

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

MEXICO

LAND MANAGEMENT TO ACHIEVE RESULTS UNDER THE CLIMATE CHANGE AGENDA

(ME-1268)

LOAN PROPOSAL

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ABBREVIATIONS

BURs	Biennial update reports
CICC	Comisión Intersecretarial de Cambio Climático [Interdepartmental Climate Change Commission]
CONAFOR	Comisión Nacional Forestal [National Forestry Commission]
CONAVI	Comisión Nacional de Vivienda [National Housing Commission]
ENAIROS	Estrategia Nacional de Manejo Forestal Sustentable para el Incremento de la Producción y la Productividad [National Strategy for Sustainable Forest Management to Increase Production and Productivity]
ENCC	Estrategia Nacional de Cambio Climático Visión 10-20-40 [“Visión 10-20-40” National Climate Change Strategy]
GHG	Greenhouse gas
ICAP	Institutional Capacity Analysis Platform
INECC	Instituto Nacional de Ecología y Cambio Climático [National Institute of Ecology and Climate Change]
INEGI	Instituto Nacional de Estadística y Geografía [National Institute of Statistics and Geography]
IPCC	Intergovernmental Panel on Climate Change
LBR	Loan based on results
LULUCF	Land use, land-use change, and forestry
MSMEs	Micro, small, and medium-sized enterprises
MtCO ₂ e/year	Metric tons of carbon dioxide equivalent per year
NAFIN	Nacional Financiera S.N.C., development banking institution
NDC	Nationally Determined Contribution
PAFSH	Programa de Acceso al Financiamiento para Soluciones Habitacionales [Access to Finance for Housing Solutions Program]
PASH	Portal Aplicativo de la Secretaría de Hacienda [Application Portal of the Department of Finance]
PECC	Programa Especial de Cambio Climático [Special Climate Change Program]
PES	Payment for environmental services
PRONAFOR	Programa Nacional Forestal 2014-2018 [National Forestry Program 2014-2018]
SEDESOL	Secretaría de Desarrollo Social [Department of Social Development]
SEMARNAT	Secretaría de Medio Ambiente y Recursos Naturales [Department of Environment and Natural Resources]
SFP	Secretaría de la Función Pública [Civil Service Department]
SHCP	Secretaría de Hacienda y Crédito Público [Department of Finance and Public Credit]
SNIIV	Sistema Nacional de Información e Indicadores de Vivienda [National Housing Information and Indicators System]
SNMRV	Sistema. Nacional de Monitoreo, Reporte, y Verificación [National Monitoring, Reporting, and Verification System]
TC	Technical cooperation
U1	Intraurban perimeter
U2	First peripheral perimeter
UNFCCC	United Nations Framework Commission on Climate Change

PROJECT SUMMARY

MEXICO LAND MANAGEMENT TO ACHIEVE RESULTS UNDER THE CLIMATE CHANGE AGENDA (ME-1268)

Financial Terms and Conditions				
Borrower: United Mexican States			Flexible Financing Facility ^(a)	
			Amortization period:	Bullet at 15.25 years
Executing agency: Department of Environment and Natural Resources (SEMARNAT), with the participation of the National Forestry Commission (CONAFOR) and the National Housing Commission (CONAVI) as the implementing agencies of priority climate change actions.			Disbursement period:	4 years
			Grace period	Bullet at 15.25 years ^(b)
Source	Amount (US\$)	%	Interest rate:	LIBOR-based
IDB (OC)	600 million	99.83%	Credit fee:	(c)
			Inspection and supervision fee:	(c)
IDB Technical Cooperation^(d)	1 million	0.17%	Weighted average life (WAL):	15.25 years
Total:	601 million	100.00%	Currency of approval:	U.S. dollars
Project at a Glance				
Project objective/description: The objective of this program is to support the Government of Mexico in improving land management to reduce emissions and vulnerability to climate change through three components: (i) land management in the housing sector; (ii) land management in the forestry sector; and (iii) interagency coordination.				
Special contractual conditions precedent to the first disbursement of the loan proceeds: The borrower, acting through the executing agency, will provide evidence of the following to the Bank: (i) the entry into force of the program Operational Guidelines; and (ii) the signature of the project mandate and execution agreement between the borrower, the executing agency, and Nacional Financiera (NAFIN), as the financial agent for the loan (see paragraph 3.9).				
Exceptions to Bank policies: None.				
Strategic Alignment				
Challenges:^(e)	SI	<input checked="" type="checkbox"/>	PI	<input type="checkbox"/>
Crosscutting themes:^(f)	GD	<input type="checkbox"/>	CC	<input checked="" type="checkbox"/>
			IC	<input type="checkbox"/>

^(a) Under the Flexible Financing Facility (document FN-655-1), the borrower has the option of requesting changes to the amortization schedule, as well as currency and interest rate conversions. The Bank will take operational and risk management considerations into account when reviewing such requests.

^(b) Under the flexible repayment options of the Flexible Financing Facility, changes to the grace period are permitted provided that they do not entail any extension of the weighted average life of the loan or last payment date as documented in the loan contract.

^(c) The credit fee and inspection on supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank's lending charges, in accordance with applicable policies.

^(d) Technical cooperation operation ME-T1361, approved on 2 November 2017 (ATN/OC-16456-ME, ATN/OC-16457-ME).

^(e) SI (Social Inclusion and Equality); PI (Productivity and Innovation); and EI (Economic Integration).

^(f) GD (Gender Quality and Diversity); CC (Climate Change and Environmental Sustainability); and IC (Institutional Capacity and Rule of Law).

