

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

URUGUAY

PROGRAM TO ENHANCE THE COMPETITIVENESS OF STRATEGIC TOURIST DESTINATIONS

(UR-L1018)

LOAN PROPOSAL

This document was prepared by the project team consisting of Adela Moreda (RE1/EN1), Project Team Leader; Héctor Malarín (RE1/EN1); Mario Gallego (RE1/EN1); Javier Jiménez Mosquera (LEG/OPR); Luis Macagno (COF/CUR); and Ximena Álvarez (RE1/EN1), who helped to produce this document.

CONTENTS

PROJECT SUMMARY

| | | |
|------|--|----|
| I. | FRAME OF REFERENCE | 1 |
| A. | The tourism sector in Uruguay | 1 |
| 1. | Economic significance and characteristics of the sector | 1 |
| 2. | Institutional and policy framework..... | 2 |
| B. | Country strategy in the sector | 4 |
| C. | The Bank's country strategy | 6 |
| D. | Lessons learned from Bank action in the sector..... | 7 |
| E. | Coordination with other international agencies..... | 8 |
| F. | Program design | 8 |
| II. | THE PROGRAM | 10 |
| A. | Objective | 10 |
| B. | Components | 11 |
| 1. | Structuring and promotion of tourist destinations | 11 |
| 2. | Improving the institutional framework for tourism..... | 12 |
| C. | Cost and financing | 13 |
| III. | PROGRAM EXECUTION | 13 |
| A. | Borrower and executing agency | 13 |
| B. | Program execution and management | 13 |
| 1. | The Ministry of Tourism and Sports (MINTURD)..... | 14 |
| 2. | Municipal councils..... | 14 |
| 3. | Administrative works commission in Cabo Polonio..... | 15 |
| C. | Preparation and oversight of works | 15 |
| D. | Operation and maintenance | 16 |
| E. | Procurement of goods and works and contracting of consultants..... | 17 |
| F. | Revolving fund | 18 |
| G. | Execution period and disbursement schedule | 18 |
| H. | Monitoring and evaluation..... | 18 |
| I. | Audit..... | 19 |
| IV. | VIABILITY AND RISKS | 19 |
| A. | Institutional viability | 19 |
| B. | Socioeconomic viability | 20 |
| C. | Financial viability | 23 |
| D. | Socioenvironmental sustainability..... | 23 |
| E. | Benefits and beneficiaries..... | 25 |
| F. | Risks | 25 |

ANNEXES

Annex I Logical framework

Proposed resolution

| Electronic Links and References | |
|--|---|
| Basic socioeconomic data | http://www.iadb.org/RES/index.cfm?fuseaction=externallinks.countrydata |
| Status of loans in execution and loans approved | http://ops/approvals/pdfs/URen.pdf |
| Tentative lending program | http://opsgsl/ABSPRJ/tentativelending.ASP?S=UR&L=EN |
| Information available in the RE1/EN1 technical files | http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=845341 |
| Procurement plan | http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=850881 |

ABBREVIATIONS

| | |
|---------|---|
| DINAMA | National Department of the Environment |
| GDP | Gross domestic product |
| ICAS | Institutional Capacity Assessment System |
| IRR | Internal rate of return |
| MINTURD | Ministry of Tourism and Sports |
| NPV | Net present value |
| UNESCO | United Nations Educational, Scientific, and Cultural Organization |

PROJECT SUMMARY

URUGUAY

PROGRAM TO ENHANCE THE COMPETITIVENESS OF STRATEGIC TOURIST DESTINATIONS (UR-L1018)

| Financial Terms and Conditions ¹ | | | | |
|--|----------------------|----------|---------------------------------|---|
| Borrower: Eastern Republic of Uruguay Executing agency: Ministry of Tourism and Sports (MINTURD), through its National Secretariat | | | Amortization period: | 25 years |
| | | | Grace period: | 4 years |
| | | | Disbursement period: | 4 years |
| Source | Amount (US\$) | % | Interest rate: | Adjustable |
| IDB (Ordinary Capital) | 5,000,000 | | Inspection and supervision fee: | 0% |
| Local | 1,250,000 | | Credit fee: | 0.25% |
| Total | 6,250,000 | | Currency: | US dollars from the Single Currency Facility |
| Project at a glance | | | | |
| Project objective: To create a proactive framework for tourism development, in which new tourism products and services are designed to capture new segments of demand, with an emphasis on Colonia, Rocha, and the hot springs region | | | | |
| Special contractual conditions: a. Prior to the first call for proposals for works under the jurisdiction of a municipal council, a participation agreement must be signed between the executing agency and the respective municipal council, detailing each party's responsibilities in executing the activities (see paragraph 3.6). b. Prior to the first call for proposals for the activities to be undertaken in Cabo Polonio, the executing agency will present the legal mechanism creating the administrative commission responsible for managing, operating, and maintaining the planned eco-center must be submitted (see paragraph 3.7). c. A midterm evaluation report will be delivered within 90 days after the date on which 50% of the loan proceeds have been committed, and a final evaluation report within 90 days after the date on which 90% of the loan proceeds have been disbursed (see paragraph 3.19). | | | | |
| Exceptions to Bank policies: None. | | | | |
| Project consistent with country strategy: Yes [X] No [] Project qualifies as: SEQ [] PTI [] Sector [] Geographic [] Headcount [] Verified by CESI on: 27 October 2006 Procurement: Program procurements will be conducted in accordance with applicable Bank policies (documents GN-2349-7 and GN-2350-7). See paragraphs 3.13 and 3.14. | | | | |

¹ The interest rate, credit fee, and inspection and supervision fee mentioned in this document are established pursuant to document FN-568-3 Rev. and may be changed by the Board of Executive Directors, taking into account the available background information, as well as the respective Finance Department recommendations. In no case will the credit fee exceed 0.75%, or the inspection and supervision fee exceed 1% of the loan amount.*

* With regard to the inspection and supervision fee, in no case will the charge exceed, in a given six-month period, the amount that would result from applying 1% to the loan amount divided by the number of six-month periods included in the original disbursement period.

I. FRAME OF REFERENCE

A. The tourism sector in Uruguay

1. Economic significance and characteristics of the sector

- 1.1 Tourism is an important economic sector in Uruguay. According to Uruguay's Central Bank, the sector contributed nearly 7% of the country's overall gross domestic product (GDP) and 10% of its GDP in services in 2000 (the most recent year for which data is available on domestic and international tourism). Even more important is its contribution to foreign exchange in the country: in 2005, international tourism generated US\$594 million, equivalent to 17.4% of the total exports for that year.
- 1.2 Tourism in Uruguay has two significant features that have determined its position on the international market. First, the international tourism demand comes primarily from Argentina, which causes its development to be intimately linked with that country's political and economic processes. Thus, Argentina's economic bonanza between 1990 and 1997 contributed to the growth of the tourism sector: in 1997 there were a total of 2.4 million arrivals generating a record US\$700 million. During this period, Argentine visitors represented 70 to 80% of international arrivals to Uruguay. Nevertheless, this dependence on a single market caused the contraction of the sector between 1998 and 2002 as a result of the Argentine economic crisis. In 2002, the flow of foreign exchange from tourism shrank to US\$315 million. Today, the solid prospects of the Argentine economy and a gradual diversification in the origin of visitors are allowing the sector to recover. Thus, in 2005 Uruguay had 1.9 million international arrivals, of which Argentines represented 58% of the total, while visitors from countries in the region (Brazil, Chile, and Paraguay), countries outside the region (primarily from North America and Europe), and Uruguayans residing abroad each represented the same proportion (about 14%).
- 1.3 Secondly, the tourism offering is geographically concentrated, by type of product and season. Today, two destinations are the focus of nearly two thirds of the international demand: Montevideo and Punta del Este. A third major destination is the hot springs region, which is estimated to have drawn 11% of all tourist visits in 2005. Forty-seven percent of Uruguayan tourism is drawn by "sun and beach" tourism, despite the presence of other types of tourism, including business and conventions (with a 15% share), hot springs and health (9%), culture (3%), and cruises. Cruises have undergone strong expansion in recent years, quadrupling the number of visitors between 1998 and 2005. The predominance of "sun and beach" tourism has a major impact on summer seasonality: most tourists come during the first quarter of the year (approximately 41% of all arrivals in 2005).
- 1.4 Other characteristics of the sector include:
 - d. In 2005, the average stay by international visitors was 6.9 days, showing a downward trend since 2002. Average spending per tourist coming to Uruguay was US\$282 per stay, or about US\$41 per day. This variable is also showing a

downward trend, due to the decrease in the average stay. According to their origin, North Americans, Brazilians, and Europeans spend the most, while the average daily spending for domestic tourists represents about half of what international tourists spend.

