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DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

EL SALVADOR, GUATEMALA, AND HONDURAS

FINANCING AND RISK MITIGATION PROGRAM FOR STRATEGIC INVESTMENTS IN THE NORTHERN TRIANGLE COUNTRIES

RG-O1667

PROPOSAL TO ESTABLISH CONDITIONAL CREDIT LINES FOR INVESTMENT PROJECTS (CCLIP)

(ES-O0005 - GU-O0004 - HO-O0004)

LOAN PROPOSAL

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CONTENTS

LINKS

REQUIRED

1. Environmental and Social Management Report (ESMR)

OPTIONAL

1. Socioeconomic Context: Northern Triangle Countries
2. The Infrastructure Gap in the Northern Triangle
3. Migration in the Northern Triangle
4. Climate Change Vulnerability and Resilient Infrastructure
5. Accomplishments – Progress made by the Plan of the Alliance for Prosperity in the Northern Triangle
6. The IDB's Role in the Northern Triangle
7. Northern Triangle Regional Infrastructure Plan
8. Preliminary identification and description of potential projects

ABBREVIATIONS

BLEND	Concessional Ordinary Capital
CCLIP	Conditional Credit Line for Investment Projects
CID	Country Department Central America, Haiti, Mexico, Panama and the Dominican Republic
CNE	National Energy Council of El Salvador
DEM	Development Effectiveness Matrix
ESMR	Environmental and Social Management Report
FITUR	Fondo de Inversión, Promoción y Fomento del Turismo [Tourism Investment, Promotion, and Development Fund]
IFIs	International Financial Institutions
IMF	International Monetary Fund
INDE	National Electrification Institute of Guatemala
INVEST-H	Honduran Strategic Investment
MCIV	Guatemalan Ministry of Communications, Infrastructure, and Housing
MEM	Guatemalan Ministry of Energy and Mining
MM-II	Multisector modality II
MOPTVDU	Salvadoran Ministry of Public Works, Transportation, Housing, and Urban Development
OC	Ordinary Capital
PAPTN	Plan of the Alliance for Prosperity in the Northern Triangle
PPP	Public-Private Partnership
SAT	Office of the Superintendent of Tax Administration of Guatemala
SIEPAC	Central American Electric Interconnection System
SMEs	Small and Medium-Sized Enterprises
VPC	Vice Presidency for Countries
VPS	Vice Presidency for Sectors
WEF	World Economic Forum

PROJECT SUMMARY

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Financial Terms and Conditions	
Borrowers: Republic of Guatemala; Republic of Honduras; and Republic of El Salvador.	
Executing agencies: Sector ministries/secretariats of Guatemala, Honduras, and El Salvador; the Honduran Fondo de Inversión, Promoción y Fomento del Turismo [Tourism Investment, Promotion, and Development Fund] (FITUR) and/or Invest-H; and a Salvadoran infrastructure vehicle	
Liaison institutions: Guatemalan Ministry of Public Finance, Honduran Ministry of Finance, and Salvadoran Ministry of Finance	

Financing instruments	Source	Amount (US$ millions)	%
El Salvador CCLIP	**Ordinary Capital (OC)**	250	35.7
Guatemala CCLIP	**OC**	250	35.7
Honduras CCLIP	**BLEND OC**	200	28.6
Total		700[a]	100.0

Conditional Credit Lines for Investment Projects (CCLIPs)	
Term:	10 years
Amortization period:	n/a
Disbursement period:	n/a
Grace period:	n/a
Interest rate:	n/a
Credit fee:	n/a
Inspection and supervision fee:	n/a
Weighted average life (WAL):	n/a
Approval currency:	U.S. Dollars

Project at a Glance
Project objective/description: This program's general objective[b] is to help revitalize strategic productive sectors in the national territories of Northern Triangle countries through the financing of public investment projects in infrastructure, promoting private investment and the generation of economic opportunities for the population. The specific objectives are: (i) to provide financing for public infrastructure to promote and revitalize strategic productive sectors and private investment in infrastructure; (ii) to foster the creation of jobs and opportunities for the population; and (iii) to modernize and expand sustainable productive infrastructure to accelerate growth and strengthen regional integration.
Special contractual conditions precedent to the first loan disbursement: To be determined based on each individual operation.
Special contractual conditions for execution: To be determined based on each individual operation.
Exceptions to Bank policies: None.

Strategic Alignment			
Challenges:[c]	SI ☑	PI ☑	EI ☑
Crosscutting Issues:[d]	GD ☐	CC ☑	IC ☑

[a] The total amount available for the three Northern Triangle countries may not exceed US$700 million. The amounts available for financing each individual operation under each CCLIP will be determined based on the Bank's fiscal year programming exercise with each country in coordination with IDB Invest.

[b] The program's estimated total cost is US$750 million to be financed through three individual CCLIPs for El Salvador, Guatemala, and Honduras. To supplement the CCLIPs, and an investment loan operation of up to US$50 million is considered for Honduras to finance investment projects through FITUR. The preparation and processing of the loan will be undertaken separately from the processing of this operation (paragraphs 1.27, 2.5, and 2.6(b)). This document presents the establishment of each of the CCLIPs for approval by the Bank's Board of Executive Directors in accordance with the provisions of the attached proposed resolutions. The investment loan operation for Honduras will be processed independently, in parallel with this operation.

[c] SI (Social Inclusion and Equality); PI (Productivity and Innovation); and EI (Economic Integration).

[d] GD (Gender Equality and Diversity); CC (Climate Change and Environmental Sustainability); and IC (Institutional Capacity and Rule of Law).

I. PROGRAM DESCRIPTION AND RESULTS MONITORING

A. Background, problem to be addressed, and rationale

1.1 **General socioeconomic context of the Northern Triangle.** The Northern Triangle countries (El Salvador, Guatemala, and Honduras) account for nearly 50% of the GDP of Central America and 67% of its population. These countries are characterized by a moderate economic growth[1] that is inadequate for poverty and inequality reduction. On average, over half of the population lives below the poverty line,[2] and poverty rates are particularly high in rural areas with significant variations throughout the region. Therefore, Northern Triangle countries need to attract investment in strategic productive sectors to increase productivity and sustain employment[3] (optional link 1).

1.2 **Fiscal and external context.** The Northern Triangle countries are facing an average fiscal deficit of 2.4%,[4] trending downward due to fiscal consolidation efforts. El Salvador has relatively high debt levels (60% of GDP[5]), while debt is 44% of GDP in Honduras. Although Guatemala's debt is 24% of GDP, the country's greatest fiscal vulnerability is its total revenue (10% of GDP). Guatemala's current fiscal deficit of 1.2% of its GDP is equivalent to slightly over 10% of its revenue.

1.3 The 2007-2008 global financial crisis created a need for countercyclical policies, which left persistent fiscal deficits and put downward pressure on public investment (primarily in infrastructure).[6] Both Honduras and El Salvador have recently had Stand-By Arrangements with the IMF due to their fiscal situations. Looking forward, these countries will become increasingly vulnerable due to the recent increase in oil prices, higher interest rates on international markets, and the corresponding increase in the cost of public debt service. Return migration may also lead to higher social expenditures and a decline in family remittances from the United States. The Northern Triangle countries' current account balances have improved as a result of lower oil prices (-1.8% of GDP on average) offsetting the trade deficit (-12.5% of GDP on average). Attracting foreign direct investment remains essential to balancing the external front. In 2015, the Bank supported Honduras with a policy-based loan (PBL), the Fiscal Consolidation Support Program (document PR-4344), to address issues such as liabilities from public-private

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1 Northern Triangle countries grew an average of 3.1% between 2005 and 2015, but per capita GDP growth has been low (less than 1%) in comparison to the average population growth rate of 1.4%. There is also a lack of creation of advancement opportunities for a predominantly young population, of which 30% of young people aged 14 to 25 (1.7 million) do not work or study (Driving employment generation and security in the Northern Triangle of Central America, McKinsey, July 2017).

2 Poverty rates are 59.3% of the population in Guatemala, 65.7% in Honduras, and 32.7% in El Salvador, according to official data from 2016 (National Statistics Institutes from each country).

3 Estimates indicate that 5.8 million individuals in the Northern Triangle face severe employment vulnerability (500,000 are unemployed while 5.3 million work in informal or vulnerable employment conditions).

4 In 2017, Guatemala recorded an overall fiscal deficit of 1.2% of GDP, while El Salvador's deficit was 2.5% of GDP, and Honduras's was 3.5% (2017).