I. PROJECT DESCRIPTION AND RESULTS MONITORING

A. Background, problem to be addressed, and rationale

- 1.1 Mexico's climate change agenda includes mitigation objectives—reduce greenhouse gas emissions by 22% by 2030—and adaptation objectives, namely: reduce the number of municipios in the “most vulnerable” category by 50% and prevent other municipios from falling into that category; establish prevention, early warning, and risk management systems; and achieve a zero-deforestation rate by 2030. To this end, it establishes the need for systemic changes to move towards a low-emission, climate change-resilient economy. The agenda is based on the General Law on Climate Change and is coordinated around two long-term instruments:
- a. The [“Visión 10-20-40” National Climate Change Strategy](#) (ENCC), which guides the country's actions through 2050. The Department of Environment and Natural Resources (SEMARNAT) coordinates the development and execution of the Government of Mexico's national climate change policy based on the ENCC through the Interdepartmental Climate Change Commission (CICC) made up of 14 federal departments. The Government of Mexico's actions are identified in the Special Climate Change Program (PECC 2014-2018) prepared by the CICC every six years. The PECC includes objectives, targets, indicators, and lines of action to be carried out by the departments.¹ To monitor progress, the departments report to SEMARNAT twice a year on the outcomes of the lines of action, to which they are committed in the PECC 2014-2018.
 - b. [Mexico's Nationally Determined Contribution](#) (NDC) was submitted to the United Nations Framework Commission on Climate Change and formalized under the Paris Agreement. Three objectives of the Paris Agreement are: (i) keep the global temperature rise under two degrees Celsius; (ii) promote adaptation to climate change; and (iii) ensure consistency between financial flows and the abovementioned objectives. The Paris Agreement relies on the NDCs put forward by countries and the information provided for clarity, transparency, and understanding of the NDCs. A transparency framework will be established for this, to facilitate better understanding of the NDCs and periodically and collectively assess progress toward the Paris Agreement objectives (“global stocktake”). A first ambition review, called the Facilitative Dialogue, will take place in 2018, to review the NDCs for 2020 and make them more ambitious. The first review after that will be in 2023, and then subsequently every five years.
- 1.2 One of the main challenges Mexico faces in its climate agenda is the scope of its commitment to the Paris Agreement, which includes a reduction of 211 MtCO₂e/year² by 2030.

¹ The development of the PECC 2014-2018 saw the participation of SEMARNAT and the departments of Agriculture, Livestock, Rural Development, Fisheries, and Food; Health; Communications and Transportation; Economy; Tourism; Social Development; Interior; the Navy; Energy; Public Education; Finance and Public Credit; Foreign Affairs; and Agrarian, Land, and Urban Development.

² This target is equivalent to Peru's total annual emissions in 2012.

- 1.3 This means that Mexico must address two big problems associated with emissions: urban sprawl, and deforestation and forest degradation. Both are directly related to land management, since the distribution of land use remains at a suboptimal balance for implementation of the climate change agenda, due either to the expansion of urban areas, or the search for short-term economic gains at the cost of destroying areas with forest value.³
- 1.4 **The importance of land management.** Effective land-use management is essential to overcome the challenges of the climate change agenda, since it can contribute to the achievement of mitigation objectives; reduce the vulnerability of communities, ecosystems, and infrastructure; and make public spending more efficient. For example:
- a. In urban areas, the horizontal growth of cities is associated with higher greenhouse gas emissions from transportation. Numerous studies have shown that high densities combined with mixed land use shortens daily trips (Chatman, 2008; Crane and Crepeau, 1998) and the number of vehicles per household (Hotzclaw et al., 2002). For example, doubling density in residential areas can reduce the number of miles traveled per automobile by 5% to 12% (Gomez-Ibáñez and Humphrey, 2009) and mitigate the use of motor vehicle transportation per household by 20% to 40% (Gottdiener and Bud, 2005). Less automobile use means lower fuel consumption, which is a key aspect of the climate change agenda, as transportation accounts for 42% of greenhouse gas emissions in Latin America and the Caribbean (Rodríguez Tejerina, 2015). According to the UN-habitat Global Report on Human Settlements (2011), doubling the density of a neighborhood leads to a 30% to 40% decrease in the use of personal vehicles per household. Curbing the expansion of urban land use also helps keep cities surrounded by land use categories such as agriculture and forests, which have greater capacity to absorb greenhouse and other polluting gases (Des Fries et al., 2010).
 - b. In rural areas, deforestation not only causes the rapid release of carbon pools that have been built up over decades in trees and the soil, but leads to lost capacity to remove and store carbon. These pools are replaced by land uses that contribute to higher emissions. By avoiding deforestation, emissions would be cut, and a natural and safe source of carbon capture and storage would be maintained (Seymour, 2016). For that reason, while net forest emissions represent 8% of the global total, reversing the deforestation could reduce total net emissions by up to 30% (Pan et al., 2011; Baccini et al., 2012). Beyond reducing emissions, avoiding and reversing the loss of forests helps diminish the vulnerability of populations to climate change, because of the environmental services forests provide. This includes their effect on water quality, storage, and disposal (Ellison, Futter, and Bishop, 2012), their ability to mitigate the impact of natural disasters (Renaud, Sudmeier-Rieux and Estrella 2013), and their contribution to pollination and pest control (Ricketts et al., 2008), in addition to other products and services they provide (Brandon, 2014).

³ According to the National Institute of Ecology and Climate Change (INECC) (2013), Mexico emits 665 MtCO₂e/year. Of that amount, 3.9% comes from the residential and commercial sector, and 4.9% from land-use changes. Nonetheless, urban sprawl, as well as deforestation and forest degradation, impact other sectors like mobile sources, which account for 26.2% of emissions, 23% of which is attributable to the trucking industry, and 12% to farming.