- e. Hotel lodging is chosen by only 25% of international visitors: the strong presence of Uruguayans residing abroad and the bonds of kinship and friendship between Argentines and Uruguayans make staying with family and friends one of the predominant forms of lodging. With sun and beach tourism, second homes and rental units are also quite common.¹ For these reasons, in recent years, food service (restaurants and supermarkets) has been the sector earning the most revenue from tourism (about 40% of average spending).
- f. In Uruguay, mid- to low-end small and medium-sized hotels dominate the market. These are family businesses with rudimentary management structures that leave them vulnerable to contractions in demand. The situation of these hotels has been aggravated since the entry of large hotel chains into the country in the 1990s, as well as franchises in the more dynamic tourist areas.
- g. Private sector participation is generally characterized by low entrepreneurial capacity and a high level of dispersion in small businesses accustomed to operating in a market with high demand, marketing individual services using a predominantly direct sales approach, without actively looking for new business opportunities. There are few entrepreneurial networks in the sector, particularly those oriented toward integrating tourism products. This limits opportunities to leverage economies of scale for promotion and targeting of relevant products and services to serve the demand of international markets.

2. Institutional and policy framework

- 1.5 The institutional framework is governed by the Law Ensuring the Operation of State Services (Law 15851 of 1986), which established the tourism management duties of the Ministry of Tourism and Sports (MINTURD): (i) to establish and guide national tourism policy; (ii) to plan and promote the improvement of tourism infrastructure in general, and the performance of complementary public works; (iii) to approve tourism development projects and programs; (iv) to enter into domestic and international agreements for tourism development; (v) to determine priority areas for tourism development from among those determined by law to be of national interest; (vi) to establish tourist information centers abroad; (vii) to grant concessions on State-owned property for purposes of tourist use; (viii) to establish registries of tourism service providers; and (ix) to undertake promotional activities and facilitate the holding in the country of international events of interest to tourists.

¹ There are a wide range of houses and apartments offered as rentals to the tourist market. This type of lodging is quite notable in the beach tourism centers, where it is becoming the primary form of lodging. In Punta del Este, the real estate sector controls 150,000 beds compared to the 12,000 in the hotel sector (Punta del Este Realtors Association).

- 1.6 Under the office of the Minister is the General Secretariat, responsible for the duties associated with the sector. The Secretariat oversees the Finance-Accounting and Administrative Divisions, as well as three technical divisions: (i) Strategic Planning, responsible for research and statistics, as well as the creation, development, and promotion of tourism products; (ii) Tourist Services, responsible for the registry of enterprises in the sector and hotel ratings; and (iii) Operations Development, responsible for promotional activities.
- 1.7 Nearly half of MINTURD's budget (averaging US\$5.5 million per year over the last three years) is devoted to financing promotional and marketing activities, primarily in the domestic market. This means that spending devoted to drawing international tourism is reduced to US\$0.8 per visitor, a very low ratio compared to other countries. The remaining 50% is used primarily to cover the agency's administrative and operating expenses (45%), leaving a small fraction for investment (5%). MINTURD's funding comes from three sources: the general federal budget, the river tax, and the Tourism Development Fund (a percentage of casino revenues). There is no contribution from air transport taxes.
- 1.8 At the municipal level, the municipal councils have tourism management agencies whose duty is to promote the activity and coordinate actions with the federal public and private sectors. They normally also address other activities such as recreation, parks, and public events. Despite the fact that for many of these local governments, tourism is considered a strategic sector, their management capacity is often limited by the lack of up-to-date tourism development plans and human resources with adequate training for the effective implementation of these plans.²
- 1.9 The Country has a National Tourism Council, a consultative body made up of representatives of MINTURD, municipal tourism agencies, civil society, and the private sector, including the Uruguayan Chamber of Tourism, which seeks to contribute to establishing medium- and long-term policies for the development of the sector. This council's duties are complemented by the actions of partially State-owned tourism corporations, public-private coordination organizations in some municipalities popular among tourists (Montevideo, Rocha, Colonia, Salto, Paysandú), which seek to establish themselves as relevant promotion agencies for tourist destinations in their respective areas.
- 1.10 Since 1991, tourism has been one sector that has benefited from various investment promotion systems, whereby tax benefits have been granted, including exemptions and other tax breaks. These benefits were particularly important in promoting an annual average flow of US\$138 million in private investment that helped support the sector's growth from 1991 to 1997. Universidad de la República estimated that investments in the sector represented 18% of all private investment made in the country in 1996. After the contraction of Argentine demand, average annual

² With Bank support through the Municipal Development and Management Program (1489/OC-UR), the central government seeks to improve management effectiveness in the areas of taxation, finance, purchasing and assets, human resources, territorial organization, citizen service, and social participation.

investment shrank to US\$48.4 million between 1998 and 2003. A new drive for tourism investment took place in 2005 with the extension of tax benefits (Decree 175/30). It is also expected that the forecast volume of foreign private investment, estimated at 20% of the GDP for 2007 by the Ministry of the Economy and Finance, will favor growth in the sector.

- 1.11 Nevertheless, the investment promotion system has not been sufficient to overcome the geographic, seasonal, and thematic concentration of the tourism offering, basically due to the lack of an active approach to looking for new opportunities. On the contrary, most of the investment made under this system went toward hotel equipment in 4- and 5-star establishments in Punta del Este and Montevideo (55% of the investment).

B. Country strategy in the sector

- 1.12 At the end of 1999, the first national tourism policy was drafted. Although the government that took office in 2000 adopted this document as a frame of reference, it actually gave priority to actions focused on short-term results to the detriment of strategic management, in the context of the emergency caused by the contraction in demand. Thus, this focus did not allow it to address the primary factors limiting sustainable growth in the sector: excessive reliance on the Argentine market, as well as the geographic, seasonal, and thematic concentration of Uruguayan tourism development.

- 1.13 Today, to strengthen the sector's competitiveness and reduce its vulnerability to market fluctuations, MINTURD's management faces the challenge of transitioning from a spontaneous development strategy (in response to demand) to one of planned development (proactive). MINTURD has begun developing a tourism plan for Uruguay in dialogue with the Bank, under which strategic tourist areas with similar and complementary tourist attractions are selected, and priority actions identified with a product/market focus. In this way, MINTURD hopes that these actions create synergies that allow the diversification of tourism demand, extend the economic and social benefits of tourism activities to new geographic areas, break the existing seasonal cycle, maximize efficiency in the use of public resources, and contribute to the country's international positioning. In short, it represents an attempt to change the country's tourism model (see table).

| Traditional model | New model |
|---------------------------------------|---------------------|
| Spontaneous development | Planned development |
| Real estate and food service business | Tourism business |
| Concentration | Diversification |
| Spontaneous demand | Induced demand |

- 1.14 As part of the activities aimed at implementing this new model, in collaboration with the Bank, MINTURD drafted a tourism map of the country. This map provides a territorial view of the tourism system for purposes of consistently applying the policies and maximizing the long-term benefits of investment in tourism. In this sense, the map defines the country's "tourism" geography, identifying areas with

homogenous tourist centers and attractions, and those that complement each other in terms of both geography and the market. This map was validated in three information and awareness workshops held during program preparation. The country's six main tourism areas identified on the map are:

- a. *Punta del Este region*: Made up of the city of Punta del Este and the nearby coastal areas in the Department of Maldonado, it is currently the country's most important tourist destination. It is oriented toward medium and high market segments, and has a robust international brand. Although it shows significant growth, it has yet to overcome its significant seasonality, marked by very strong dependence on "sun and beach" and second home tourism, associated primarily with the Argentine market.
- b. *Montevideo and its eastern metropolitan area*: including the Old Town area (*Ciudad Vieja*) and the capital's downtown, as well as *Ciudad de la Costa* and the *Costa de Oro*. The destination features sites of historical and architectural value, though many are currently poorly maintained and developed for tourism. It is not a tourist destination with a "brand" as robust or clearly defined as Punta del Este, but it does receive flows of tourists year round, given its nature as a business center and national capital.
- c. *Colonia*: This area covers Colonia del Sacramento and the coast of the Colonia department, including the town of Carmelo and other smaller centers. The historic neighborhood of Colonia de Sacramento was declared a World Heritage site in 1995, as it represents an example of fusion of the Portuguese and Spanish colonial styles. This area has the potential to draw tourists from regional markets and beyond, as it is emblematic of the country's cultural tourism. It also has high potential for city breaks and nautical tourism. It may represent a port of entry into the country for tourists, since it is one of the primary gates of access by river.
- d. *Rocha and mountain areas*: Made up of an expansive area of lakes and Atlantic coastline, it also includes the mountain areas. It currently operates as a domestic tourism destination aimed at mid-level segments, and draws regional tourism, to a lesser extent, oriented toward higher end markets. In addition to its many beaches, the destination has a resource and an image associated with "nature," since it includes Bañados del Este, an area declared a Biosphere Reserve by the United Nations Educational, Scientific, and Cultural Organization (UNESCO) in 1976 and included in the Ramsar List of Wetlands of International Importance since 1984. It is a highly seasonal tourist destination, given its still major dependence on the sun and beach market.
- e. *Hot springs region (Salto – Paysandú Corridor)*. Located on the banks of the Uruguay River, this area is currently focused on leveraging the thermal spring resources in competition with neighboring areas offering similar attractions in

the Entre Ríos province of Argentina. While its primary market is Argentina, domestic tourism is gradually gaining importance.