5 World Economic Outlook Database, International Monetary Fund (IMF).

6 According to InfraLatam, public investment in transportation infrastructure in Guatemala declined from 1.5% of GDP in 2008 to 0.47% in 2015. In El Salvador, the decrease over a similar period was from 0.92% to 0.79% of GDP, whereas in Honduras it was from 1.11% to 0.69% of GDP.

partnerships (PPPs), which had climbed to 8% of GDP. As part of that program, Honduras agreed to set a legal limit on the total volume of PPPs at 5% of GDP (the current level is 6% of GDP). Honduras's fiscal management of PPPs has improved with the assistance provided by the Bank's Fiscal and Municipal Management Division (IFD/FMM). However, the country must continue to closely monitor potential risks from PPPs and the maximum limit of the stock of investments in PPPs as a percentage of GDP.

1.4 **Growth outlook.** Average yearly economic growth rates are expected to hover around 3.1% for the next three years. Despite the positive outlook on future growth, Northern Triangle countries will face significant challenges in producing inclusive growth in light of the risks associated with a possible increase in oil prices, an increase in international interest rates, and changes to U.S. trade policy (the Northern Triangle countries' main trading partner). At the same time, the potential decline of remittances and the reintegration of returning migrants could have significant macroeconomic and social impacts (paragraph 1.10).

1.5 **Structural factors that limit growth.** Low investment levels, informality, and insecurity are three structural economic constraints to economic growth and an improved business climate (attracting investment) in all three countries, causing a vicious cycle of low productivity and noninclusive growth:

a. **Low investment levels:** Gross capital investment in the Northern Triangle countries averages less than 19% of GDP, nearly half the verified amount in emerging developing countries. In particular, the growing infrastructure gap (paragraph 1.6) and the limited availability of quality education, health, and nutrition services hinder future growth and perpetuate low, noninclusive growth. In addition to the lack of significant investment and scant capital formation, the concentration of economic activity in production chains that have low added value and high levels of informality significantly hinders productivity, these countries' ability to absorb skilled workers, and to competitively engage in international trade.

b. **Informality:** Estimated informality rates are around 63% of GDP in El Salvador and 74% of GDP in Guatemala and Honduras. High informality rates inhibit inclusive growth by restricting formal sector development, productivity growth, public resources, and access to quality jobs. Informal employment affects 55% of the workforce (5.3 million workers).

c. **Insecurity:**[7] The Bank's recent estimates indicate that the welfare costs of crime and violence as a percentage of GDP amount to 6.1% of GDP in El Salvador, 6.5% of GDP in Honduras, and 3% of GDP in Guatemala (without including the indirect costs of emigration), as a result of homicide rates as high as 60 to 103 per 100,000 inhabitants and significantly higher than the regional average of 26. These high social costs are specifically associated with high rates of violent crime (homicides and assaults), private sector losses and security costs, and crime-related government expenditures. The Northern Triangle countries also have the highest femicide rates in the region.

[7] "The Costs and Crime of Violence: New Evidence and Insights in Latin America and the Caribbean" (IDB, Laura Jaitman, IDB-MG-510, 2017).

1.6 **The infrastructure gap.** On average, Northern Triangle countries have invested 2.2% of their GDP on infrastructure (2008-2015). This level of investment is equivalent to less than half of the investment required to reduce their infrastructure gap compared to emerging and developed countries (5% of GDP[8]). Infrastructure deficiencies give rise to high freight costs,[9] high electricity costs,[10] border hub delays, and limited connectivity, which make developing more highly productive activities in the formal sector difficult and result in an export matrix that is geographically concentrated in few products. The region struggles with high logistics costs (equivalent to 30%-35% of the value of exported products), which are an obstacle to competitive trade integration, attracting productive investment, and value chain integration (optional link 2).

1.7 **Institutional weaknesses in infrastructure management.** The region still faces significant obstacles in the timely execution of public-private infrastructure investments. In the IDB's experience, the poor rates of executing the infrastructure project portfolio result directly from: (i) a portfolio of projects that poses challenges in terms of planning, preparation, and implementation; (ii) the long legislative processes for the approval of financing contracts; (iii) difficulties in preparing and evaluating competitive bidding processes; and (iv) weak oversight of awarded contracts. More resources are needed to consolidate a preinvestment process that is conducive to initiating soundly prepared projects and facilitates timely project execution. Innovative mechanisms for expediting the execution of priority projects are also needed to attract private financial resources given the fiscal context in the Northern Triangle.

1.8 **The private sector's role in infrastructure financing.** Public investment has played a central role in infrastructure financing in Northern Triangle countries. Although the private sector has actively participated in the energy and telecommunications sectors, its involvement in other key productive sectors (e.g., transportation, water and sanitation, etc.) has been limited. In a context of fiscal deficits and decreasing public investment, these countries need innovative mechanisms to spark a significant growth in private infrastructure investment. According to the World Economic Forum (WEF),[11] Guatemala is ranked 106th of 137 in infrastructure quality, while El Salvador is ranked 93rd and Honduras is ranked 80th. Attracting greater private financing will require medium- and long-term efforts to improve the business climate, reduce country risk, strengthen capital markets, and create economies of scale at the project level to more successfully

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8 Several studies have suggested that Latin American and Caribbean countries need to invest around 5% of GDP in infrastructure over an extended period of time in order to close this gap (IDB, 2014, 2013; Bhattacharya et al., 2012; ECLAC, 2011; Kohli and Basil, 2010; Fay and Yepes, 2003; Calderón and Servén, 2003; Perrotti and Sanchez, 2011).

9 The average ground freight cost in the region is approximately US$0.17 per ton-kilometer for international trade, while it ranges from US$0.20 to US$0.60 for domestic routes with low levels of competition. In more developed countries, ground freight costs are less than US$0.10 per ton-kilometer, while in other developing regions (e.g., Africa), average ground freight costs do not exceed US$0.10 to US$0.13 per ton-kilometer.

10 High electricity costs are a major challenge for the region. Wholesale prices in Central America fluctuate around US$150 per megawatt hour (as of December 2017, US$185 was the median regulated price; US$153.30 in El Salvador and US$139 in Honduras), compared to US$50 per megawatt-hour for comparable electricity systems.

11 WEF, "The Global Competitiveness Report 2017-2018."

attract international investors. These countries' experience with PPPs is limited to the sectors indicated above.[12] Ensuring healthy competition and high levels of participation in competitive bidding processes, limiting changes to contracts after they have been awarded, achieving effective mechanisms for risk transfer and managing contingent liabilities, and strengthening public sector capacity and transparency continue to be significant challenges to attracting higher levels of private investment. This program will help reduce obstacles to private sector financing and will act as a catalyst for greater private investment in productive infrastructure.

1.9 **Underdeveloped financial markets.** Northern Triangle countries have a stable and profitable banking system. Private sector credit accounted for a high percentage of total assets (73% on average[13]), with credit for household consumption (El Salvador) and the corporate sector (Honduras - El Salvador) being highly dynamic sectors. Forty-six banks operate in the subregion, and foreign banks maintain a significant presence in El Salvador and Honduras (91% and 42.5% of assets, respectively) with access to external financing. Past-due portfolio rates in the Northern Triangle are less than 3%. However, the three countries should redouble their efforts to promote more competition in the financial market, make headway in banking the unbanked and financial inclusion efforts, and expand the coverage of long-term financing products such as project finance. In particular, capital markets need to be developed in a way that expands long-term financing sources for the productive sector. Each individual market's size is a challenge for international investors, given the relatively low project amounts. The lack of financial instruments and risk mitigation mechanisms resulting from these markets' lack of depth limits private infrastructure financing in particular. This program attempts to expedite the introduction of innovative financing mechanisms to attract strategic investment in line with national legislation.

1.10 **Employment needs – return migration.** Northern Triangle countries have faced constant, increasing emigration flows (over 10% of their populations, on average) provoked by limited economic and employment opportunities, violence, and the desire for family reunification. The lack of access to formal, stable, and well-paid employment opportunities has produced high unemployment and underemployment rates in all three countries, which have particularly affected the young population (under 25 years old). Estimates indicate that more than 5.8 million jobs can be classified as vulnerable because of their informal nature. Faced with this potential decline in remittances and the wave of returning immigrants, Northern Triangle countries need to absorb additional workers and sustain economic growth. This program will therefore support economic growth and job creation by acting as a catalyst for public and private investment to finance productive infrastructure (optional link 3).

[12] According to InfraLata, Guatemala financed three transportation projects with private resources totaling US$154 million from 1990 to 2016; Honduras financed seven projects totaling US$1.27 billion, and El Salvador has no such experience to date. As for water and sanitation projects, Honduras has experience with private investments totaling US$208 million and Guatemala has one experience with private investment totaling US$7 million.

[13] Source: Office of the Executive Secretary of the Central American Monetary Council.