1.5 Challenges of climate change-related land management in Mexico. Mexico faces the following land management challenges:

- a. The footprint of urban areas continues to grow: while the country's urban population doubled from 1980 to 2010, the surface area of cities increased sevenfold. In some cities, this low-density, peripheral growth resulted in a 25-fold increase in the size of urban areas, while populations have only grown by 330% (Department of Social Development (SEDESOL), 2011). Fifteen percent of the housing stock is unoccupied, as it is located in areas that are lacking services and far away from places of work (Organization for Economic Cooperation and Development (OECD), Herbert et al., 2012). Urban sprawl also has a negative impact on the country's capacity to adapt to climate change. As demonstrated by the Urban Development and Housing Sector Framework Document (document GN-2732-6), a large proportion of vulnerable groups reside in informal residential areas located far outside of the center of cities and are often highly susceptible to extreme events. There are complex links between the impact of climate change and the urbanization process. Combined with increasing urbanization and the existing social and environmental problems in urban areas, risk and vulnerability are likely to worsen (OECD, 2017). Thus, if urban growth and development patterns contribute to increasing greenhouse gas emissions, the urban population and infrastructure are also at increasing risk in terms of the detrimental effects of climate change (IFRC, 2010).
- b. Another factor in land management that impacts Mexico's ability to reduce emissions is related to its dedicated forest land. Despite a downward trend, gross annual deforestation in Mexico between 2007 and 2011 was 348,013 hectares (National Forestry Commission (CONAFOR), 2015), which generated emissions of 32 MtCO₂e/year (INECC and SEMARNAT, 2015). This led to a significant loss of economic opportunities, ecosystem functionality, and environmental services (Sarukhán, 2009). Forests have been lost in favor of expanding farming, tourism, urban, and industrial zones, which are more profitable. This transition has been facilitated by a lack of control mechanisms and weak coordination between land policies and stakeholders (CONAFOR, 2017).
- c. Although the urban and forestry sectors are closely linked insofar as land-use policies guide their development, land management now faces the challenge of aligning those policies with the achievement of climate change agenda targets. Another issue to be considered is the need to take the necessary steps to ensure that the system for tracking the objectives, strategies, indicators, and lines of action of the next PECC is robust, reflecting national circumstances and international best practices in monitoring, reporting, and verification.

1.6 Existing programs. While the Government of Mexico has made headway over the last few years in coordinating land management and climate change, these changes are recent and require support to become entrenched:

- a. Land-use planning became a part of Mexico's policy agenda in the 1940s with isolated actions aimed at capitalizing on regional potential for economic development. But it was only in 1976, with the enactment of the General Law on Human Settlements, that a federal legal entity was introduced to regulate the organization of the national space (Rebora, 1978). This law, however,

focused on regulating urban settlements to address the rapid growth of population centers. The rural sector, especially its ecological dimension, was included in land-use planning with the 1982 Federal Law on Environmental Protection and the 1988 General Law on Ecological Balance and Environmental Protection (Wong, 2009).

- b. Mexico's body of land-use planning laws was gradually integrated through the parallel evolution of these two laws, resulting in a lack of coordination in land-use policy. Urban areas became governed by the State Land-use Planning Programs, and the rural, ecological environment by the Ecological Land-use Plans. This disconnect has exacerbated the difficulties with the definition of land-use concepts, the organization of responsibilities at the different levels of government, and the inclusion land-use in public administration planning and sector management tools (Wong, 2009).
- c. The new General Law on Human Settlements, Land-use Planning, and Urban Development was passed in 2016. This law seeks to consolidate coordination between the federal government, federative entities, and municipios for the regulation of human settlements, in order to set rules for their land-use planning.
- d. At the same time, the Government of Mexico has made headway in coordinating federal sector actions in the country and in its focus on climate change goals. In urban areas, one of the main challenges has been creating incentives for housing subsidies offered by the National Housing Commission (CONAVI) to go primarily to city center areas that are higher-density, more accessible to employment, and have more urban amenities. In rural areas, the agenda focuses on reducing emissions caused by deforestation and forest degradation and expanding carbon sinks. This includes the strengthening of CONFOR's management, reforestation, and conservation efforts.
- e. CONAVI is implementing the Access to Finance for Housing Solutions Program ([PAFSH](#)), which provides support for the acquisition of lots with access to utilities, home purchases, improvement projects, and self-production. For the 2014-2018 period, the PAFSH has established lines of action, targets, and indicators, as well as an estimated budget and operating rules for implementation. PAFSH subsidies are solely for low-income households. Thus, the PAFSH program fills in a market gap by helping families that do not earn enough to own a home and cannot access a mortgage that meets their needs.⁴ As of 2014, CONAVI includes incentives to improve the geographic targeting of subsidies, so that housing policy can be better aligned with the climate change agenda. To this end, the urban containment perimeters geostatistical model has been created. This model assigns differentiated values to the urban areas of each one of the 384 cities forming the national urban system, according to the proximity of sources of employment and the

⁴ Through August 2017, 94.1% of subsidies have been for beneficiaries earning up to 2.7 times the minimum wage, whereas in 2016, that figure was 62.9%.

existence of services.⁵ Locating housing in the central perimeters with access to sources of employment, goods and services, and urban amenities lowers energy consumption in transportation and, therefore, greenhouse gas emissions. Medina (2012), in fact, finds a negative correlation between density and energy consumption and transportation. Thus, the policies of cities and urban action are part of the climate solution. The way cities grow and operate influences the demand for energy and, therefore, greenhouse gas emissions. Lifestyles, spatial shape, and availability of public transportation are also crucial. Urban policies, such as densification, can complement global climate policies and reduce the overall cost of lowering emissions (OECD, 2010).