- f. *Rural Uruguay*. This area covers the zones farthest away from the capital and the coast. Its tourist attractions are associated with traditional rural life, some unique natural resources, and its small towns and cities. It includes multiple still minor destinations, aimed mainly at domestic tourism.
- 1.15 MINTURD has decided to prioritize those destinations that have the highest potential to produce a sustained increase in tourism, as well as to achieve a greater diversification in tourist demand, in order to reduce the sector's vulnerability. In this regard, its strategy includes two complementary lines of action: (i) to consolidate the Punta del Este region and Montevideo, with its metropolitan area, currently the country's top two international tourist destinations; and (ii) to begin structuring and promoting alternative tourist destinations, through illustrative and leveraged public investments to stimulate private investment: the priorities are Colonia, Rocha, and the hot springs region, to take advantage of their potential. These three destinations offer the following characteristics to achieve the expected results from this second strategic action: they represent an attraction capable of establishing modes of tourism beyond the sun and beach and generating new guidelines for tourism management in the country; a high level of attraction to draw new segments of demand, particularly in international markets; accessibility and competitiveness with other destinations; and the will of the local and national participants to focus efforts and investments in these areas.

C. The Bank's country strategy

- 1.16 The Bank's country strategy with Uruguay 2005-2009 (document GN-2398-2) proposes three target areas: (i) improving public management and sustaining fiscal soundness; (ii) strengthening competitiveness and Uruguay's international positioning to sustain growth; and (iii) poverty reduction and social inclusion as a pillar of sustainable growth. The proposed operation supports the line of action related to competitiveness and international positioning by prioritizing actions aimed at improving the business climate in order to stimulate investment in the tourism sector, making microeconomic interventions to increase productivity by promoting clusters of activities in a dynamic sector of the economy, diversifying tourism products and markets, and developing support infrastructures.
- 1.17 The program is also consistent with the Bank's competitiveness strategy in Uruguay. This strategy aims to enhance the quality of the economic and institutional environment for the sustainable development of private activity in the country, through actions in three relevant areas: (i) business climate; (ii) institutional framework of support for the productive sector; and (iii) business promotion. The program is framed in the business climate area with illustrative investment activities aimed at stimulating private investment in strategic tourist areas. Furthermore, through actions aimed at modernizing the organization and management of national and local tourism administration in the public sector,

within the framework of the new planned tourism development model adopted by the government, the program contributes to institutional strengthening aimed at supporting the productive sector.

- 1.18 The following operations that support the objective of the Bank's competitiveness strategy in Uruguay complement the actions of this operation: (i) *Program for Cluster and Production Chain Competitiveness* (1763/OC-UR), approved in July 2006, whose activities aim to overcome the low entrepreneurial capacity and the high dispersion of enterprises in the tourism sector, among others; and (ii) *Programmatic Competitiveness Loan* (UR-L1007), currently in preparation. Both operations have mechanisms that will allow close coordination during program execution. In the case of 1763/OC-UR, MINTURD is participating on a public execution committee responsible for monitoring activities; for UR-L1007, there are plans to create an Interministerial Commission for Foreign Trade Affairs that will include MINTURD, among other entities. In addition to these operations, *Development of the Tourism Cluster in Salto* (UR-M1009), approved in November 2005, uses Multilateral Investment Fund (MIF) resources to support the implementation of a coordination strategy among private enterprises and public agencies in Salto.

D. Lessons learned from Bank action in the sector

- 1.19 The Bank has learned lessons from its participation in tourism programs in other countries in the region; these lessons are addressed in the proposed program:
- a. *Careful planning of investments is necessary to achieve strategic objectives.* Application of this lesson requires that tourism investments be based on methodologies that prioritize actions in geographic areas or pilot destinations, selected according to strategic objectives. In this regard, the tourism map developed by MINTURD allows spatial planning of the program's actions in destinations selected based on strategic criteria for the diversification and expansion of tourism development in Uruguay.
 - b. *Tourism projects require the joint participation of local governments, private interests, and civil society in their planning.* An open process of participation contributes to a better penetration of the benefits of tourism into the local population and enhances the environmental sustainability of the investments. Under the proposed program, the tourism map and the investments themselves were subjected to validation and consultation processes in working meetings held during the operation's preparation phase.
 - c. *Tourism projects must balance infrastructure investments with local institutional strengthening to achieve better tourism management.* This balance is necessary to ensure an orderly use of the territory, to reduce environmental or aesthetic damages, and to allow the sustainability of the areas addressed as tourist destinations over the long term. In this regard, the program combines actions aimed at encouraging improvements in the public sector's institutional framework, both centrally and locally, by changing the

reactive development model to one that is more proactive and planned. Local authorities will also participate in the review and approval of the technical bidding documents for works planned under the program, and will play a role both during and after project execution, particularly relating to the sustainability of the investments.

- d. *Destination tourism planning should address communication through interpretation techniques as a key factor in the sustainability of investments.* All destinations with tourism potential have their own history and significance. Tourism planning should capture, highlight and communicate the essence of the destination to visitors through tourism interpretation.³ Destinations of many different kinds are increasingly using interpretation as a way of meeting their visitors' emotional needs (curiosity, attention, interest) and ensuring their satisfaction by changing their behavior at the destination and educating them on environmental and cultural topics. The program has built this lesson learned into the program by adding two interpretive centers at strategic destinations for the country.

E. Coordination with other international agencies

- 1.20 The program is strengthening and complementing efforts undertaken by the government with other international agencies (such as the European Union, the World Tourism Organization, the United Nations Development Program, the Andean Development Corporation, or the Agencia Española de Cooperación Internacional), to improve the competitiveness of Uruguayan tourism. One example is the Punta del Este Tourism Cluster, financed by the European Union under the Program Supporting Competitiveness and Export Promotion for Small and Medium-sized Enterprises. The Bank's program addresses areas complementary to those covered by these other institutions, seeking synergies within a strategic framework of tourism planning for the entire country.

F. Program design

- 1.21 This program has grown out of sector dialogue with the country, from which emerged a new strategic vision for making Uruguay's tourism sector more competitive and less vulnerable to the external economic environment. The program seeks to drive a growing, sustainable trend in generating foreign exchange from tourism through diversification of tourism demand and the motivating factors for travel, thus reducing the sector's vulnerability to the market's seasonal conditions. Its design considers the lessons learned from similar operations in the sector, by moving from a spontaneous development scenario to planned development with a medium- and long-term strategic vision.

³ Unlike tourism information, tourism interpretation is a **communication** activity aimed at opening visitors' eyes to the meaning and relationships between natural and cultural resources. It utilizes artifacts, technologies, people, landscapes, and sites as points of departure to guide and orient visitors as they discover the destination.

- 1.22 The program includes illustrative investment activities aimed at stimulating private investment in three strategic destinations on Uruguay's tourist map, selected for their potential to diversify the tourism offering: Colonia, Rocha, and the hot springs region. To complement the investment activities, the program supports the strengthening of the nation's public tourism management, by strengthening MINTURD's capacity to fulfill its management, regulatory, and evaluation duties efficiently and effectively within the framework of a planned tourism development model. Furthermore, considering the major role of local governments in tourism management, the program includes actions to strengthen the planning and management capacity of the municipal agencies under whose jurisdiction the works will be executed. It is important to recognize the Bank's role as a catalyst in raising municipal awareness of the importance of thinking about tourism in national terms, so that different tourism destinations are cohesive and complement one another and synergies can be maximized.
- 1.23 The program design process included four steps in the preparation phase. For the first step, with the Bank's support, the government defined the works to be included in the program in the three selected tourist areas: Colonia (US\$1.3 million), Rocha (US\$1.1 million), and the hot springs region (US\$1.2 million). A project data sheet was prepared for each of the works, including their objectives, rationales, expected results, costs, and execution schedules.
- 1.24 The interpretive center in Colonia and the eco-center in Cabo Polonio (Department of Rocha), represent nearly 60% of the total cost of these works. The two centers are the first of their kind in Uruguay and will be important for jump-starting and diversifying tourism there, since through their graphical, educational, and interpretive content, they will represent: (i) a restoration of the cultural and natural resources of Colonia and Rocha, expanding the breadth and depth of their existing tourism potential; (ii) a useful tool for drawing visitors to other parts of the same destinations, and even the country; and (iii) for the private sector, an excellent showcase for its offerings, and a focal point for organizing the creation of new products.⁴ In short, these centers will contribute to creating synergies between the institutional tourism planning and development efforts and the private sector, and will facilitate the linkage among various entrepreneurial initiatives involving novel thematic tours of the destinations.
- 1.25 As a second step, the government defined technical assistance and training activities to be included in the program to strengthen public tourism management in the country on both the national and local levels, in order to achieve balance with the investments in infrastructure and ensure proper management to maximize their benefits. Nationally, these activities will build MINTURD's capacity in terms of

⁴ For example, if the Cabo Polonio eco-center includes a tour of the history of shipwrecks along the Uruguayan coast, specific entrepreneurial initiatives may be organized around this tour, to provide it with content and draw tourist spending. These initiatives may range from boat trips with stops at shipwrecks, to guide enterprises, arts and crafts, or sales of materials published or produced on the theme of shipwrecks.