1.11 **Climate change vulnerability.** Northern Triangle countries are highly vulnerable to extreme weather events and climate change, which continues to have a considerable impact on the region's existing infrastructure. Worldwide, Honduras has been the country that has suffered the most economic impact in terms of deaths and economic losses from extreme weather events over the past 20 years (1997-2016). Guatemala and El Salvador are ranked 10th and 15th respectively (Global Climate Risk Index 2017). Climate change scenarios for Northern Triangle countries generally point to higher temperatures, lower annual precipitation, and increased extreme participation in several parts of the region. The need to invest in resilient infrastructure is crucial, which is why all three Northern Triangle nations have identified the matter as a priority in their Nationally Determined Contributions (NDC).[14] This program seeks to help develop resilient infrastructure in the region, thereby mitigating the impact of climate change (for more information about climate vulnerability and the methods and tools used to prioritize and include resilient features in the projects to be financed by this program, see optional link 4).[15]

1.12 **Plan of the Alliance for Prosperity in the Northern Triangle (2014).** The Plan of the Alliance for Prosperity in the Northern Triangle (PAPTN) is an initiative by the three governments to create socioeconomic development conditions that would dissuade the local population from emigrating. After PAPTN implementation began in 2015, the governments agreed to work together to address factors identified as the causes of the flow of undocumented migrants who head primarily to the United States and Mexico since 2010. The countries agreed to a joint strategy that has defined four strategic priorities:

a. Invigorating the productive sector through the promotion of strategic sectors and employment; investments in connectivity, logistics, and energy; and access to financing and strengthening small and medium-sized enterprises (SMEs).

b. Improving citizen security and access to justice.

c. Developing human capital.

d. Strengthening institutions and enhancing transparency.

1.13 **PAPTN country resources and achievements.** As of 2016, the three countries have earmarked in their respective budget laws an aggregate amount of US$8.577 billion in resources for implementing PAPTN initiatives. The plan has managed to make the region's social and investment climate more favorable, with advances in four core areas: (i) improvements to citizen security and access to justice, with additional resources being allocated to strengthen the legal system and security forces and coordinated actions to fight crime and violence; (ii) tax and public administration/procurement system reforms (fiscal-customs) to improve revenue collection and transparency; (iii) support for human capital development, including improvements to basic social safety net services, comprehensive women's services, and return migration services, along with communication

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[14] http://www4.unfccc.int/submissions/indc/Submission%20Pages/submissions.aspx.

[15] The team is working to prepare a technical cooperation project that would finance, in part, preinvestment activities to ensure that climate risk studies and evaluations are included in the CCLIP projects financed under this program. The team has tentatively identified funding sources, which include the NDC Pipeline Accelerator Multi-Donor Trust Fund (document GN-2890).

campaigns to reduce illegal migration; and (iv) support for the productive sector, through investments in infrastructure, electricity matrix diversification, and customs integration, and SME financing support. PAPTN accomplishments and budget allocation details by country and by major donor are summarized in optional link 5.

1.14 **The Bank's technical and financial role in the PAPTN.** The Bank has supported the Plan's initiatives from its inception. Through its Country Department Central America, Haiti, Mexico, Panama, and Dominican Republic Country Department (CID), in coordination with the Vice Presidency for Sectors and the Bank's respective Country Offices, the Bank provides advisory support and technical assistance, supporting Plan execution and budgetary appropriations, facilitating country dialogue at a public-private level, coordinating with donors, and organizing high-level events.[16] The Bank has an outstanding portfolio in the three Northern Triangle countries of 31 operations and an undisbursed loan balance of nearly US$1,236,500,000, which is itemized in optional link 6.

1.15 **Northern Triangle Strategic Priorities (2017-2022).** After discussions with international donors and evaluating the progress that has been made, the three governments have identified three priorities for the 2017-2022 five-year period: (i) employment and growth; (ii) institutional framework and transparency; and (iii) security. The priority action areas are summarized below:

Table 1. Strategic Issues for 2017-2022

Growth and employment	• Macroeconomic stability • Attracting investments (infrastructure - productive sectors) • Business climate improvement • Regional integration • Migration cooperation
Institutional framework and transparency	• Fighting corruption • Strengthening the justice system • State efficiency - increase tax revenue collection
Security	• Security in the flow of goods • Security in the flow of people • Citizen security • Regional cooperation

1.16 In order to attract the private capital needed to drive the region's productive transformation, the three governments agreed[17] to adopt measures to increase competitiveness, improve the business climate, and reduce the economic infrastructure gap. A consensus was reached on five basic guidelines: (i) strategic sector promotion and attracting investment; (ii) electricity service improvements; (iii) road infrastructure and logistics corridors modernization and expansion; (iv) coordinated border management; and (v) facilitating international trade. The

[16] The Bank's technical responsibilities include: advising each government on PAPTN strategies and activities; ensuring that programs and projects align with PAPTN objectives; encouraging broad participation (of representatives from civil society, academia, the private sector, and local governments) in the planning, implementation, and evaluation of PAPTN programs and projects; ensuring transparency in program and project execution; supporting country decisions and issuing recommendations for reports and evaluations; encouraging participation by the international community; and designing and implementing a communication strategy to inform citizens about PAPTN progress.

[17] Conference on Prosperity and Security in Central America, Miami, United States, June 2017.

private sector has expressed its commitment to encouraging private investment in infrastructure and strategic sectors. Regular meetings between public and private sector representatives from the three countries in 2017 and the most recent Northern Triangle summit held in Miami on 16 June 2017 prioritized quality infrastructure development as a catalyst for economic development and job creation in the Northern Triangle. In these discussions, the private sector was assigned an essential role in financing. This program's financing instruments will support the financial architecture that has been proposed by the three countries (paragraph 1.22) to make strategic sector growth viable and expedite the development of transportation, energy, and water and sanitation infrastructure, thereby adding value to the financing chain and acting as a catalyst in attracting financing resources from several sources.[18]

1.17 **Program rationale.** This program will help revitalize strategic productive sectors in Northern Triangle countries through financing for public investment projects in infrastructure, promoting the creation of economic opportunities for the population and private investment. It aims to reduce the infrastructure gap, act as a catalyst for greater private sector financing in productive development, create new job opportunities to dissuade the local population from emigrating and decrease migrant flows, address institutional weaknesses in infrastructure management, and strengthen all three countries' capacity for developing resilient infrastructure.

1.18 The program[19] provides a regional and national approach for the development of the infrastructure investment agenda. It will help the Northern Triangle countries develop the PAPTN regional agenda while acknowledging important specific circumstances of each country in the process of mobilizing private resources for investment in infrastructure, in consolidating the expected institutional framework, and in strengthening infrastructure management. This regional approach with flexibility at the national level will enable individual progress toward the objective of regional consolidation with specific national actions generating the necessary scale and commitment. The commitment of the public and private stakeholders of all three countries was demonstrated at the Northern Triangle summit (paragraph 1.16) as well as during 2016-2018 with the national advances in the context of the PAPTN (paragraph 1.13), in the formation of the funds and with the work done to identify and prioritize strategic sectors and projects to narrow the infrastructure gap (paragraph 1.19). The Bank has supported the countries in these areas and in the preparation of a program that will enable them to continue moving forward with the regional and national objectives under the Northern Triangle development agenda. It currently remains very important to continue supporting the coordinated efforts to promote growth and employment with a regional vision, while clearly differentiating the realities of each country.

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[18] The IDB Group will not only provide its own resources to support this effort at the country level, but also expects that its participation will act as a catalyst for contributions from the private sector, other donor countries, institutional investors, and potential donors.

[19] On an exceptional basis, the program is being led by the Country Department Central America, Haiti, Mexico, and the Dominican Republic (VPC/CID) to address the nature of the program as support for the PAPTN that is: (i) multi-institutional (IDB Group), including the role in the programming (IDB) and the pipeline (IDB Invest) of the Representative in each country; (ii) multisector, based on the demand of the countries; and (iii) tailored to national and regional characteristics. However, each of the individual operations under the CCLIPs will be led by the sectors (VPS).

1.19 **The IDB Group's knowledge in this sector.** The IDB Group has vast experience in financing infrastructure projects in Northern Triangle countries. Since 2000, the IDB Group has approved 47 sovereign guaranteed operations for US$2.087 billion (20 transportation sector operations for US$688 million, 11 energy operations for US$510 million, 6 water and sanitation operations for US$196 million, and 10 strategic sector support operations for US$693 million). The Bank has promoted regional integration with its support for projects such as: (i) the modernization of the Pacific Corridor, with US$269 million in operations for Northern Triangle countries; and (ii) the development of the Central American Electric Interconnection System (SIEPAC[20]), for which the Bank provided US$255 million of the required investment of US$505 million. The IDB Group has also participated in several projects with private sector and/or donor country cofinancing and in infrastructure funds (through the IDB's now-defunct Structured and Corporate Financing Department (SCF) and IDB Invest).[21] Recently, the IDB approved the First Operation of the Agua Negra Pass International Tunnel Construction Program (4338/OC-RG) and the Program to Support Productive Infrastructure Financing in Argentina (4502/OC-RG, Investment Guarantee Facility). The Bank has provided technical and financial resources to support the Northern Triangle countries' efforts to establish Infrastructure Funds in Guatemala and Honduras[22] and define a Regional Infrastructure Investment Plan that identifies potential needs for approximately US$11.370 billion in investment in transportation, energy, and border cooperation (optional link 7).