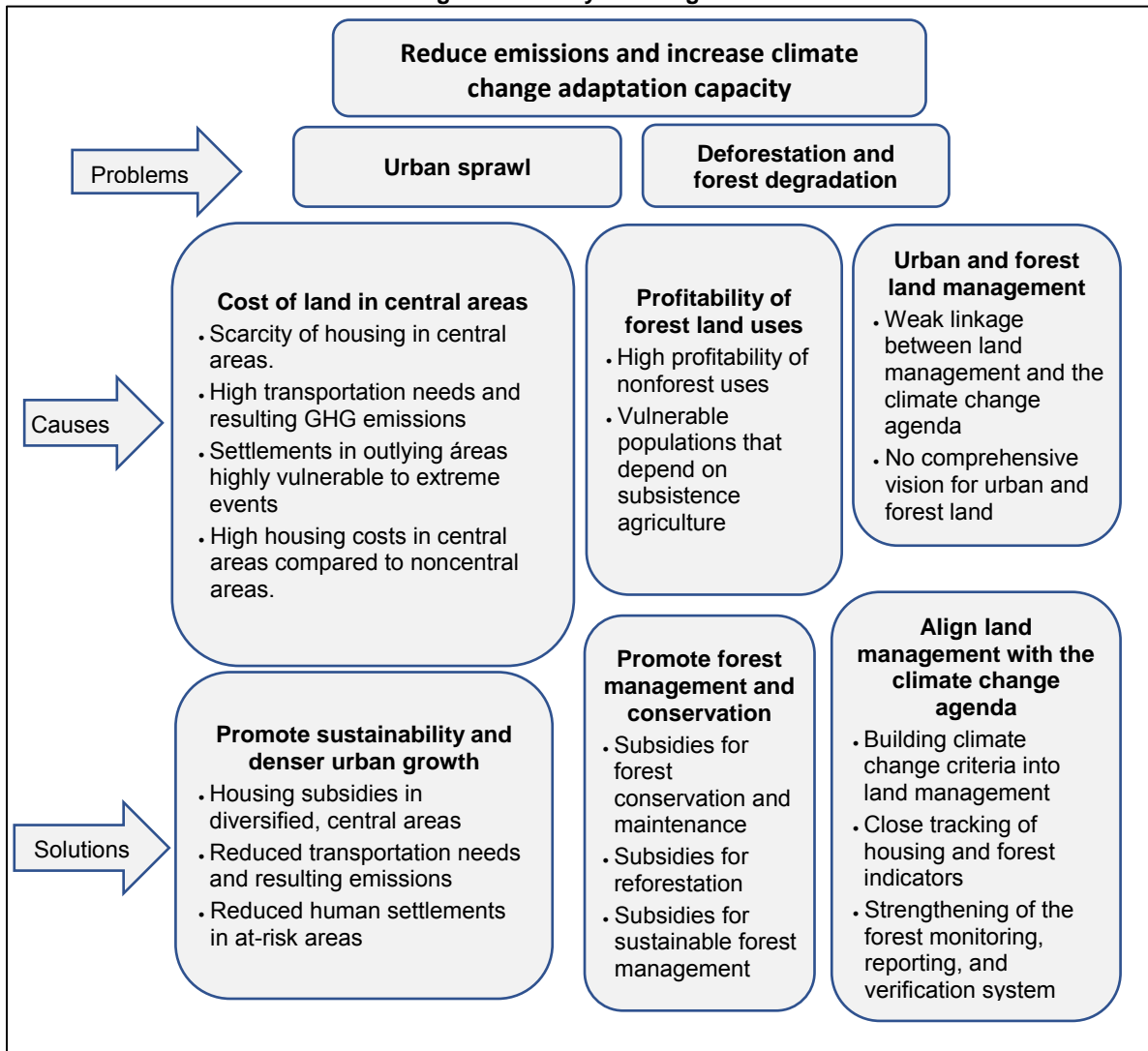
- f. CONAFOR implements the National Forestry Program 2014-2018 (PRONAFOR), which comprises six components, including reforestation and restoration, sustainable forest management, and payment for environmental services (PES). The objective of PRONAFOR is to grant subsidies to owners of forestlands that request them voluntarily. PRONAFOR subsidies address a market failure by internalizing the positive externality derived from the social benefits generated by forest environmental services. These subsidies can complement sustainable management where there is productive potential while, at the same time, compensating landowners for market opportunity costs, such as land-use changes to more profitable private alternatives. The PES program establishes 15 priority criteria in its operating rules to rank proposals. These criteria incorporate a variety of factors, such as the property being located in: (i) protected natural areas; (ii) areas at risk of deforestation (iii) areas with a high percentage of forest coverage; (iv) overexploited aquifers; and (v) watersheds with low water availability; among other sites. This reflects the priority given to areas that are highly important in terms of biodiversity and water services, or at high risk of being converted to other uses (see [required electronic link 4](#)).
- 1.7 Despite progress made in these programs, their continuity and opportunities for improvement are at risk. According to the Institutional Capacity Analysis Platform (ICAP) both for CONAVI and CONAFOR, there is a problem with the design, targeting, implementation, monitoring, and evaluation of the programs and their linkage to the funds allocated in the annual budget. The Federal Expenditure Budget for 2016 included a 37% cut to SEMARNAT's budget, and a 40% cut to the budget for the operation of the forestry sector (Mexican Civil Council for Sustainable Forestry, 2016), while CONAVI's 2017 budget has been slashed by 38.55% from last year (Chamber of Deputies, 2016). These cuts affect the scope and frequency of interagency coordination activities and lessen the likelihood of achieving results in climate change mitigation and adaptation.
 - 1.8 **Theory of change.** From all of this, it can be inferred that, by making the management of actions in the country more comprehensive and aligned with the climate change agenda, the Government of Mexico could potentially have a bigger