- coordination, strategic planning and innovation, promotion, regulation, and evaluation of tourism development. Locally, the program includes tourism development capacity-building actions for municipal agencies.
- 1.26 As a third step, MINTURD held three information and awareness workshops as part of the program's consultation process: one in the city of Salto (11 September 2006), one in Colonia (14 September 2006), and one in Montevideo (15 September 2006). Among other things, these workshops validated the proposed operation's components and the investments in each of the selected destinations. Representatives of the National Department of the Environment (DINAMA), the municipal public administration of each identified destination, the local private sector, and civil society participated in these workshops.
- 1.27 As a fourth step, MINTURD and the Bank jointly analyzed the economic and environmental feasibility of the program's two primary works: the interpretive center in Colonia and the eco-center and visitor welcome facilities in Cabo Polonio (Rocha). MINTURD also prepared instructions to guide the preparation and oversight of works execution, including methodologies for the feasibility studies and management plans. These instructions will be used as a reference during program execution. These efforts, together with the analysis of MINTURD's institutional capacity, were considered in determining the program's scope.
- 1.28 The program preparation process analyzed institutional considerations relevant to the execution of the operation, such as the degree of interinstitutional coordination between MINTURD and the participating municipal councils. The results of this analysis were used to define the roles and responsibilities of the participating entities within the framework of program execution.
- 1.29 The program represents an initial effort at strengthening one of the country's two strategic lines in the sector in order to achieve the objective of diversifying demand, and it should provide the lessons learned necessary to support future actions aimed at improving the sector's competitiveness. The resources allocated to the program are considered sufficient for the initial stage, since they are guided by a very specific product/market plan and are geographically targeted in areas with high tourism potential. These investments are also coordinated within a nationwide vision, in which the government is working to consolidate the destinations in the regions of Punta del Este and Montevideo with the support of other international agencies.

II. THE PROGRAM

A. Objective

- 2.1 The goal of the program is to create a growing, sustainable trend in the generation of foreign exchange through tourism. The purpose is to create a proactive framework for tourism development, in which new tourism products and services are designed to capture new segments of demand in Colonia, Rocha, and the hot

springs region. The program's impacts, as well as its expected results and outcomes, are presented in the Logical Framework (Annex I).

- 2.2 The program's specific objectives are: (i) to promote destinations and products capable of diversifying demand; and (ii) to strengthen institutional tourism management. Both specific objectives will be analyzed through the execution of two components, whose actions are described below. Their specific outcomes are presented in the logical framework (Annex I).

B. Components

1. Structuring and promotion of tourist destinations (US\$4.3 million)

- 2.3 This component will include feasibility and environmental studies, final designs, and investments in works and equipment to properly leverage the potential of the three priority tourist areas:
- a. *Colonia area (US\$1.3 million)*. The program's investments will focus on Colonia del Sacramento, the capital of the Department of Colonia, located just a few kilometers southeast of the confluence of the Uruguay River and the River Plate. The component includes the implementation of an interpretive center, through the recovery and restoration of an old railroad machine shop, aimed at providing greater depth and richness for the visit to the Colonia World Heritage Site, and encouraging the visitor to visit other destinations in Uruguay. The investment in the interpretive center will be accompanied by investments in interpretive signage for thematic tours in Colonia's historic center. Technical assistance will be provided aimed at determining recovery and new use strategies for El Real de San Carlos, an area on the outskirts of Colonia del Sacramento, where a currently abandoned tourist complex was developed in the early 20th century.
 - b. *Rocha and mountain areas (US\$1.1 million)*. This area has attractions relevant for the development of nature tourism products. This component focuses several investments in Cabo Polonio, one of the areas with the best potential for tourism, as it forms part of Bañados del Este. The investments in Cabo Polonio include: (i) visitor welcome facilities at Cabo Polonio's primary point of access, including a tourist information center, ticket sales areas for the various transportation enterprises authorized to provide access to Cabo Polonio, waiting areas, public restrooms, and parking; and (ii) an eco-center in Cabo Polonio, including a nature-focused interpretive center, created by renovating the old sea lion slaughterhouse facilities, restaurant and shopping facilities, restrooms, viewpoints, and an interpretive trail. The component also includes the restoration of Villa Serrana (in the Department of Lavalleja) as a primary node of an alternative nature circuit, thus creating a new offering aimed at regional and extraregional tourism visiting Punta del Este. The restoration includes the rehabilitation of a unique building that will house food services, as well as the construction of a small visitor center providing tourist information.

- c. *Hot springs region (Salto – Paysandú corridor; US\$1.2 million).* This area's tourist draw is primarily centered around the hot springs and nautical tourism. Tourism development is currently focused on the hot springs. To improve the competitiveness of this offering, which is significant in terms of breaking the seasonality of tourism in Uruguay, the program includes minor works aimed at: (i) enhancing the quality of existing thermal spring facilities, some of which are quite obsolete; (ii) providing innovation in the range of products offered in the current facilities by developing new options; and (iii) ensuring the conservation of the wells that supply the thermal waters. The works mentioned will be defined through a reengineering plan for the current thermal spring system, aimed at modernizing and optimizing the current thermal spring offering. Infrastructure investments are also planned to facilitate river tourism, through the generation of a strategic network of nautical bases made up of small jetties and moorings, as well as tourist information facilities. These investments on the river are expected to fulfill the dual objective of promoting the river area (along the Uruguay River and tributaries) y revitalizing the current hot springs tourism offering by linking it to new possibilities for tourist recreation.
- 2.4 This first component also includes the development of a National Tourism Marketing Plan and the actions planned during its first year of execution. This plan will include the offering generated within the framework of the program in each of the three priority areas. The plan will update the marketing efforts made by the country to date with a medium- and long-term perspective.
- 2. Improving the institutional framework for tourism (US\$1 million)**
- 2.5 This component's actions will be aimed at strengthening tourism administration both nationally and locally:
- a. *Strengthening the national tourism administration.* This subcomponent will include technical assistance and training to modernize the organization and management of MINTURD through: (i) the establishment of a Project Management and Innovation Unit; (ii) the improvement of the National Tourist Information System to gather, process, analyze, and disseminate statistical information relevant for decision-making, including the implementation of the national Tourism Satellite Account, and environmental monitoring systems in areas with high tourist traffic; (iii) the optimization of internal processes, including budgetary management, purchasing, payments, management of promotional tools (e.g. the website), communications activities, and customer service; and (iv) the optimization of current legislation and the application of the incentive framework to the sector.
 - b. *Strengthening municipal administrations.* This subcomponent will include process reengineering for tourism and environmental management; technical assistance for the administration of works under their jurisdiction; training courses for municipal technicians on tourism development planning and

management; support for the drafting and/or updating of sustainable local tourism development plans; and raising awareness among local communities of the risks and benefits of tourism development.

C. Cost and financing

- 2.6 The program is a targeted investment operation whose estimated cost is US\$6.25 million. The Bank will finance US\$5 million (80%), while the local counterpart, equivalent to US\$1.25 million (20%), will be contributed by the federal government. The cost and financing plan is presented in the following table:

Table I. Program cost and financing
(in US\$ thousands)

| Category | Bank | Local | Total | % |
|---|--------------|--------------|--------------|--------------|
| I. Administration and oversight | 300 | 200 | 500 | 8.0 |
| II. Direct costs | 4,500 | 800 | 5,300 | 84.8 |
| 2.1 Structuring and promotion of tourist destinations | 3,800 | 500 | 4,300 | 68.8 |
| 2.2 Improving the institutional framework for tourism | 700 | 300 | 1,000 | 16.0 |
| III. Indirect costs | 200 | | 200 | 3.2 |
| 3.1 Midterm and final evaluations | 50 | | 50 | 0.8 |
| 3.2 External audits | 50 | | 50 | 0.8 |
| 3.3 Contingencies | 100 | | 100 | 1.6 |
| IV. Financial costs | - | 250 | 250 | 4.0 |
| 4.1 Interest | | 240 | 240 | 3.8 |
| 4.2 Credit fee | | 10 | 10 | 0.2 |
| 4.3 Inspection and supervision fee | 0 | | 0 | 0 |
| Total | 5,000 | 1,250 | 6,250 | 100.0 |

III. PROGRAM EXECUTION

A. Borrower and executing agency

- 3.1 The borrower will be the Eastern Republic of Uruguay and the executing agency will be the Ministry of Tourism and Sports (MINTURD) through its General Secretariat.