1.20 **IDB country strategies.** This program is aligned with the IDB country strategies with the three Northern Triangle countries. The program aligns with the 2015-2019 country strategy with El Salvador (document GN-2828) through its improving logistics infrastructure priority area, whose objectives include: (i) improving connectivity between production hubs and markets by strengthening infrastructure and transportation services; and (ii) promoting Mesoamerican regional integration. The program is also aligned with the strategy's energy dialogue area. The program aligns with the 2015-2018 country strategy with Honduras (document GN-2796-1)

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20 SIEPAC is a power transmission network with a nominal capacity of 300 MW that stretches 1,792 km from the La Vega II and Moyuta substations in Guatemala, through El Salvador and Honduras, to the Dominical substation in Panama.

21 The Bank and IDB Invest currently participate or have previously participated in several infrastructure funds, including BALAM Fund I, 2936/OC-ME; Ashmore Colombia Fund, 2214/OC-CO; and the Central American Mezzanine Fund I, 1760/OC-RG and 2909/OC-RG. They have also participated in projects with public-private mobilization, such as the Reventazón project in Costa Rica (2747/OC-CR and 2806/OC-CR), which had sovereign guaranteed and non-sovereign guaranteed financing, and the Geothermal Exploration and Transmission Improvement Program in Nicaragua (3729/OC-NI).

22 Through technical cooperation project RG-P1569, the Bank has supported the development of rules and regulations for the creation of Infrastructure Funds, advocating for governance structures that make public-private investment viable so that strategic investments can be developed.

through its priority areas of: (i) road infrastructure for regional integration[23] and (ii) sustainability and competitiveness in the energy sector. Both areas play an essential role in supporting the sustainability and competitiveness of the tourism sector, which has been prioritized by the country's national development strategy (Honduras 2020). The program also aligns with the 2017-2020 country strategy with Guatemala (document GN-2899), and with its private sector development priority area in particular, through public investment in infrastructure, including the objectives of: (i) the expansion and modernization of logistics infrastructure, including border crossings, transportation, logistics facilities, and telecommunications; and (ii) the generation of renewable energy and gas by improving the transmission system and investing in electrical integration. The country strategy with Guatemala also includes the PAPTN as a guiding principle in the implementation of the strategy. The integration of climate change elements is a crosscutting theme in all three country strategies. Each of the program's individual operations will state how it aligns with the corresponding country strategy.

1.21 **Strategic alignment.** This program aligns with the Update to the Institutional Strategy (UIS) 2010-2020 (document AB-3008) and the following development challenges: (i) economic integration,[24] in accordance with the principle of national subsidiarity, because the program promotes a coordinated regional effort in infrastructure financing within the context of the PAPTN; (ii) productivity and innovation, because of its innovative financing mechanism that aims to improve the productivity and competitiveness of the countries; and (iii) social inclusion and equality, through the creation of formal employment opportunities and interventions in underdeveloped geographic regions. The program is aligned with the crosscutting areas of: (i) climate change and environmental sustainability by incorporating adaptive features into project design; and (ii) institutional capacity and rule of law through its focus area of improving infrastructure management. It is also consistent with the 2016-2019 Corporate Results Framework (document GN-2727-6) country development results indicators associated with the reduction of emissions with the support of IDB Group financing and installed power generation from renewable energy sources.

1.22 This program is consistent with the Transportation Sector Framework Document (document GN-2740-7); and with the Support to SMEs and Financial Access/Supervision Sector Framework Document (document GN-2768-7), in that it promotes access to productive sector financing and increasing productivity; and with the Integration and Trade Sector Framework Document (document GN-2715-6) and the Energy Sector Framework Document (document GN-2830). It is also consistent with the Sustainable Infrastructure for

[23] Road infrastructure is characterized by low quality road systems with inadequate coverage. Honduras has the lowest road density (0.30 km/km^2) in Central America and the Dominican Republic. Only 24% of the 15,000 kilometer road network is paved. Territorial development in Honduras is not equitable or balanced across departments, which limits access to production, tourism, and forest areas. With regards to logistics infrastructure, Honduras needs to strengthen border crossing services because of their impact on the country's competitiveness and international trade costs. As for digital connectivity, Honduras was ranked 129 of 176 in the 2017 Information and Communication Technology Development Index.

[24] Economic infrastructure limitations are still one of the main factors determining the region's low productivity, which gives rise to social exclusion and adversely affects regional integration.

Competitiveness and Inclusive Growth Strategy (document GN-2710-5), in that it addresses the need for infrastructure design and management that helps improve service quality and contributes to sustainable and inclusive growth. This program is also aligned with the Bank's Operational Policy on Gender Equality in Development (document GN-2531-10), because of its contribution to poverty and inequality reduction through the promotion of employment opportunities to empower women.

1.23 Lastly, the program aligns with the Bank's Institutions for Growth and Social Welfare Strategy (document GN-2587-2) in its objectives for income generation and the countries' macrofiscal management, as well as with the Fiscal Policy and Management Sector Framework Document (document GN-2831-5) in that it addresses fiscal sustainability issues and the potential risks of contingent liabilities in general and PPPs in particular, as applicable.

B. Objectives, components, and cost

1.24 **Objectives.** This program's general objective is to help revitalize strategic productive sectors in the national territories of the Northern Triangle countries[25] through the financing of public investment projects in infrastructure, promoting private investment and the generation of economic opportunities for the population. The specific objectives are: (i) to provide financing for public infrastructure to promote and revitalize strategic productive sectors and private investment in infrastructure; (ii) to foster the creation of jobs and opportunities for the population; and (iii) to modernize and expand sustainable productive infrastructure to accelerate growth and strengthen regional integration.

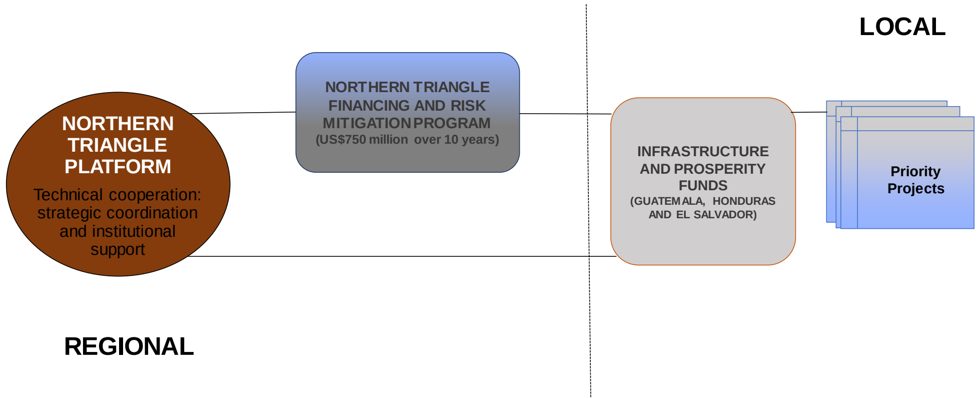
1.25 **This program, which will combine two financial instruments (three CCLIPs and one investment loan,[26]** paragraphs 2.1 y 2.2), **is an essential element in the national and regional financial architecture** that is being designed to increase the viability of local and regional interventions to add value to the infrastructure and strategic sector financing chain.[27]

[25] It will be understood that the strategic investments may be made in the entire national territory of all three Northern Triangle countries.

[26] The investment loan is for the Republic of Honduras.

[27] Based on the efforts of Honduras 2020, the tourism sector has been identified as a strategic sector for job creation in Honduras in the coming years.

Figure 1. Financial architecture supporting the Northern Triangle



1.26 The financial architecture will comprise the following elements**:**

a. **Country level.** To revitalize investment and contribute to closing the infrastructure gap, the IDB Group is helping the countries formulate investment vehicles and/or funds based on each country's legal and regulatory frameworks and international best practices, and it is also providing assistance with project identification and preparation. Work has been done on innovative institutional structures that seek to mobilize public and private resources to finance infrastructure and strategic sector projects. These could include public and private participation in their capital and financing, to be contributed over time based on the demand for capital and financing for the infrastructure and strategic sector projects that are part of their project portfolio. The Bank will continue to support these countries throughout this process, devoting special attention to international best practices for corporate governance and transparency and to the fiscal context thereof.[28]

b. The Bank helped **Honduras** prepare a preliminary draft of the *Ley Especial del Fondo de Inversión, Promoción y Fomento del Turismo* [Tourism Investment, Promotion, and Development Fund Act] (FITUR) for discussions among Honduran authorities. The proposed law recommends the creation of a Fund that would operate as an autonomous entity, with independent legal status, governed by private law, which would receive contributions from various sectors (including the public sector). The purpose of FITUR will be to ensure financing for tourism development and promotion at the national level, and its funds will be allocated to projects in the tourism, transportation, renewable energy, energy efficiency, and water and sanitation sectors, etc.

c. In the case of **Guatemala,** the Bank has focused on the preliminary identification of a portfolio of projects that could be developed and executed through the sector entities or ministries and/or an investment mechanism that could be established under national law.