⁵ This model is built using numerous sources, such as the National Institute of Statistics and Geography (INEGI), SEDESOL, and the National Population Council, and establishes three urban containment perimeters per city: (i) (U1): Consolidated urban areas with access to employment, equipment, and urban services. They are determined by the "employment potential" variable, defined as the measurement of physical accessibility to jobs for each location within the urban area; (ii) U2: Areas in the process of consolidation with at least 75% coverage of urban water and drainage infrastructure and services; and (iii) U3: Areas contiguous to the urban area in a buffer zone (peripheral ring around the urban area) defined according to the size of the city.

impact on mitigating emissions and building climate change adaptation capacities. This change in management should aim to contain urban sprawl and reverse deforestation and forest degradation, as well as improve coordination among institutions in charge of these policies.

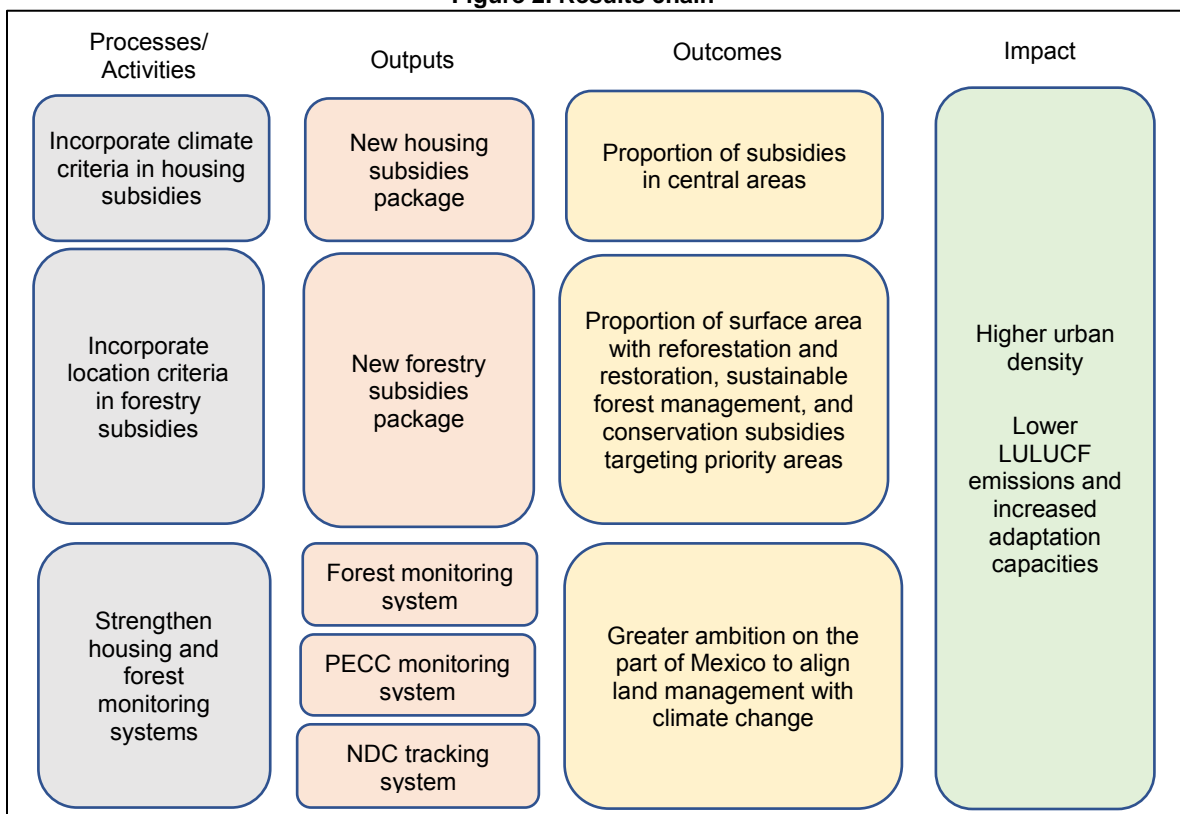
- 1.9 Figure 1 summarizes the theory of change, stating the main problems, their causes, and possible solutions that the program seeks to support.
- 1.10 This theory of change is based on a large body of evidence on the potential of land management. In urban environments, in addition to what was mentioned above (see paragraph 1.4), appropriate densities can provide sufficient localized demand to justify the costs of mass transit (O’Sullivan, 2009), while incentivizing alternative modes of transportation like walking or riding bicycles (UN-Habitat, 2013). Besides reducing the use of cars, greater density also helps lower energy consumption, making it an effective climate change mitigation policy. Glaeser (2009) estimated that, for a sample of 48 metropolitan areas, the average city household generated up to 35% fewer emissions than if it had been located in the suburbs.

Figure 1. Theory of change



- 1.11 In rural environments, the shift to land uses such as farming, ranching, and urban sprawl is responsible for the majority of emissions from land use, land-use change, and forestry (LULUCF) and the rising vulnerability of ecosystems and communities. Addressing the direct and indirect drivers of deforestation requires a complex set of interventions, including: (i) incentives systems that limit land-use changes; (ii) the valuation of forest goods and services; and (iii) the sustainable intensification of agriculture and livestock production. To create these focal points in Mexico, there are opportunities for the collective management of forests by communities and the communal farms known as ejidos. This kind of collective management has been associated with lower deforestation rates (Bray, 2010). PES arrangements, an area in which Mexico has vast experience, can play a part in reducing deforestation to the extent that they are effectively targeted (Drizz et al., 2016).
- 1.12 To reduce emissions and increase adaptation to climate change, land management must be transformed by enhancing location criteria in housing and forest programs and stepping up coordination among these sectors and SEMARNAT. It is assumed that if subsidies associated with these programs are conditioned on the above criteria, better outcomes will be achieved in terms of increasing urban density, reducing energy consumption from transportation, lowering emissions, and building adaptation capacities, as illustrated in Figure 2. Lastly, Mexico faces the challenge of consolidating its institutional monitoring, supervision, and coordination systems to meet the commitments made.