B. Program execution and management

- 3.2 As executing agency, MINTURD will be responsible for general administration, financial-accounting management, program monitoring and control, as well as the procurement of designs, execution and oversight of works, while ensuring compliance with environmental legislation throughout the project cycle.
- 3.3 The municipal councils will be an integral part of program execution, since they will participate in the review and approval of the technical bidding documents for the works, support MINTURD during works execution, and be responsible for

operation and maintenance of the investments. The strengthening of local agencies under the project will sufficiently ensure that they play their role in the project cycle effectively. The works in Cabo Polonio will be managed under the responsibility of an Administrative Commission to be established for such purposes.

1. The Ministry of Tourism and Sports (MINTURD)

- 3.4 MINTURD's responsibilities include: (i) opening separate bank accounts and maintaining accounting records allowing identification of the sources and uses of program resources by component; (ii) preparing and submitting disbursement requests to the Bank as well as appropriate justification for eligible expenses and audited program financial statements; (iii) preparing calls for proposals and bidding processes upon prior approval of the respective municipal council when the activity is undertaken in its jurisdiction, and undertaking procurement, the respective payments, and technical and environmental oversight of the contracts for program activities; (iv) performing periodic inspections of the works during their execution and the subsequent monitoring of the operation and maintenance thereof; (v) preparing, submitting to the Bank, and making available to the public the required monitoring and evaluation reports; and (vi) ensuring compliance with the contractual clauses established in the Loan Contract and the agreements to be entered into with the beneficiary municipal councils. MINTURD has an established integrated accounting system that will allow adequate financial administration of the program and timely reporting.
- 3.5 MINTURD will carry out its duties through its General Secretariat. Its Director General will be responsible for execution, administration, and oversight of the program. Its Financial-Accounting Division will assist in the administrative, financial, and accounting management of the resources allocated under the program, and its Strategic Planning Division will assist in the review of compliance with the targets established in the logical framework (Annex I) and program evaluation. As a result of the analysis of the works documentation submitted by MINTURD to the Bank, the need was established to support the General Secretariat in its project review capacity through a team of consultants, including a coordinator specialized in project management and three specialists in the areas of procurement, finance-accounting, and monitoring systems. The Secretariat will also have the support of specific consulting services for the economic and environmental evaluation of projects.

2. Municipal councils

- 3.6 The responsibilities of the municipal councils participating in the program include: identifying the institutional strengthening activities necessary for proper tourism management to be addressed by the program; implementing the institutional cost recovery mechanisms to cover the operation, maintenance, and depreciation of the works, once transferred to their jurisdiction; documenting the right of ownership or possession of the land where the works will be executed and turning them over free of occupants, if necessary; collaborating in the processing of authorizations,

permits, approvals, easements and other internal processes required by projects in their jurisdiction; allowing free, unrestricted access to the construction areas for the works, for MINTURD, contractors, external auditors, and the Bank, during program execution and for five years following the final loan disbursement; operating and properly maintaining the projects, in accordance with generally accepted technical standards and the applicable works management plan, and reporting annually to MINTURD on the status of this work; and maintaining an annual record of visitors and revenues generated for each of the program's investments. These responsibilities will be formalized in agreements between MINTURD and the municipal councils of the destinations selected for the investments, in principle, Rocha, Salto, and Colonia. **The entry into effect of the agreements between the executing agency and the municipal councils, in the terms agreed upon with the Bank, will be a condition precedent to the first open call for proposals for works under the respective municipal jurisdictions.**

3. Administrative works commission in Cabo Polonio

- 3.7 Since Cabo Polonio is located in Bañados del Este, a Biosphere Reserve and Ramsar site, the program plans to establish an administrative commission comprising at least MINTURD, the Rocha Municipal Council, the Ministry of Livestock, Agriculture, and Fisheries, acting through its relevant office, and the Ministry of Housing, Regional Planning and the Environment, acting through its National Department of the Environment (DINAMA), which will be responsible for the management, including operation and maintenance, of the works for the eco-center planned for Cabo Polonio, within the framework of component 1. The commission will be the mechanism for participation by all institutions having jurisdiction in Cabo Polonio and, in particular, DINAMA, the entity responsible for the development, evaluation, and oversight of the National Environmental Protection Plans, and the implementation of the National Protected Area System, and whose organization includes the Ramsar representative responsible for Uruguay. This commission's responsibilities will include, among others: approving the technical bidding documents for the planned works prior to the start of physical execution, operating and properly maintaining the projects, in accordance with generally accepted technical standards and the applicable works management plan, and reporting annually to MINTURD on the status of this work; implementing cost recovery mechanisms to cover the operation, maintenance, and depreciation of the works, once they are transferred to it; and maintaining an annual record of visitors and revenues generated for each of the program investments. **The entry into effect of the legal mechanism creating this commission, in the terms agreed upon with the Bank, will be a condition precedent to the first call for proposals for the activities to be performed in Cabo Polonio.**

C. Preparation and oversight of works

- 3.8 MINTURD will hire and supervise the work of consulting firms, who will prepare the executive projects for the works under their responsibility, following the guidelines established in the *Instructions for the preparation of the program's*

executive projects. The instructions define the scope of the technical support documentation for the execution, to be prepared by type of work: engineering studies; drawings; technical specifications; construction schedule; management plan; economic viability study; cost recovery study; and environmental study.

- 3.9 The works under the jurisdiction of the municipal councils must comply with the pertinent legislation in terms of the environment, building and planning, safety, and access to persons with disabilities, among other issues. To verify compliance with these standards, MINTURD will send the technical documentation on the works to the applicable municipal councils for their approval, in accordance with pertinent legislation. Environmental studies will be sent for approval to the applicable agency based on the jurisdiction of each project. For works in areas declared historical or cultural heritage sites, the technical support documentation for execution will be sent to the National Heritage Commission for its approval. For the works in Cabo Polonio, DINAMA will review the consistency of the technical documentation for execution of the works with the Master Plan for the Bañados del Este Biosphere Reserve. Once the applicable approvals are received, MINTURD will send the technical support documentation for execution of the works to the Bank for its no objection.
- 3.10 MINTURD will be responsible for the technical oversight and verification of compliance with environmental legislation by contractors. The contracts for the program's works will include the environmental measures that result from such legislation, including a socioenvironmental management plan for the construction phase. For works under municipal jurisdiction, oversight will be performed jointly with the municipal council responsible for the operation and maintenance of the work. To carry out the oversight, MINTURD will have the assistance of consulting services, following the guidelines established in the *General instructions for oversight of program works*. As part of its semiannual execution report, MINTURD will submit the results of its oversight work, indicating progress made in compliance with environmental legislation, general problems encountered, and measures adopted to resolve them.

D. Operation and maintenance

- 3.11 After program works are completed and transferred to the beneficiary municipal councils, the councils will perform the operation and maintenance, based on their respective areas of jurisdiction and according to a management plan developed using the criteria established in the *Instructions for the preparation of the program's executive projects*. This plan will be submitted to the Bank for its no objection, as part of the technical support documentation for execution of the works. For the two larger scale works included in the program, the interpretive center in Colonia and the eco-center and visitor welcome facilities in Cabo Polonio, the annual costs of both projects were estimated at US\$170,000 and US\$22,700, respectively. The technical support documentation for execution of the works to be submitted by MINTURD to the Bank for its no objection will include a cost recovery study for these projects based on the estimates in the management plan, as

- well as the depreciation costs associated with the works. The cost recovery mechanisms available to the municipal councils include the introduction or adjustment of visitor entry fees and the concession taxes on the services that will be located in the works financed by the program. The implementation of the cost recovery mechanisms by the entity responsible for operation and maintenance will be monitored in the program evaluation reports.
- 3.12 For the investments in Colonia and Cabo Polonio, the respective management plans will aim to revitalize the set of destinations in the area, and provide the necessary coordination with the private sector. These plans will be used to focus the coordination efforts between MINTURD, the participating municipal councils, and tourism entrepreneurs, on specific tourism offerings. The plans will include: (i) a description of the demand and target segment objectives; (ii) the design of priority tourism products based on these segments, including interpretive, educational, and graphical content for the centers and proposals for thematic tours associated with this content in the destinations; (iii) identification of the key private participants and the mechanisms for their participation in leveraging the benefits derived from the products; (iv) design of communications and promotional activities, including a calendar of events; (v) guidelines for the proper maintenance of the facilities and their content; and (vi) the human resources necessary for their proper implementation. The plan will have an itemized cost budget. The management plans will form part of the technical bidding documents for works execution and be developed by teams made up of specialized tourism management professionals.
- E. Procurement of goods and works and contracting of consultants**
- 3.13 Goods, related services, and works will be procured in accordance with the Policies for the procurement of works and goods financed by the IDB dated July 2006 (document GN-2349-7). Consulting services using program resources will be selected and contracted in accordance with the Policies for selection and contracting of consultants financed by the IDB dated July 2006 (document GN-2350-7). International competitive bidding will be used for works whose estimated cost is greater than or equal to US\$3 million and for goods and related services whose estimated cost is greater than or equal to US\$250,000. The contracting and selection of consulting services whose estimated cost is greater than or equal to US\$200,000 will be announced internationally. The procurement of goods and services planned for the first 18 months of program execution is included in the Procurement Plan (see Annex II).
- 3.14 Considering that MINTURD has no prior experience executing operations with the Bank, it has been determined that initially all procurement will be subject to ex ante review. Twelve (12) months after the first procurement, periodic reviews and inspection visits will be conducted and the reports on the external audit of the program's financial statements will be submitted to determine the quality of MINTURD's internal controls. Based on the results of this analysis, it will be determined whether ex post review is possible for procurement processes and disbursements for works and goods under the thresholds for international

competitive bidding and consulting contracts for under US\$200,000 for consulting firms, and under US\$50,000 for individual consultants. The ability to undertake procurement subject to ex post review may be revoked in whole or in part at any time and, based on the results of ex post reviews, financing may be denied from both loan and counterpart resources.