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[28] The approval of the laws governing the funds is expected to be a condition precedent to the approval by the Board of those individual operations under the CCLIPs that use the funds as executing agencies.

d. Initial efforts in **El Salvador** have focused on identifying a portfolio of priority projects that could be developed and executed by sector ministries/secretariats and/or a Fund established at a later date.

e. **Regional level.** The regional level will consist of two elements: (i) the Northern Triangle platform[29] to help make the funds operational and/or provide institutional strengthening to the executing agencies based on country demand, including: (a) efforts to build their institutional and execution capacity and support in areas such as the selection of fund administrators, the creation of regulations, corporate governance structure, transparency, socioenvironmental safeguards and risk management, and consultation processes, etc.; (b) strategic coordination between the program's relevant stakeholders and PAPTN objectives; and (c) preparation of the first projects that will be implemented under the program and providing training in future project preparation to national teams; and (ii) this program, which will provide additional, complementary support for the mobilization of the public and private resources expected in the creation of the funds.

1.27 **IDB Invest's uncommitted financial facility.** As a joint, coordinated effort, IDB Invest is preparing an Uncommitted Financial Facility for up to US$750 million. The amounts corresponding to the individual operations approved by the IDB and IDB Invest within the framework of the annual country programming or pipeline (IDB Invest) will be deducted from the total amount designated for the CCLIPs, the investment loan for the Republic of Honduras, and the IDB Invest facility, in order to ensure that the total approved amount is US$750 million. In the case of private operations, the no objection from each country of the investment to be made will be required.

1.28 **Program scope.** The program's is structured in response to the preidentified infrastructure financing needs in the Northern Triangle countries; the execution period required when implementing infrastructure operations; the multisector nature of the operations; PAPTN's regional focus; and the Bank and IDB Invest's commitment to using financing mechanisms that are suitable for attracting public and private resources. This structure seeks to attract a significant amount of private investment by encouraging strategic public investment promoting efficient financing for a portfolio of infrastructure and strategic sector projects.

1.29 At the same time, this structure will consolidate the support offered by the IDB Group in terms of infrastructure and strategic sector investments in the Northern Triangle, strengthen the countries' commitment, and facilitate dialogue and regional cooperation. The IDB Group's participation will help align the financed operations with the applicable socioenvironmental regulatory frameworks. The amount allocated to each individual operation under the program will be determined through agreements between the Bank and the corresponding country within the framework of the annual \programming exercise and in coordination with IDB Invest.

1.30 **Resource allocation.** This program provides an innovative mechanism that allows resources to be allocated efficiently between the IDB and IDB Invest, according to

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[29] Regional technical cooperation project RG-T3168 includes institutional strengthening, support for the strategic coordination of funds, and training teams in project preparation.

the needs and demands of the Northern Triangle countries and the individual operations. The total program amount has been determined without establishing fixed sub-limits between: (i) the IDB and IDB Invest; (ii) financial products (loans or guarantees (IDB Invest));[30] (iii) or the countries (Guatemala, Honduras, and El Salvador). This lack of fixed sub-limits lets the program encourage: (i) efficient resource allocation based on country demand and need; and (ii) the use of program resource availability as a means of recognizing individual efforts made by the countries, as applicable, in creating the funds and/or execution mechanisms agreed upon between each country and the Bank, the capacity to mobilize private resources, and progress in project preparation. While the IDB and IDB Invest maintain separate approval processes, the objective is to reach an available amount of up to US$750 million in aggregate between the two institutions. The determination of the amounts available for the financing of each of the individual operations under each CCLIP will be determined in the context of the Bank's programming exercise with each country in coordination with IDB Invest.

1.31 **Additionality.** This program represents approximately 6.5% of the total financing requirements identified for potential project demand (regional infrastructure plan). This program intends to use these resources to mobilize public and private sector financing for infrastructure and strategic sector projects in the Northern Triangle. The funds are expected to mobilize between US$1 billion and US$1.6 billion in the coming years as they become operational and build up capital assets from public and private sources and other International Financial Institutions (IFIs).

C. Evaluation and monitoring of the program and of the specific operations that make it up

1.32 The achievements of the program, comprising the three CCLIPs, will be evaluated by determining the specific contribution[31] of each operation under the CCLIPs, according to the nature of the project, to the following regional impact indicators: (i) the reduction of the infrastructure gap in each country as measured by an increase in their rankings on the logistics index and the general infrastructure quality index; (ii) higher employment levels as measured by an increase of the employment rate in each country; and (iii) increased private investment in infrastructure as measured by private participation in infrastructure in each of the countries. The outcomes will correspond to: (i) resources leveraged for financing productive infrastructure projects; (ii) reduced travel times and a lower cost of operating a vehicle on the roads that have been subject to intervention; (iii) an increase in the annual average volume of regional energy exchanges through SIEPAC; (iv) a greater percentage of the population with access to better sources of drinking water and sanitation systems; and (v) increased private investment in the tourism sector. The report on the contribution of each loan operation to the program's achievements will be specified in the section on Relevance in each individual project completion report (PCR).

[30] Please note that the loans can also be used to mitigate or diversify risk that the private sector is not able to absorb efficiently in current market conditions, especially for long-term financing. In this sense, the program will support risk mitigation.

[31] Specific contribution refers to how the expected outcomes of each intervention align with the program indicators. There is no need to establish responsibility at the program level.

1.33 Each individual operation under the three CCLIPs will be processed and approved under current Bank procedures and according to the legislation of each country. Each individual operation will submit a DEM to establish the ex ante evaluability of the proposed intervention. Each operation's execution will also be monitored through individual progress monitoring reports. Upon the completion of every loan operation under the three CCLIPs, each executing agency will draft a project completion report that will evaluate the intervention's achievements according to the Board-approved results matrix. The achievements of the program, taking into account all three CCLIPs, will be evaluated by establishing the specific contribution (specific contribution refers to how the expected results of each intervention align with program indicators). There is no need to establish responsibility at the program level for each operation under the CCLIP with respect to regional-level impact indicators.

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instruments

2.1 This program will be implemented through three CCLIPs for an aggregate total of up to US$700 million awarded over a period of ten (10) years. CCLIPs are based on good project performance and establish long-term credit lines. The CCLIPs will finance investment loan projects by providing borrowers with timely resources, thereby ensuring program continuity. CCLIPs encourage the Bank to maintain an ongoing presence in strategic sectors where investments have achieved their development goals, placing an emphasis on continuous institutional analysis and expediting the loan preparation process by reducing processing costs for both the Bank and the borrowers. A multisector modality II (MM-II) CCLIP has been adopted given the nature of the program, which involves multiple executing agencies and one liaison institution that will coordinate the entire program in each country. Program costs are itemized below:[32]

Table 2. Program Costs (in US$)

Categories	Financing (US$)	Percentage
Guatemala CCLIP	250,000,000	35.7
El Salvador CCLIP	250,000,000	35.7
Honduras CCLIP*	200,000,000	28.6
Total	**700,000,000**	**100.00**

* Honduras has access to concessional Ordinary Capital resources with biennial allocation.

2.2 The program framework also provides for an investment loan in the amount of US$50 million for the Republic of Honduras to finance eligible FITUR projects (paragraph 2.6(b)).

[32] The amount corresponding to each CCLIP is a country estimate that may vary depending on each country's demand for resources and the operations financed by IDB Invest. The total amount available for the three Northern Triangle countries may not exceed US$700 million. The amounts available for financing each individual operation under each CCLIP will be determined based on the Bank's programming exercise with each country and in coordination with IDB Invest. Should the maximum amount allocated to each CCLIP be increased, an amendment will be submitted to the IDB Board of Executive Directors for approval.

2.3 As mentioned in paragraph 1.26, as part of the financial architecture developed for the Northern Triangle, the Bank has supported, for the countries that have requested it, the development of innovative mechanisms for mobilizing private resources for infrastructure financing. Once established, these financial vehicles could take part in program implementation arrangements as executing agencies if such an arrangement has been provided for in individual CCLIP operations, in accordance with national legislation.