Figure 2. Results chain



- 1.13 **The Bank's experience in Mexico.** Since 2008, Mexico has received support from the IDB to consolidate its long-term climate change agenda. It is currently the Bank's principal beneficiary for projects in this area. This support has allowed for the implementation of technical and financial products (e.g., investment and policy-based loans, and technical cooperation (TC) activities). In the forestry sector, the IDB has supported the country with "Support for Forest-related MSMEs in Ejidos. Implementation of the Forest Investment Program in Mexico" (operation 2930/SX-ME, 2930/SX-ME-1)⁶ and "Financing Low-carbon Strategies in Forest Landscapes" (operation 2838/SX-ME).⁷ In housing, the IDB has supported the Habitat Program with four loans (loans 1583/OC-ME, 1928/OC-ME, 2569/OC-ME, and 3607/OC-ME), the "Housing Finance Program" (operation 1298/OC-ME), "This House is MIA (MINE): New Affordable Housing Models" (operation SP/ES-16-23-ME), and the "ECOCASA' Program" (operations 2896/OC-ME, 2896/OC-ME-1, 2897/TC-ME), among others. The Bank drew lessons from the above projects that are reflected in this program. In the forestry sector, specifically, it has been clear that there is heightened awareness of the support for sustainable forest management and conservation. It is therefore plausible to assume that a loan based on results (LBR) instrument could guide public policy towards areas with greater deforestation risk and hydrologic vulnerability. An important lesson learned in housing is that, while favorable outcomes can be achieved on the supply side through programs like ECOCASA, this does not necessarily reflect the ideal location criteria. The discussion on this issue and specific lesson learned from it have given rise to a demand-based approach, through subsidies, with the goal of making urban containment areas denser as an effective measure in the implementation of the climate change agenda.
- 1.14 **Lessons learned to achieve results under the climate change agenda.** The Bank's support for the climate change agenda has made possible the following:
- a. In the period 2008-2010, programmatic policy-based loan (PBP): Consolidation of the Government of Mexico's institutional and operational capacity to address climate change by strengthening SEMARNAT through the creation of the Office of Climate Change Policies, as well as the Sustainable Project Division within Nacional Financiera, S.N.C. (NAFIN). It is also worth highlighting the support for the incorporation of climate change into all aspects of Mexican public policy with the preparation of the PECC in 2009, and through the development of an information system to monitor the degree to which the targets set in the PECC are met.
 - b. In the period 2010-2016, investment loans (mainly, channeling climate financing from Climate Investment Funds): Through national development and private investment banking, IDB operations have furthered the implementation of financial instruments, such as efficient energy investment bonds, and the development of energy savings insurance for energy efficiency, wind farms, and solar parks. In these last two cases, concessional and technical cooperation financing were provided to NAFIN to address financial and technical barriers to greater investment in these sectors.
- 1.15 **Strategy and rationale of the operation.** The Paris Agreement is a framework for the consistent and accelerated growth of climate financing. According to the World

⁶ See [optional electronic link 5](#).

⁷ See [optional electronic link 6](#).

Bank (2017), this transformation will depend on the capacity of climate financing to support: (i) sound monitoring, delivery of reports, and verification; (ii) strong national institutions to implement policies; (iii) effective incentives for private investment; and (iv) ways to successfully expand mitigation and adaptation efforts (World Bank, 2017). Results-based financing shows strong potential to meet each of these requirements for transitioning to low-carbon development. Mexico has made headway in creating the institutional architecture to drive the climate change agenda and in defining outcomes in this area. One way to garner collaboration is through the financial and technical support of the IDB aimed at helping the Government of Mexico build its capacity to achieve and track these outcomes. A tool for meeting this objective is the new loan based on results (LBR), approved by the Board of Executive Directors in late 2016 (document GN-2869-1). This financial instrument has proven highly useful at other multilateral development banks to support both structural changes and the achievement of results under the climate change agenda ([World Bank, 2017](#)). The LBR is an effective financing instrument to promote the achievement of results in the climate change agenda, since a large part of the agenda consists of fostering changes in the modus operandi of government programs to reduce carbon emissions. In this case, the changes aim to enhance incentives for the inclusion of criteria for targeting land management in housing and forestry programs to locations that can make a greater contribution to the climate change agenda. This is reinforced by support with technical cooperation resources to improve institutional coordination to collect and report information on the country's processes and achievements, as well as the development and implementation of new procedures. This LBR will also help give continuity to the CONAVI and CONAFOR programs, which have been affected by budget cuts in recent years.

