. (Borrower), a promoted company of the Fund through which the Fund intends to make infrastructure investments, is seeking a US\$150 million loan from the IDB. In addition, the Fund is seeking to raise further commitments from local institutional investors as well as from international institutional investors to reach a target size of US\$1,100 million.
- 1.2 **Fund Manager.** The Fund is managed by Macquarie México Infrastructure Management, S.A. de C.V. (Fund Manager) part of Macquarie. Macquarie is one of the largest dedicated specialist fund managers in the world. [http://www.macquarie.com.au/au/corporations/sfpc/infrastructure\\_funds/overview.htm](http://www.macquarie.com.au/au/corporations/sfpc/infrastructure_funds/overview.htm) The International Finance Corporation (IFC) and the European Bank for Reconstruction and Development (EBRD) have supported Macquarie managed funds in India, East Europe and Africa. As such, Macquarie is experienced with the environmental and social requirements of Multilateral Development Institutions (MDIs).
- 1.3 **IDB Environmental Impact Category.** Based on Directive B.13 of the Environment and Safeguards Compliance Policy (OP-703), the Fund is classified as a Flexible Lending Instrument (financial intermediary) and therefore is not categorized according to its potential environmental and social impacts and risks. However, given the Fund's target

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<sup>1</sup> Fonadin was established in Mexico by Banobras with an initial capitalization of MX\$40 billion with the purpose of promoting private investment for infrastructure development in Mexico. The Bank has established a technical cooperation with Fonadin to support the preparation and appraisal of infrastructure projects.

investments (e.g. construction or modernization infrastructure, including roads, railroads, ports, airports, and water and sewage) it is expected that some of the individual transactions will involve significant environmental and social, health and safety and labor impacts and risks and would fall into categories A and B under the Bank's environmental and social classification system. Consequently, this transaction is considered a financial intermediation operation with significant risk.

- 1.4 **Environmental, Social, Health and Safety and Labor Impacts and Risks.** The Fund is designed to invest in infrastructure projects and related companies and in sectors that are likely to have potentially significant environmental, social, health and safety and labor impacts and risks (direct, indirect or cumulative). The Fund's pipeline of potential investments to date includes three roads projects, three renewables projects and a social infrastructure opportunity in Mexico. A very preliminary screening of the potential investments by the IDB has not identified complaints, the need for resettlement, affectation of critical natural habitats or cultural sites or any significant impact or risk that could not be controlled and managed by the implementation of mitigation measures in accordance with the IDB's or the International Finance Corporation's (IFC) environmental and social safeguards. In any case, each and every investment and the respective environmental and social aspects will have to be identified, analyzed and managed on a project-by-project basis. The specific environmental and social impacts and risks will be those related to or caused by each specific project investment and will be evaluated and managed in that context.
- 1.5 Some of the projects in the pipeline of potential investments might not materialize and thus other projects will be considered in the investment period of the Fund. The impacts of potential infrastructure projects will be diverse and their significance will depend on project characteristics, such as size, sector, and location. Potential impacts and risks will include aspects of pollution and contamination from the construction and operation of infrastructure as well as risks related to the insertion of the projects in certain specific contexts, including any resettlement, impacts on indigenous peoples, impacts on natural habitats and other social and environmental impacts that could trigger other Bank safeguard policies such as the Information Disclosure Policy (OP-102), Natural Disaster Risk Management Policy (OP-704), Involuntary Resettlement Policy (OP-710) and Indigenous People Policy (OP-765). In addition, there could be other issues commonly associated with the construction of large infrastructure projects such as labor management aspects, and workers' health and safety. Most of the projects to be supported by the Fund are also likely to have public disclosure in accordance with both OP-703 and OP-102.
- 1.6 **Management of Environmental and Social Aspects.** As with other infrastructure funds, staff of the Fund Manager will be ultimately responsible for screening, assessing and

managing the environmental and social aspects, and ensuring that projects and their sponsors implement the respective commitments included in the Fund's Environmental and Social Management System (ESMS). Macquarie has developed several ESMS for funds in India, East Europe and Africa, which have been supported by the IFC and the European Bank for Reconstruction and Development (EBRD). Macquarie is experienced with the environmental and social requirements of Multilateral Development Institutions (MDIs) and it should be relatively simple for IDB and Macquarie to agree on an ESMS that accounts for IDB policies and procedures with respect to environmental, social, labor and health and safety aspects of the proposed Fund's relevant operations.

- 1.7 IDB, the Borrower and the Fund Manager will agree the key elements of the ESMS such as: screening of subprojects against exclusion criteria, impact categorization of proposed subprojects, undertaking of due diligence and monitoring procedures commensurate with the levels of impacts, the structuring of subprojects so that they meet environmental requirements, and where necessary require corrective actions and provide adequate legal remedies. In addition, when a subproject involves activities determined as high environmental and social impact, the subproject will be referred proactively to the IDB early in the due diligence process to enable the IDB to undertake any complementary analysis.
- 1.8 **Requirements for Investments for which IDB Resources are to be Used.** The IDB will require that the environmental, social, health and safety and labor aspects of potential investments for which the IDB facility is to be utilized during the investment period and eventually of its corresponding portfolio during the life of the loan or Fund be managed in accordance with the IDB Safeguard Policies and the ESMS, and that adequate resources be guaranteed for the successful implementation of the ESMS. In addition, special emphasis will be placed in ensuring the implementation and legal availability of measures and mechanisms to address any non-compliances with IDB policies or unmitigated environmental and social impacts or risks during the execution of relevant Fund investments. While the Bank has agreed on the principles of the ESMS, a final version of the ESMS will be required prior to Financial Closure and in any case before the Fund makes any investment, whichever occurs first. As part of the contractual arrangements and/or of the ESMS, the Borrower will commit to obtaining the IDB's non-objection prior to making an investment in a category A project using IDB resources. Contractual arrangements between the IDB and the Borrower will also include routine reporting and supervision as well as the implementation of audits and corrective action plans as needed to identify and remedy non-compliance. The Bank's environmental specialists will monitor the implementation of the ESMS closely, and in coordination with the Borrower, will closely supervise this operation, including the performance of a representative sample of investments, to ensure the proper functioning of the ESMS, and

satisfactory with the environmental and social requirements applicable to each sub-project.