2.4 **Fulfillment of MM-II CCLIP eligibility criteria.** The program's liaison institutions will be the Salvadoran Ministry of Finance, the Guatemalan Ministry of Public Finance, and the Honduran Ministry of Finance. These institutions meet the eligibility requirements for the MM-II CCLIP pursuant to the Proposed Modifications to the Conditional Credit Line for Investment Projects (CCLIP) (document GN-2246-9) and the CCLIP Operational Guidelines (document GN-2246-11) because (i) they have the legal mandate and authority to coordinate and monitor the credit line as the Bank's liaison institutions, since they are acting as the borrower, and as the parties responsible for programming the portfolio with the Bank and other IFIs, and they have demonstrated their capacity to coordinate and monitor such financing operations; and (ii) they have a clear understanding of the multisector objectives defined in paragraphs 2.9, 2.13, and 2.17 for El Salvador, Guatemala, and Honduras, respectively, because these objectives are aligned with the national development plans, the Bank's country strategies with the three Northern Triangle countries, and the PAPTN strategic objectives.

2.5 **Program structure.** This program seeks act as a catalyst for attracting financing resources from multiple sources through three CCLIPs and one investment loan for the Republic of Honduras. This will allow it to support the efficient mobilization of public and private resources for productive investment to contribute to regional economic growth and job creation. While the CCLIPs will support the necessary public investment, the investment loan for Honduras will promote private participation in eligible projects through FITUR. The investment loan for Honduras will be prepared and processed separately from this program. As a joint, coordinated effort, IDB Invest is preparing an Uncommitted Financial Facility for up to US$750 million, which can be used to finance individual projects that the funds have invested in. These individual financing operations will be processed according to IDB Invest's standard approval process.[33]

2.6 **The program's financial instruments.** The program will be implemented through the establishment of:

[33] IDB Invest's Uncommitted Financial Facility and/or investment loans for a total of up to US$750 million will be recorded against the IDB Invest Ordinary Capital framework.

Figure 2. The Program's Financial Instruments

a. Three MM-II CCLIPs,[34] one with each of the Northern triangle countries, with an estimated amount of US$250 million each for El Salvador and Guatemala and an estimated amount of US$200 million for Honduras. The maximum total amount for all three lines will be US$700 million over a ten-year effective period. Each individual operation financed under the CCLIPs will be processed and approved according to current Bank policies and procedures. Should the maximum amount allocated to each CCLIP be increased, the increase will be submitted to the IDB Board of Executive Directors for approval.

b. An investment loan for up to US$50 million for the Republic of Honduras to finance eligible investment projects through FITUR, contributing to the strategic development of the tourism sector, while complementing the development of the infrastructure promoted under the CCLIP. The loan will be prepared and processed separately from the processing of this operation to establish the CCLIPs, in light of the differences between the information and processing requirements for conditional credit lines and investment loans.

2.7 This document proposes the creation of the three CCLIPs (for El Salvador, Guatemala, and Honduras) without including a first individual operation, because the countries are working to develop a multisector project pipeline and they are currently developing and implementing the funds or investment vehicles, within the countries' regulatory frameworks. The establishment of these CCLIPs will: (i) support one or more sectors; (ii) support Northern Triangle countries in accordance with their programming with the Bank; and (iii) forge a stronger link between projects and demand and execution capacity in each country. With regard to the eligibility criteria for the credit lines, the program will ensure that the areas to be financed are aligned with the priorities defined in the corresponding country strategy and program, as well as the fulfillment of the established multisector objectives and the respective liaison institution's proven capacity. Optional link 8 includes a preliminary identification and description of potential projects for each CCLIP.

34 Pursuant to CCLIP Guidelines (document GN-2246-11), CCLIPs provide borrowers with timely resources allowing investment programs to have continuity, and they provide a vehicle for efficient Bank support and continuous presence.

2.8 **El Salvador CCLIP.** This document proposes an MM-II CCLIP to support improvements to logistics and energy infrastructure. The Bank's strategic approach with El Salvador is to support government efforts to strengthen public finance and create conditions for broad-based economic growth. During the 2015-2019 period, the public sector window will prioritize improvements to logistics infrastructure, while the IDB Group's private sector window will promote renewable energy. The IDB's country strategy with El Salvador considers the energy sector to be an area of strategic dialogue due to its importance for the country's competitiveness. Interventions in both sectors should enable the country to improve its competitiveness (by reducing logistics and electricity costs) and support an economic growth that is more inclusive by creating job opportunities that encourage the local population to set down roots and facilitate the integration of returning migrants into the job market. According to optional link 2, El Salvador is the country with the greatest infrastructure gap, with an average infrastructure investment of 1.5% of GDP (the average investment for Latin American and Caribbean countries is 2.7% of GDP). Stimulating strategic investments will strengthen the country's efforts to spark a productive transformation that will energize the economy and international trade. El Salvador's membership in the Northern Triangle Customs Union would create important synergies with the individual operations under this CCLIP in terms of competitiveness and trade facilitation.

2.9 The CCLIP will pursue the following objectives in the logistics infrastructure sector: (i) improved logistics infrastructure and better connectivity between logistics and production hubs; (ii) a better ranking on the logistics performance index; and (iii) enhanced infrastructure assets management and greater resilience to climate change. As for the energy sector, the CCLIP intends to: (i) reinforce the national electricity transmission system; (ii) strengthen the country's integration into SIEPAC; and (iii) boost investment in renewable energy and energy efficiency.

2.10 The Salvadoran Ministry of Finance, as the liaison institution, will coordinate and monitor the program's general operations in all sectors included under the credit line. The Ministry has the authority and experience to coordinate and monitor the program and the sectors included under this credit line. The Ministry has demonstrated that it is fully capable of administering operations with the Bank over the last five years, and it can ensure that individual operations are on track to meet the program's multisector objectives. As the Bank's liaison institution, the Ministry of Finance is entrusted with programming and will coordinate the entire investment program included under the credit line.

2.11 The Salvadoran Ministry of Public Works, Transportation, Housing, and Urban Development (MOPTVDU), the National Energy Board of El Salvador (CNE), and/or a Fund that may be established in the future are expected to act as executing agencies. The Bank has extensive experience in executing projects with MOPTVDU, which has demonstrated its solid institutional capacity for project preparation and execution. The CNE sets national energy policy and leads the execution of investments in the sector as the local counterpart executing energy efficiency projects cofinanced by the Japan International Cooperation Agency. Projects in each of these sectors will contribute to the achievement of the CCLIP's multisector objectives. An institutional analysis of the executing agency will be carried out for each financing operation under the CCLIP.

2.12 **Guatemala CCLIP.** This document proposes an MM-II CCLIP for the logistics infrastructure and energy sectors. These sectors are essential for the promotion of productive sector (private sector) development, which is one of the Bank's strategic priorities with Guatemala for the 2017-2020 period. The current lack of productive infrastructure in Guatemala limits the country's economic integration and the creation of job opportunities for poverty reduction. Public investment in infrastructure has been less than 1% of GDP, and Guatemala needs more and better infrastructure to sustain growth and create job opportunities. Inadequate infrastructure has been identified as one of the main obstacles to business development in Guatemala (Doing Business-Global Competitiveness Report) and has hindered the country's ability to attract foreign direct investment. It is also a significant impediment to greater regional integration and to stimulating trade to diversify export destinations and promote value chain integration. The CCLIP will seek to deliver timely resources to provide continuity to strategic investments in both sectors.

2.13 In the logistics infrastructure sector, the CCLIP will promote the following sector objectives: (i) improve the connectivity and capacity of the primary road network; (ii) energize air transportation by improving the capacity of the infrastructure; and (iii) improve the logistical performance of strategic cargo transportation corridors, including interventions in border crossings, highways, urban transit, ports, airports, and logistics facilities. In the energy sector, the CCLIP will seek to: (i) improve the coverage and capacity of the domestic transmission network and investments in electricity integration; and (ii) support the promotion of renewable energies to diversify the national / regional energy matrix. Both sectors have been identified as priorities for productive sector development in the Bank's current country strategy with Guatemala (document GN-2899).

2.14 The Guatemalan Ministry of Public Finance, as the liaison institution, will coordinate and monitor the credit line. The Ministry will lead the country's efforts to improve public management and transparency with the Bank's support, together with the government agencies involved in this area. It has full capacity to manage the Bank's outstanding portfolio and coordinate the entire investment program included under the proposed credit line.

2.15 The Guatemalan Ministry of Communication, Infrastructure, and Housing (MCIV), the National Electrification Institute of Guatemala (INDE), and the Office of the Superintendent of Tax Administration of Guatemala (SAT), and/or an investment or execution mechanism established pursuant to national legislation are expected to act as executing agencies. These institutions have solid experience and institutional capacity in preparing and executing projects in their sectors. Each individual operation will have a specific executing agency. Projects in each of these sectors will contribute to the achievement of the CCLIP's multisector objectives. An institutional analysis of the executing agency will be carried out for each financing operation under the CCLIP.