- 1.16 **Alignment with the IDB country and sector strategy.** This program is consistent with the Update to the Institutional Strategy 2010-2020 (document AB-3008) and aligned with the challenge of social inclusion and equality, as a large part of its activities are aimed at reducing social and environmental vulnerability through housing solutions and support for reforestation, sustainable management, and conservation. The operation is further aligned with the crosscutting theme of climate change and environmental sustainability, since it is geared towards mitigation and adaptation. One hundred percent of the operation's funds are invested in climate change mitigation and adaptation activities, according to the [joint methodology of multilateral investment banks on estimating climate finance](#). These resources contribute to the IDB Group's goal of increasing the financing of climate change-related projects to 30% of total approvals by the end of 2020. For the same reason, the program is consistent with the Climate Change Sector Framework Document (document GN-2835-3). It also contributes to the Corporate Results Framework 2016-2019 (document GN-2727-6) and to the country development results indicators related to mitigation with support from IDB Group financing and beneficiaries of improved management and sustainable use of natural capital.⁸ The operation is also aligned with the strategic objective of "promoting the orderly, safe, and sustainable growth of cities," in that it seeks to make cities denser. Lastly, it is directly aligned with the strategic objective of the country strategy with Mexico 2013-2018 (document GN-2749) to "support the implementation of national climate change policy fostering adaptation measures taking a long-term approach." This is

⁸ Indicator 11: beneficiaries of improved management and sustainable use of natural capital; and Indicator 12: households benefiting from housing solutions.

because the program involves developing and promoting adaptation measures aimed at integrated watershed management and soil restoration; reduced vulnerability and greater resilience of human settlements; conservation and sustainable use of ecosystems; and the maintenance of environmental services.

- 1.17 **Nonfinancial additionality.** The program will strengthen the inclusion of land management criteria in housing and forest programs by consolidating and improving incentives to target new housing purchase and forestry subsidies to locations that will have a greater impact on the climate change agenda. The program will also improve the technical tools used to identify these locations and the reporting instruments. This LBR will improve SEMARNAT's monitoring capabilities to accomplish the climate change agenda by consolidating CONAFOR PECC reports on forestry subsidies, as well as generate new CONAVI reports on housing location. Lastly, this program will improve the level of coordination among these entities through joint monitoring mechanisms.
- 1.18 **Gender.** Both commissions include gender considerations in their current operating rules. The housing sector promotes the building of inclusive cities by giving preference to victimized women and women heads of household when granting subsidies (CONAVI, 2017). In 2016, 41.3% of subsidies were allocated to women (CONAVI, 2017). In the forestry sector, the 2017 operating rules count women among the target population regarded as a social priority for the selection and allocation of subsidies. In 2016, coverage was achieved for 2,256 women (CENEVAL, 2017). As part of the nonfinancial additionality, this operation will work with institutions to consolidate gender equality incentives and develop indicators to measure them.
- 1.19 This loan presents an opportunity to improve land management to achieve results under the climate change agenda, building on prior IDB actions in sectors facing financial and technical barriers like wind and solar energy. At the same time, this program will generate valuable information to evaluate the impact of land management on climate change by creating historical data and baselines.

B. Objectives, components, and cost

- 1.20 **Program objectives and components.** The objective of this program is to support the Government of Mexico in improving land management to reduce emissions and vulnerability to climate change, through three components.
- 1.21 **Component 1: Land management in the housing sector (US\$434.2 million).** This component seeks to reduce greenhouse gas emissions resulting from the decreasing density of cities. The outcome of this component is a rise in the proportion of housing subsidies targeted in line with the climate change agenda. The LBR will provide CONAVI with input to strengthen an incentives system that rewards the application of subsidies in central areas, to reduce urban sprawl and, thus, contribute to mitigating energy consumption in the transportation sector and greenhouse gas emissions. Over four years, the program will benefit 131,484 families with an average housing subsidy of US\$3,302.⁹
- 1.22 **Component 2: Land management in the forestry sector (US\$165.8 million).** This component seeks to increase the capacity of forests for emissions mitigation and climate change adaptation, while increasing the climate benefits of forestry

⁹ For a detailed description of the program see [required electronic link 4](#).

subsidies, by improving their location. It will cover three activities: (i) restoration; (ii) incorporation of surface area into sustainable forest management systems; and (iii) payment for environmental services (PES). The LBR will assist in improving the results of climate change-related forestry actions by better targeting subsidies on areas with a higher deforestation risk or critical areas for ecosystem services. These areas are determined from PRONAFOR eligibility criteria. The proportions of surface areas supported for the implementation of PES, sustainable management, and reforestation will be taken as outcomes, with a focus on priority areas. These outcomes are directly associated with the reduction of deforestation and vulnerability in priority watersheds and ecosystems.¹⁰ The operation will work through subsidies for conservation, reforestation, and sustainable management on 3.7 million hectares at an average of about US\$44 per hectare.¹¹

- 1.23 **Component 3: Interagency coordination (US\$1 million, with resources from technical cooperation operation ATN/MC-16456-ME, ATN/OC-16457-ME).** This component will strengthen the capabilities of the Government of Mexico to conduct monitoring and land management tied to the climate change agenda, consolidating SEMARNAT's role for monitoring actions and results, while strengthening the technical capabilities of CONAVI and CONAFOR. This component seeks to lay the groundwork for Mexico to make its NDC more ambitious. To achieve this objective, a technical cooperation program is being prepared to finance such activities as: (i) creation of a platform for monitoring and reporting on the PECC lines of action; (ii) strengthening of interagency coordination for PECC monitoring; (iii) consulting services or firm to verify the project outcomes; and (iv) assurance review of project financial information.