F. Revolving fund

- 3.15 In order to provide advances on resources for the performance of activities financed by the loan, a revolving fund will be established, limited to 5% of the amount of the Bank's loan.

G. Execution period and disbursement schedule

- 3.16 The program's disbursement period will be four years. The disbursement schedule is presented in the following table:

Table II. Disbursement schedule
(in US\$ millions)

| | Year 1 | Year 2 | Year 3 | Year 4 | Total |
|--------------------|---------------|---------------|---------------|---------------|--------------|
| IDB | 0.75 | 2.25 | 1.25 | 0.75 | 5.00 |
| Local contribution | 0.19 | 0.56 | 0.31 | 0.19 | 1.25 |
| Total | 0.94 | 2.81 | 1.56 | 0.94 | 6.25 |
| % | 15 | 45 | 25 | 15 | 100 |

H. Monitoring and evaluation

- 3.17 MINTURD will monitor and evaluate compliance with the periodic quantitative targets associated with the outcome and impact indicators established in the logical framework (Annex I). To do so, MINTURD will have a computerized monitoring system that will integrate the operation's financial-accounting management with the periodic achievement of results. This system will also allow the monitoring of potential socioenvironmental impacts, as well as compliance with the management plans once the investments are implemented. For the periodic measurement of outcomes and impacts, the General Secretariat will have the support of the Strategic Planning Division, which will collect and process annual statistical information associated with the applicable indicators described in the logical framework. This division will be strengthened by the National Tourist Information System and the implementation of the Tourism Satellite Account, which will allow for the standardization of the information that currently comes from inbound tourism surveys periodically conducted by MINTURD.
- 3.18 MINTURD will prepare and submit to the Bank, no later than 30 May and 30 November of each year during program execution, a monitoring report on the progress of activities. These reports will be focused on compliance with the outcome indicators and progress on the results specified in the logical framework (Annex I). These reports will include the results of the monitoring of the

environmental impact of tourism in protected areas and in areas with historical and cultural heritage, and will analyze any problems encountered and the corrective measures taken. The reports for the second half of each year will also include the schedule for the next calendar year, with a projection of disbursements and an updated procurement plan. Adjustments to the program based on discussion of these reports will be agreed upon with the Bank in the respective meetings to be held every six months. Once accepted by the Bank, the monitoring reports will be made available to the public on the program page in the MINTURD website.

- 3.19 As part of the program's evaluation, MINTURD will prepare and deliver to the Bank a midterm evaluation report within 90 days after the date on which 50% of the loan proceeds have been committed, and a final evaluation report within 90 days after the date on which 90% of the loan proceeds have been disbursed. These reports will include: compliance with the targets for outcomes and results and progress on the expected impacts, based on the indicators established in the program's logical framework; the effectiveness and efficiency of the project preparation process, with emphasis on quality, time, and cost; the level of compliance in the implementation of cost recovery mechanisms ensuring the sustainability of the investments transferred to the municipal councils; a summary of the socioenvironmental impacts of tourism in protected areas and areas declared historical and cultural heritage; and the level of compliance with contractual commitments and pertinent agreements. Once accepted by the Bank, these two evaluation reports will be made available to the public on the program page in the MINTURD website. These evaluations will be conducted by consultants who will be hired by MINTURD and financed with program resources. The reports, including statistical support information and documentation, will remain available for ex post evaluation, if the government or the Bank decides to do so after completion of the program. **The executing agency will submit the program's midterm evaluation report to the Bank within 90 days after the date on which 50% of the loan proceeds have been committed, and the program's final evaluation report within 90 days after the date on which 90% of the loan proceeds have been disbursed.**

I. Audit

- 3.20 The program's annual and final financial statements will be submitted by MINTURD, in accordance with the Bank's rules and procedures, during execution, and will be audited by the Federal Audit Court.

IV. VIABILITY AND RISKS

A. Institutional viability

- 4.1 The viability of the program's proposed execution system was evaluated during program preparation based on three considerations: (i) MINTURD's ongoing obligations; (ii) the quality of the technical documentation for the works submitted to the Bank for its review; and (iii) the results of the institutional capacity analysis

of MINTURD using the Institutional Capacity Assessment System (ICAS) methodology.

- 4.2 Consistent with its ongoing obligations, MINTURD was assigned the execution, monitoring, and evaluation of activities, in addition to general administration and financial-accounting management responsibilities. Based on this assignment of responsibilities, the planning, execution, and control capacity of its organizational units was analyzed using the ICAS. As a result of this analysis, the general institutional capacity of MINTURD was classified as satisfactory and low-risk. The analysis determined that the entity has adequate systems of personnel administration, administration of goods and services, and financial administration, ensuring an adequate execution capacity. Its personnel administration system is governed by the guidelines set forth in the National Civil Service Act, which establishes the professionalization of public sector employment with attributes such as merit, capacity, service vocation, efficient performance of duties, accountability, and honesty. Its goods and services administration system is framed within the State Purchasing Information System, which is based on a public sector procurement management model that allows analysis of the various stages of the purchasing process, the identification of the organizational unit placing the order, interaction with the publications site, and the interrelation of the stages in the purchasing process with those in the expenditure process through their connection in the Integrated Financial Information System (SIIF). Its financial administration operates within the framework provided by the SIIF, which facilitates the recording, monitoring, and evaluation of all of the government's budgetary and financial operations using open computer technology and enhancing the accounting-financial management of public resources.
- 4.3 The analysis also determined that MINTURD needs to strengthen some aspects of its programming activities. Although the five-year budget tool allows the entity to perform this task, by establishing associated targets and objectives to be met each year, the ICAS classified this system as medium-risk, since the entity does not have a formal procedure for performance of this function. To address this weakness, the program established the drafting and submission of annual work plans as part of the semiannual monitoring reports.

B. Socioeconomic viability

- 4.4 The economic benefits of tourism programs can be measured using various indicators, including: (i) net foreign exchange revenues; (ii) benefits associated with employment, or the value of the employment generated as a result of tourist spending in the destinations served by the project, less the value of the employment lost in other tourist destinations not visited by the same tourists; and (iii) benefits perceived by tourists, or the increase in the value the tourists attributed to the improvement in the destinations, traditionally measured using surveys and random utility models. In theory, the economic viability of the investments in a tourist area should be calculated using estimates of the internal rate of return or the discounted flow of net profits, using quantitative information from the indicators mentioned

above. This methodology should consider that some investments serve both tourists and residents (e.g. improvements in urban areas) and that some of the economic benefits of tourism are also generated by complementary private investments.

- 4.5 Given the lack of reliable quantitative information allowing an accurate estimate of the economic viability of the set of investments in each of the selected tourist areas, the economic analysis focused on the program's two largest investments: (i) the interpretive center in Colonia; and (ii) the eco-center and visitor welcome facilities in Cabo Polonio, Rocha. The methodology outlined below will be used as the basis for conducting the economic viability analysis that MINTURD will submit to the Bank as part of the technical support documentation for the execution of the rest of the works planned under the program.

- a. **Interpretive center in Colonia.** For the calculation of revenues, only those generated by center ticket sales were considered. This calculation used the official figure of international visitors entering Uruguay through Colonia in 2005 (456,000),⁵ as well as the estimate of domestic visitors by the Colonia Tourist Information Office, based on the proportion of Uruguayans who ask questions in this office (20% of the total number of foreign visitors, or 91,200). Considering the strategic location of the center, near the point of entry to the country by river, a conservative rate of likelihood of visiting the center of 50% of total arrivals (273,600) was adopted. It was assumed that only 75% of those visiting the center would pay to enter the interpretive circuit (205,200), since access to the food service and merchant areas would be free. The calculation considered a fixed average entry fee of US\$2.2, which is considered reasonable for the center's target segments, as well as an annual growth rate of foreign visitors entering Uruguay through Colonia that reflects this rate between 1999 and 2005 (2%). To calculate costs, the investment expenses over the three years of execution were considered, as were constant operating and maintenance costs over time. Considering a 10-year analysis horizon, the net present value (NPV) of the net profits from the investments, discounted at a rate of 12%, was estimated at US\$54,496; the internal rate of return (IRR) was estimated at 13.4%. This conservative calculation does not include economic benefits from the food services and merchants offered at the center.