2.16 **Honduras CCLIP.** This document proposes an MM-II CCLIP to support the transportation and logistics, energy, and water and sanitation sectors as sectors to promote the development of the Honduran tourism sector and improve its

competitiveness.[35] The Bank's strategy with Honduras seeks to support the government's efforts to reverse productive stagnation and increase inclusive growth, and its priorities are stimulating strategic productive sectors, improving the competitiveness of the energy sector, and narrowing the infrastructure gap in transportation and water and sanitation to achieve effective social and territorial inclusion in the country. A key element of Honduras's national development strategy has been encouraging the tourism sector to develop the Caribbean coast and Bay Islands (Honduras 20/20 - sun and sand), an area that is expected to attract US$3.9 billion in foreign investment over the next decade, create over 255,000 new jobs, and consolidate the tourism sector as the country's fourth largest source of foreign currency, after remittances, export assembly plants, and coffee exports.

2.17 The CCLIP will promote the following objectives in the transportation sector: (i) expanding and modernizing connectivity infrastructure for air tourism; (ii) improving the connectivity of regional highways and their integration with priority logistics corridors; (iii) expanding the coverage of the existing road network, and (iv) improving cargo logistics and trade facilitation. In the water and sanitation sector, the CCLIP seeks to: (i) support the comprehensive management of water resources (potable water, sanitation, purification, drainage, and solid resource management) by improving and providing infrastructure in tourism development zones; and (ii) promote the protection of environmental assets. Meanwhile, the CCLIP's objectives in the energy sector for tourism development zones aim to: (i) improve electricity service efficiency and quality and diversify the generation matrix; (ii) increase access to electricity services; and (iii) promote energy efficiency. Sustainability and competitiveness in the energy sector, road infrastructure for regional integration, and social inclusion are three priority issues in the Bank's current country strategy with Honduras (document GN-2796-1).

2.18 The Honduran Ministry of Finance, as the liaison institution, will coordinate and monitor the credit line, as well as its consistency with the multisector objectives of the CCLIP. The Ministry has full capacity to manage the Bank's outstanding portfolio and coordinate the investment program covered under the proposed credit line. Invest-H[36] is expected to act as the executing agency that will prepare, develop, and execute transportation operations, because its institutional capacity and performance in the sector has been recognized by several actors, including

[35] The tourism sector represented 5.5% of GDP in 2017 (15% of GDP after taking into account indirect and induced effects) and was also one of the main producers of exports, foreign exchange, investment, and jobs. Tourism accounts for 7.23% of total exports (US$715.83 million in absolute terms). Estimates indicate that tourism-related exports will grow an average of 7.2% annually over the next decade. In other words, tourism-related exports are expected to have more than doubled by 2028, reaching US$1,543,300,000. Additionally, the tourism sector was responsible for more than 10% of total investment in Honduras in 2017. Tourism investment is expected to grow 3.3% annually over the next decade to reach US$876.6 million dollars of investment per year in 2028. Furthermore, nearly one of every six jobs in Honduras is currently created by tourism activities (including indirect and induced effects). Data obtained from statistics compiled by the World Tourism Organization (UNWTO), the Central Bank of Honduras, and the World Travel Tourism Council (WTTC).

[36] Invest-H (Honduran Strategic Investment Office)—also known as Millennium Challenge Account Honduras—is a management unit for strategic development projects and programs. The unit is affiliated with the *Coordinación General de Gobierno* [General Government Coordination Committee]. Invest-H currently acts as an executing agency for projects with the IDB and the World Bank.

the Bank. In the energy sector, the National Electric Energy Company (ENEE) has been identified as an executing agency, since it has institutional capacity and prior experience with similar projects financed by the Bank and other multilateral institutions. Likewise, the Public-Private Partnership Promotion Agency (COALIANZA) has experience in developing generation and distribution investments. Once FITUR becomes operational, it can also act as the executing agency of specific operations. Each individual operation will have a designated executing agency. Projects in each of these sectors will contribute to the achievement of the CCLIP's multisector objectives. An institutional analysis of the executing agency will be carried out for each financing operation under the CCLIP.

B. Environmental and social risks

2.19 This project has not been subject to ex ante classification[37] pursuant to Directive B.13 of the Bank's Environment and Safeguards Compliance Policy (Operational Policy OP-703). The Bank will use the CCLIPs to finance investments in public projects or in PPPs for infrastructure projects that will be classified as category "A," "B," or "C" operations (the list of potential projects includes projects for highway infrastructure, ports, airports, transmission and distribution lines, border crossings, and energy production).

2.20 The potential socioenvironmental impacts of the projects will be diverse, and their impact level will depend on the characteristics of each project (sector, location, social context, size, etc.). For the most part, adverse socioenvironmental impacts will be local and short-term, for which effective mitigation measures are readily available. Certain category "A" projects may have more significant negative impacts.

2.21 The potential environmental, social, health, and safety risks and impacts of the various projects to be funded will be identified, assessed, and managed through: (i) the Bank's procedures for the approval of each project under each CCLIP and for program supervision and monitoring. The strategic environmental and social analysis will include an Environmental and Social Management Framework that defines which types of plans will be required for project development based on the potential impacts expected for each project type; and (ii) in the event the execution is done by a fund or other investment and/or execution mechanism, and pursuant to the legislation of each country, according to the procedures defined in the strategic environmental and social analysis. Each project will require an environmental and social impact study prior to Bank approval.

2.22 The potential environmental, social, health, and safety risks associated with the program are identified in the program's Environmental and Social Management Report (ESMR).

C. Fiduciary risks

2.23 The Policies for the Procurement of Goods and Works Financed by the Inter-American Development Bank (document GN-2349-9) and the Policies for the

[37] The potential socioenvironmental impacts of the projects will be diverse, and their impact level will depend on the characteristics of each project (sector, location, size, etc.). Overall, socioenvironmental impacts are expected to be local, short-term, and moderate, for which effective mitigation measures are readily available.

Selection and Contracting of Consultants Financed by the Inter-American Development Bank (document GN-2350-9) will be used for procurement processes. The principles and criteria in the Financial Management Guidelines for IDB-financed Projects (document OP-273-6) will be taken into account for financial management matters for each operation designed under the credit line.

2.24 The executing agencies will be the sector ministries/secretariats, as applicable, of Guatemala, Honduras, and El Salvador; FITUR and/or Invest-H, and the Salvadoran infrastructure vehicle, as applicable. The fiduciary capacity of these executing agencies will be evaluated within the framework of each individual operation in each country. If weaknesses are identified, strengthening and/or risk mitigation measures will be defined.

2.25 Given the Bank's experience in the countries and the nature of this program, the following fiduciary risks can be expected: (i) low technical-fiduciary capacity of staff given the expected complexity of program procurement; and (ii) potential delays in the procurement processes of the operations financed by this program. Both of these risks have been identified a priori as having medium impact. To address them, each individual operation will include an institutional strengthening component that will seek: (i) to strengthen the execution unit in terms of financial and procurement management; and (ii) to hire consultants to strengthen the management of the financial structure of PPP projects.

D. Other program risks

2.26 **Fiscal sustainability.** This project's fiscal sustainability risk is considered medium. Insofar as the program's individual operations are executed as PPPs, the operations may entail fiscal impacts resulting from PPP contracts. These impacts need to be identified and managed at both the project and aggregate levels. Potential fiscal and budgetary implications (both contingencies and firm commitments) will be quantified and recorded. PPP projects should be monitored from the start to ensure their integrity in terms of risk identification and allocation, public comparators, contract preparation, and other elements that are key to evaluating value for money, as well as methodologies for selecting private partners, keeping records, and ensuring transparency. To this end, the Bank will continue supporting the region with fiscal projects including specific PPP components (see the note on Honduras in paragraph 1.3).[38] The recent creation of the PPP unit within the Vice Presidency for Countries (VPC) can also ensure that the Bank becomes involved in PPP operations from early on, should any such operations exist.

2.27 The creation of investment vehicles or mechanisms or infrastructure funds should consider the potential fiscal impact limitations, based on national legislation and in accordance with international best practices.

2.28 **Infrastructure fund approval.** There is a medium risk of delays in the legislative approval of the infrastructure funds. For Honduras, the Tourism Incentives Act was

[38] It is also important to note that Honduras continues to make progress in its PPP operational framework, not only through its reformed PPP Act (2014), but also through its creation of an appropriate institutional framework and fiscal supervision mechanisms. The Bank continues to support Honduras in these efforts. The Fiscal Implications of Public–Private Partnerships in Honduras, IDB-DP-391, Gerardo Reyes Tagle and Mikel Tejada (July 2015).

approved in August 2017. The Bank has assisted Honduras in designing the FITUR Act, which should be legislatively approved in the near future. In the case of Guatemala, any proposal should consider that the law currently does not allow public credit operations to be managed by third parties. In El Salvador and Guatemala, the program is initially expected to be implemented through sector ministries and/or secretariats. The participation of various executing agencies in the execution of this program will allow the Bank to make ongoing headway in individual operations and enable approval and implementation of funds or investment vehicles, as applicable.

2.29 **Project management and governance.** Medium risks have been identified in each country's interagency coordination to prioritize projects, their ability to fast-track preinvestment processes, and/or difficulties in structuring PPP projects. Expected risks also include risks from public decision-making during project selection, in which interventions with short-term impact may be prioritized and/or the benefits programs offer to interest groups may not be taken into account. To mitigate these risks, the team has helped the countries identify priority investments, has facilitated public-private dialogue, and has designed a multicriteria methodological approach to strategically analyze investments in terms of development impact and feasibility. As for the risks associated with PPP project structuring, the team has made arrangements with the VPC's PPP Unit and has coordinated efforts to obtain preinvestment resources.

2.30 **Intraregional coordination.** Medium risks associated with the coordination of different stakeholders (public, private) at the national and intraregional level are expected. To mitigate these risks, the team has made arrangements for regional technical cooperation project RG-T3168, which provides support for institutional strengthening, strategically coordination of funds, and training teams in project preparation. The technical cooperation project will help make headway with preliminary studies for the identified project portfolio to facilitate their evaluation for financing.

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation arrangements

3.1 Demand for each CCLIP's individual operations will be monitored at the country level as part of the programming exercise. Each country's respective Representative will play an important role (with the support of VPC/CID) in ensuring that individual operations remain within the program's approval limits. During the preparation of individual operations led by VPS,[39] the approval process will ensure that the individual operations are consistent with the respective CCLIP guidelines and the program's overall objectives. The progress made under the program will be periodically evaluated at the regional level and as part of the Bank's activities with the PAPTN, under VPC/CID leadership in coordination with the countries and VPS.

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[39] Individual PPP operations will receive support from the VPC/APP unit and the Fiscal and Municipal Management Division of VPS. This latter division will also provide support to individual operations using funds or investment vehicles as executing agencies.

3.2 **CCLIP.** The borrowers will be the Republic of Guatemala, the Republic of El Salvador, and the Republic of Honduras, which will act through their Ministries of Finance as Liaison Institutions. Each of the individual operations that receives financing or risk mitigation under the CCLIPs will be part of country programming led by VPC/CID and will be prepared by the VPS Sector Divisions, in close coordination with the executing agencies of the countries according to the investment area of the individual project and with VPC/CID. The amount allocated to each individual operation under the program will be agreed between the Bank and the corresponding country within the framework of annual programming and in coordination with IDB Invest.

3.3 **Coordination and administration.** The liaison institutions will coordinate and monitor each CCLIP, supporting progress toward their multisector objectives. The liaison institutions' role will be to manage the credit line and monitor the results of each sector loan operation. The executing agencies will be the sector ministries/secretariats of Guatemala, Honduras, and El Salvador, FITUR, and/or Invest-H in the case of Honduras, and the Salvadoran infrastructure vehicle, as applicable. The executing agencies will be responsible for tasks including the following: (i) collaborating with Bank teams on financing operation preparation; and (ii) executing the approved individual operations in accordance with the policies set forth by the financing agreements.[40] The legal mandate provided to the liaison institutions to coordinate and monitor the credit line seeks to promote the achievement of the multisector objectives of each operation managed and executed through a CCLIP under the program.

3.4 **Regional coordination.** The Northern Triangle platform will provide strategic support for the program's regional coordination. This platform will: (i) support the implementation of the Northern Triangle funds or investment vehicles in each country as permitted under national legislation, and their institutional and technical capabilities, including the implementation of their social and environmental safeguard systems; (ii) provide strategic coordination between each country's funds and other stakeholders and between the these entities and PAPTN objectives; and (iii) assist with the preparation, structuring, and execution of projects financed under the program. The Northern Triangle platform will also seek to attract the participation of strategic partners (including donor countries) in order to expand the resources that are available for cofinancing projects that have been prioritized in the program's framework. To coordinate the program interventions by each country, the three countries will form a trinational technical group that will meet every two years to review the progress of project preinvestment and investment processes under the credit line.

[40] The executing agencies will be responsible for tasks including the following: (i) assisting with procurement of works, goods, and services; (ii) processing Bank disbursements; (iii) conducting external audits; (iv) submitting work plans to the Bank (including the financial plan, the procurement plan, the annual work plan, etc.; (v) presenting reports to the Bank, including audit reports, progress reports, evaluation reports, and other program documents; and (vi) assisting with oversight and audits for works and service contracts.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-___/18

El Salvador. ES-O0005. Conditional Credit Line for Investment Projects (CCLIP)
Financing and Risk Mitigation Program for Strategic Investments
in the Northern Triangle's countries
(RG-O1667)

The Board of Executive Directors

RESOLVES:

1. To authorize the President of the Bank, or such representative as he shall designate, to enter into such agreement or agreements as may be necessary with the Republic of El Salvador, as Borrower, to establish the Conditional Credit Line for Investment Projects (CCLIP) - ES-O0005 - for an amount of up to US$250,000,000 chargeable to the resources of the Bank's Ordinary Capital, to cooperate in the execution of the Financing and Risk Mitigation Program for Strategic Investments in the Northern Triangle's countries.

2. To determine that the resources allocated to the above-mentioned Conditional Credit Line (CCLIP) ES-O0005 shall be used to finance individual loan operations in accordance with: (a) the objectives and regulations of the Conditional Credit Line for Investment Projects approved by Resolution DE-58/03, as amended by Resolutions DE-86/16, DE-10/07 and DE-164/07; (b) the provisions set forth in the document proposal for the Conditional Credit Line for Investment Projects (CCLIP) – ES-O0005; and (c) the terms and conditions included in the Loan Proposal for the corresponding individual operation.

(Adopted on ___ ____________ 2018)

LEG/SGO/CID/EZSHARE-456533210-49252
ES-O0005

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-___/18

Guatemala. GU-O004. Conditional Credit Line for Investment Projects (CCLIP)
Financing and Risk Mitigation Program for Strategic Investments
in the Northern Triangle's countries
(RG-O1667)

The Board of Executive Directors

RESOLVES:

1. To authorize the President of the Bank, or such representative as he shall designate, to enter into such agreement or agreements as may be necessary with the Republic of Guatemala, as Borrower, to establish the Conditional Credit Line for Investment Projects (CCLIP) - GU-O0004 - for an amount of up to US$250,000,000 chargeable to the resources of the Bank's Ordinary Capital, to cooperate in the execution of the Financing and Risk Mitigation Program for Strategic Investments in the Northern Triangle's countries.

2. To determine that the resources allocated to the above-mentioned Conditional Credit Line (CCLIP) GU-O0004 shall be used to finance individual loan operations in accordance with: (a) the objectives and regulations of the Conditional Credit Line for Investment Projects approved by Resolution DE-58/03, as amended by Resolutions DE-86/16, DE-10/07 and DE-164/07; (b) the provisions set forth in the document proposal for the Conditional Credit Line for Investment Projects (CCLIP) – GU-O0004; and (c) the terms and conditions included in the Loan Proposal for the corresponding individual operation.

(Adopted on ___ ____________ 2018)

LEG/SGO/CID/EZSHARE-456533210-49275
GU-O0004

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-___/18

Honduras. HO-O004. Conditional Credit Line for Investment Projects (CCLIP)
Financing and Risk Mitigation Program for Strategic Investments
in the Northern Triangle's countries
(RG-O1667)

The Board of Executive Directors

RESOLVES:

1. To authorize the President of the Bank, or such representative as he shall designate, to enter into such agreement or agreements as may be necessary with the Republic of Honduras, as Borrower, to establish the Conditional Credit Line for Investment Projects (CCLIP) - HO-O0004 - for an amount of up to US$200,000,000 chargeable to the resources of the Bank's Ordinary Capital, to cooperate in the execution of the Financing and Risk Mitigation Program for Strategic Investments in the Northern Triangle's countries.

2. To determine that the resources allocated to the above-mentioned Conditional Credit Line (CCLIP) HO-O0004 shall be used to finance individual loan operations in accordance with: (a) the objectives and regulations of the Conditional Credit Line for Investment Projects approved by Resolution DE-58/03, as amended by Resolutions DE-86/16, DE-10/07 and DE-164/07; (b) the provisions set forth in the document proposal for the Conditional Credit Line for Investment Projects (CCLIP) – HO-O0004; and (c) the terms and conditions included in the Loan Proposal for the corresponding individual operation.

(Adopted on ___ ____________ 2018)

LEG/SGO/CID/EZSHARE-456533210-49276
HO-O0004