⁵ Annual Statistics 2006, Inbound tourism, Ministry of Tourism and Sports.

Table III
Economic return on Interpretive Center, Colonia
(in US\$ thousands)

| | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Year 6 | Years 7-10 |
|-------------------------------|--------|---------|---------|--------|--------|--------|------------|
| A. Revenues from ticket sales | | | | 451.4 | 460.5 | 469.7 | 479.1* |
| B. Cost of investment | 17.0 | 933.0 | 250.0 | | | | |
| C. Operation and maintenance | | | | 170.0 | 170.0 | 170.0 | 170.0 |
| Net profit (A-B-C) | (17.0) | (933.0) | (250.0) | 281.4 | 294.5 | 299.7 | 309.1 |
| Net Present Value | 54.5 | | | | | | |
| Internal Rate of Return | 13.4% | | | | | | |

* Assuming annual growth of 2%.

- b. **Eco-center and visitor welcome facilities in Cabo Polonio, Rocha.** Cabo Polonio is an area with restricted tourist access that can only be reached in authorized vehicles. The calculation of revenues only considered those generated by ticket sales. This calculation used the record of entries into Cabo Polonio for 2005, through ticket sales by authorized vehicles (45,600). The calculation considered a fixed average price of US\$4, representing an increase of US\$3.4 with respect to the current entry fee. It assumed an annual growth rate of visitors to Cabo Polonio reflecting this rate between 2001 and 2005 (2.3%). To calculate costs, the investment expenses over the two years of execution of the eco-center and the visitor welcome facilities were considered, as were the constant operating and maintenance costs of the eco-center. Considering a 10-year analysis horizon, the NPV of the net profits from the investments, discounted at a rate of 12%, was estimated at US\$4,717; the IRR was estimated at 12.2%. This conservative calculation does not include economic benefits from the food services and merchants offered at the eco-center.

Table IV
Economic Return on Eco-center and Visitors Facilities
in Cabo Polonio, Rocha
(in US\$ thousands)

| | Year 1 | Year 2 | Year 3 | Year 4 | Year 5 | Years 6-10 |
|-------------------------------|---------|---------|--------|--------|--------|------------|
| A. Revenues from ticket sales | | | 186.0 | 190.3 | 194.7 | 199.1* |
| B. Cost of investment | 10.6 | 858.1 | | | | |
| C. Operation and maintenance | | | 22.7 | 22.7 | 22.7 | 22.7 |
| D. Net profit (A-B-C) | (10.6) | (858.1) | 163.3 | 167.6 | 172.0 | 176.5 |
| Net Present Value | 4,717.4 | | | | | |
| Internal Rate of Return | 12.2% | | | | | |

* Assuming annual growth of 2.3%.

- 4.6 The program's logical framework (Annex I) includes key outcome indicators that will allow annual monitoring of the flow of ticket sale revenues for both the

interpretive center in Colonia and the eco-center and visitor welcome facilities in Cabo Polonio. In each case, the annual targets are based on the values estimated in the economic analysis, which will allow us to evaluate the return on these investments upon completion of the program.

C. Financial viability

4.7 A detailed financial analysis was performed on the two largest investments in order to verify that the flows of revenues and expenditures will allow for their satisfactory operation and maintenance. The investments analyzed were the interpretive center in Colonia and the eco-center and visitor welcome facilities in Cabo Polonio, Rocha.

4.8 **Interpretive center in Colonia:** It is estimated that the operation and maintenance of the project will represent an annual cost of US\$170,000. Its annual cost of depreciation is estimated at US\$80,000, assuming straight-line depreciation over 15 years. Consistent with the socioeconomic viability analysis, considering an estimate visitor flow of 205,200 per year, the collection of a fixed average entry fee of US\$2.2 would allow for annual revenues of US\$451,440, which would cover the annual costs of operation, maintenance, and depreciation (US\$250,000) required for the project. The revenue calculation did not consider other revenues from service concession taxes.

4.9 **Eco-center and visitor welcome facilities in Cabo Polonio, Rocha:** The annual operation and maintenance cost of the works in Cabo Polonio was estimated at US\$22,700. The annual depreciation costs for these works were estimated at US\$57,300, considering straight-line depreciation over 15 years. Consistent with the socioeconomic viability analysis, the calculation of revenues considered only those generated by entries into Cabo Polonio. Assuming a constant visitor flow equal to that recorded in 2005 (45,600) and a fixed average entry fee of US\$4, projected annual revenues would total US\$182,400. This amount would cover 100% of the annual operation, maintenance, and depreciation costs of the works (US\$80,000).

D. Socioenvironmental sustainability

4.10 The program seeks to strategically increase tourism revenues in the selected destinations by creating new tourism offerings and products capable of drawing new segments of demand. In this regard, the activities included in the program include the implementation of infrastructure for the development of this demand and interventions to allow enhanced public management of these areas.

4.11 Based on the types of projects to be financed by the program, potential environmental effects and impacts were analyzed. The analysis concluded that these effects and impacts are minor, and easy to identify and mitigate using good practices in the construction and operation phases. As a result, the program includes the following recommendations: (i) preparation of a socioenvironmental management plan for the prevention and mitigation of potential impacts of the

investments and the establishment of environmental guidelines for the preparation of the feasibility studies and designs of specific works, both contained in the *Instructions for the preparation of the program's executive projects*; (ii) compliance with national and local environmental legislation for the executive projects, which includes the submission of pertinent environmental studies; (iii) inclusion of environmental mitigation measures and obligations in the construction contracts; and (iv) environmental oversight as part of the general technical oversight of works, following the guidelines established in the *General instructions for oversight of program works*, the results of which will be included in the program's monitoring and evaluation reports.

- 4.12 The program includes the implementation of an interpretive center in the historic center of Colonia (US\$1.2 million), declared a World Heritage Site by UNESCO, as well as an eco-center and visitor welcome facilities in Cabo Polonio (US\$868,000), an area that is part of the Bañados del Este Biosphere Reserve and a Ramsar site, and which has been proposed to enter the country's National Protected Area System. Both investments imply a restoration of the beneficiary areas and will represent significant means of raising environmental and cultural awareness, among both visitors and residents. During program preparation, socioenvironmental evaluations were conducted on both projects, and they were classified as "projects or works whose execution would not represent negative environmental impacts or could present minor environmental impacts, within acceptable levels pursuant to current legislation." The evaluations recommended socioenvironmental management plans for the projects' construction and operation phases, and these plans are included in the *Instructions for the preparation of the program's executive projects*. For the Colonia project, the technical support documentation for execution is also to be submitted to the National Heritage Commission for its approval (§3.9). For the Cabo Polonio works, plans include the creation of an administrative commission, including DINAMA and the Ramsar representative in Uruguay, to ensure participation and a high degree of coordination for proper environmental management (§3.7). As the agency responsible for the National Protected Area System, DINAMA will review the consistency of the technical documentation for execution of the works in Cabo Polonio with the Master Plan for the Bañados del Este Biosphere Reserve, published in 2000.
- 4.13 The implementation of the foregoing recommendations will be up to MINTURD as the party responsible for oversight and verification of compliance with environmental legislation by contractors. MINTURD will have the support of an environmental specialist to perform these duties, as well as works oversight firms responsible for overseeing compliance with contractual environmental protection obligations. Moreover, MINTURD's monitoring system will allow the environmental monitoring of tourism, particularly in protected and historical and cultural heritage areas. The program's midterm and final evaluation reports will include a summary of the results of this monitoring, and will analyze the level of compliance with environmental legislation in the execution of the works.

- 4.14 The analysis of the project typology also concluded that they will generate positive social impacts due to the additional benefits that the investments will provide to local communities. The analysis also included a review of domestic legislation for impact assessment and concluded that there are clear procedures and adequate established responsibilities, such that domestic legislation will be followed to assess the environmental impacts caused by the works. The actions included in the Program to Modernize and Develop Environmental Institutions (UR-L1033), currently in preparation, are expected to contribute to improving the institutional framework for national environmental policy.
- 4.15 As part of the program's consultation process, MINTURD held three information and awareness workshops in the cities of Salto (11 September 2006), Colonia (14 September 2006), and Montevideo (15 September 2006). These workshops validated the tourism map of Uruguay, presented the objective, selected tourist destinations, and components of the proposed operation, discussed challenges, and identified needs with representatives of DINAMA, the municipal administration of each destination identified, the local private sectors, and civil society. The comments and recommendations arising from these workshops were incorporated into the program.
- 4.16 This operation does not qualify as a project promoting social equity, as described in the key objectives for the Bank's activity contained in the report on the Eighth General Increase in Resources (document AB-1704). This operation does not qualify as a poverty-targeted investment.

E. Benefits and beneficiaries

- 4.17 The primary beneficiary will be the private tourism sector, through improving the capacity of the destinations to attract, retain, and satisfy tourists. The program will benefit the local populations directly by offering new business and job opportunities, as well as better options for leisure and recreation. The program will also generate social benefits by contributing to the restoration and conservation of the country's cultural and natural heritage.
- 4.18 The main expected outcome will be the increase in foreign exchange from tourism activity in the selected destinations. Specifically, the following results are expected from the project: (i) changes in the origin and motivations of visitors; (ii) increase in average spending per day/tourist in the selection destinations; and (iii) expansion of the tourist season.

F. Risks

- 4.19 **Interinstitutional coordination:** Program execution will require close collaboration between MINTURD, the beneficiary municipal councils, and the private sector, to ensure efficient execution and sustainable investments with an invigorating effect on the destinations. Although these collaborative bonds were successfully developed during joint preparation of the program's preliminary studies, it is essential to ensure nimble and effective process for developing and

overseeing investments. To minimize the potential risk of a lack of coordination between MINTURD and the municipal councils, the program anticipates the direct involvement of the municipal councils in the review and approval of technical documentation for works and activities. In addition, MINTURD's involvement in the execution mechanism of the cluster and production chain competitiveness program (loan 1763/OC-UR) will ensure coordination with the private sector, by bringing that operation's beneficiary businesses under the umbrella of this program.

- 4.20 **Sustainability of demand for inbound tourism.** The program's expected results were quantified, assuming that the country's macroeconomic conditions will remain favorable to tourism, no events will have a negative impact on the sector regionally or internationally, and MINTURD will maintain sustained efforts in marketing Uruguay as a tourist destination.

PROGRAM TO ENHANCE THE COMPETITIVENESS OF STRATEGIC TOURIST DESTINATIONS (UR-L1018)
LOGICAL FRAMEWORK

| Narrative summary | Indicators | | | Means of verification | Assumptions | |
|--|---|-------------------------------------|----------------------------|--|--|--|
| Goal | | | | | | |
| To contribute to creating a growing, sustainable trend in the generation of foreign exchange through tourism in strategic areas. | Impacts | | | Tourism statistics generated by the Ministry of Tourism and Sports (MINTURD) | | |
| | Gross revenues from inbound tourism increase: | | | | | |
| | Region | Baseline 2005 Thousands of US\$ | 2012 Thousands of US\$ | | | |
| | Colonia | 19.2 | 25.9 | | | |
| | Rocha | 13.9 | 18.7 | | | |
| | Hot springs region | 22.7 | 29 | | | |
| | Changes in the seasonal pattern of demand are detected with a greater share of total arrivals in the second and third quarters: | | | | | |
| | Quarter | Baseline 2005 Total arrivals (%) | 2012 Total arrivals (%) | | | |
| | Second | 14.2 | 18 | | | |
| Third | 17.8 | 22 | | | | |
| Purpose | | | | | | |
| To create a proactive framework for tourism development, in which new tourism products and services are designed to capture new segments of demand in Colonia, Rocha-Serranía, and the hot springs region. | Outcomes | | | Gross revenues from inbound tourism increase: | Tourism records and statistics generated by the Ministry of Tourism and Sports (MINTURD) | No situations arise in the primary outbound markets that have a negative effect on the Uruguayan tourism industry. |
| | Number of inbound tourists increases: | | | | | |
| | Region | Baseline 2005 (US\$ millions) | 2010 (US\$ millions) | | | |
| | Colonia | 19.2 | 24 | | | |
| | Rocha | 13.9 | 17.3 | | | |
| | Hot springs region | 22.7 | 27.2 | | | |
| | The diversification of the motivations of visitors to Uruguay changes in percentage terms as follows: | | | | | |
| | Primary travel motivation | Baseline 2005 (%) | 2010 (%) | | | |
| | Sun and beach | 47 | 40 | | | |
| Other | 53 | 60 | | | | |

| Narrative summary | Indicators | | | Means of verification | Assumptions |
|---|--|-------------------|--|--|-------------|
| | <ul style="list-style-type: none">The share of total destinations visited in the country increases: | | | | |
| | Region | Baseline 2005 (%) | 2010 (%) | | |
| | Colonia | 5.7 | 9.2 | | |
| | Rocha | 2.8 | 4.1 | | |
| | Hot springs region | 11.4 | 13.8 | | |
| | <ul style="list-style-type: none">Diversification increases in origin of international tourists, excluding Argentines and Uruguayans residing abroad, as follows: | | | | |
| | Demand | 2005 (%) | 2010 (%) | | |
| | Regional (w/o Argentina) | 13.6 | 19.6 | | |
| | Extraregional | 13.8 | 23 | | |
| | <ul style="list-style-type: none">The total revenues generated by the Colonia interpretive center in years one and two of operation reach US\$451,400 and US\$460,500, respectively.The total revenues generated by the Cabo Polonio eco-center in years one and two of operation reach US\$186,000 and US\$190,300, respectively.Approximately 60% percent of tourism entrepreneurs have a positive perception of the new local management model promoted by the Colonia interpretive center and the Cabo Polonio eco-center by the end of the program. | | | | |
| | Components | | | | |
| New offerings in three selected tourist destinations are structured and promoted. | Outcomes <ul style="list-style-type: none">A strategic marketing plan is completed in year 1 of the program.The activities established in the strategic marketing plan for year 1 of operations are implemented in year 2 of the program. | | <ul style="list-style-type: none">Program monitoring reports | There is close collaboration among MINTURD, the municipal councils, and the private sector during program execution. | |

| Narrative summary | Indicators | Means of verification | Assumptions |
|-------------------|--|-----------------------|-------------|
| | <p><i>Colonia:</i></p> <ul style="list-style-type: none"> • An interpretive center is operating in year 3 of the program. • Four thematic tours are implemented in the colonial part of the city in year 4 of the program. <p><i>Polonio:</i></p> <ul style="list-style-type: none"> • Visitors and tourist information facilities at the point of entry to Cabo Polonio are operating in year 2 of the program. • 2,000 m² are prepared for private vehicle parking at the point of entry to Cabo Polonio in year 2 of the program. • 700 m² are prepared for bus parking for tourist transport at the point of entry to Cabo Polonio by year 2 of the program. • An interpretive center is operating in Cabo Polonio in year 2 of the program. • A 170 m trail for the observation of seal lions is built in Cabo Polonio in year 2 of the program. <p><i>Rocha mountain areas:</i></p> <ul style="list-style-type: none"> • Primary structure of Ventorrillo de la Buena Vista is restored and operating in year 2 of the program. • A visitors and tourist information center is operating on the access road to Villa Serrana in year 2 of the program. <p><i>Salto – Paysandú corridor:</i></p> <ul style="list-style-type: none"> • A reengineering plan for the hot springs offering in Salto is completed in year 1 of the program. • A new administrative system for hot springs managed by public agencies is implemented in year 2 of the program. • A strategic plan for river navigation in the departments of Salto and Paysandú is completed in year 1 of the program. | | |

| Narrative summary | Indicators | Means of verification | Assumptions |
|--|---|--|---|
| Improvement of the institutional framework for tourism | <p style="text-align: center;">Outcomes</p> <p><i>Strengthening of National Tourism Administration (MINTURD)</i></p> <ul style="list-style-type: none"> • Satellite Account is implemented in year 2 of the program. • Improvement in budget management, purchasing, payment, management, and monitoring processes for promotion and customer service in year 2 of the program. • Project Management and Innovation Unit is operating in year 2 of the program. • Improvements in the legal and tax framework are implemented in year 2 of the program. <p><i>Strengthening of Municipal Administrations</i></p> <ul style="list-style-type: none"> • At least three courses on tourism development planning and management for three municipal councils are designed and taught in year 2 of the program. • Three local tourism development plans are implemented in year 3 of the program. • Six municipalities are made aware of the risks and benefits of tourism development in year 3 of the program. | <ul style="list-style-type: none"> • Program monitoring reports | <p>There is close collaboration among MINTURD, the municipal councils, and the private sector during program execution.</p> |

10000/11/15/00

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION

Uruguay. Loan ____/OC-UR to the Eastern Republic of Uruguay
Program to Enhance the Competitiveness of Strategic Tourist Destinations

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Eastern Republic of Uruguay, as Borrower, for the purpose of granting it a financing aimed at cooperating in the execution of a program to enhance the competitiveness of strategic tourist destinations. Such financing will be in the amount of up to US\$5,000,000, from the resources of the Single Currency Facility of the Bank's Ordinary Capital, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.