C. Key results indicators and beneficiaries

- 1.24 The impacts of the program relate to: (i) Greater urban density measured by a larger number of dwellings in diversified central areas and their impact on the mitigation of emissions; and (ii) LULUCF emissions in the country. The outcomes are a larger proportion of housing and forestry subsidies targeting priority areas and the submission by Mexico of a more ambitious NDC to the United Nations Framework Commission on Climate Change (UNFCCC) (see Annex II).
- 1.25 The outcome indicators to be used for disbursements are: (i) the proportion of subsidies for new housing targeted in line with the climate change agenda; (ii) the proportion of surface area supported by subsidies for restoration and reforestation targeting priority areas for adaptation; (iii) the proportion of surface area supported by sustainable forest management subsidies targeting reactivation areas of the National Strategy for Sustainable Forest Management to Increase Production and Productivity (ENAIPROS) 2013-2018; and (iv) the proportion of surface area incorporated into PES conservation arrangements located in high-priority areas to stop deforestation and reduce vulnerability.
- 1.26 **Beneficiaries.** The main direct beneficiaries of the program will be those individuals that access subsidies for new housing in selected areas, and those benefited by reforestation and restoration in priority areas, the incorporation of active forest

¹⁰ CONAFOR determines the methodologies for activities financed under PRONAFOR (restoration, sustainable forest management, and PES) in the technical annexes of its operating rules ([CONAFOR 2016](#)).

¹¹ See footnote 9.

management, and areas covered by conservation arrangements. Furthermore, as improved land management will allow for reduced emissions and vulnerability to climate change, the whole population can be said to benefit indirectly.

- 1.27 **Economic evaluation.** The projected is estimated to yield a reasonable economic and social return. The net present value of the project would be US\$27.1 million (calculated at a 12% discount rate). Benefits were estimated using: (i) the estimated monetary value for each ton of CO₂ removed as a result of reforestation actions; and (ii) the capital gains from housing built in central areas of cities. The project still maintains a positive net present value in pessimistic scenarios due to a lower-than-expected performance or exogenous factors that result in a lower number of effectively reforested hectares or financed housing (see [optional electronic link 2](#)).

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instruments

- 2.1 The financing instrument is a loan based on results (LBR) from the Bank's Ordinary Capital, for a total of US\$600 million. The dimensioning of the operation is based on: (i) the need to cover a four-year period (see paragraph 2.2); and (ii) the annual amount required to achieve the expected outcomes. The program is linked to technical cooperation operation ME-T1361 (ATN/OC-16456-ME, ATN/OC-16457-ME), which was approved to support the institutional arrangements envisaged in Component 3 for institution-strengthening and monitoring of actions and outcomes. The budget by component is given in Table 1.

Table 1. Cost by component (US\$ millions)

Component	Loan		Technical cooperation*	
	Amount	Percentage	Amount	Percentage
Component 1. Land management in the housing sector	434.20	72.40%		
Component 2. Land management in the forestry sector	165.80	27.60%		
Component 3. Interagency coordination			0.80	80
Program administration			0.20	20
Total	600.00	100	1.00	100

* Operation ME-T1361 (ATN/OC-16456-ME, ATN/OC-16457-ME) approved on 2 November 2017.

- 2.2 The transition to a low-carbon, climate change-resilient economy will pass through a new phase over the next few years. At the national level, the current Special Climate Change Program (PECC) is ending; there will be a changeover to a new administration, and the new administration will prepare the new PECC according to national priorities to be determined. At the international level, the first exercise of the global stocktake under the Paris Agreement will occur, as will the first biennial reporting cycle within the transparency framework. In light of these changes, the Bank proposes a four-year disbursement period for this operation. This time frame will help to ensure that the outcomes are achieved despite the risks entailed by these transitions, and that the outcomes provide feedback enrich these processes (see Table 2).

Table 2. Disbursement schedule (US\$ millions)

Component	Year 1	Year 2	Year 3	Year 4	Total
Loan					
Component 1 (housing sector)	127.60	85.50	124.30	96.80	434.20
Component 2 (forestry sector)	42.80	43.60	44.50	34.90	165.80
TOTAL	170.40	129.10	168.80	131.70	600.00
Percentage by year	28.40	21.52	28.12	21.96	100.00
Technical cooperation operation ME-T1361 (ATN/OC-16456-ME, ATN/OC-16457-ME)					
Component 3 (coordination)	0.40	0.40	0.00	0.00	0.80
Program administration	0.05	0.05	0.05	0.05	0.20
TOTAL	0.45	0.45	0.05	0.05	1.00
Percentage per year	45	45	5	5	100

- 2.3 The operation meets the requirements provided for an LBR (document GN-2869-1) since: (i) it supports the climate change agenda in the delivery of results by CONAFOR and CONAVI; (ii) it promotes good practices for management, such as improving interagency coordination and the sector stewardship of SEMARNAT; (iii) it promotes the alignment of existing government programs for the purchase of housing under CONAVI, as well as reforestation and conservation programs implemented by CONAFOR, to the climate change agenda with the resulting mitigation of emissions; and (iv) the institutional capacity analysis of SEMARNAT and the implementing agencies shows that they possess adequate legal authority, governance capacity, and institutional environments, along with sufficient management and technical capacity, to administer and monitor an LBR.¹² The evaluation of its procurement and financial management systems found that they are compatible with established principles and good practices in this area. Thus, there are systems in place to ensure the appropriate use of loan proceeds and reliable monitoring on the outcome indicators, including the targets for each indicator.

B. Environmental and social safeguard risks

- 2.4 According to Directive B.13 of the Bank's Environment and Safeguards Compliance Policy (document GN-2208-20 and Operational Policy OP703), no environmental impact classification is required. In keeping with procedures for processing LBRs, no activities classified as category "A" under the IDB's Environment and Safeguards Compliance Policy (Operational Policy OP703) will be financed. The possible environmental and social impacts, and the risks associated with the program, as described in the environmental and social management report (see [required electronic link 3](#)), were rated as low. As disbursements will be made after the project's outcomes have been achieved, the activities to achieve these outcomes will be implemented using the borrower's country environmental and social safeguards systems. In line with Directive B.16 of Operational Policy OP-703, an equivalency and acceptability analysis was carried out on the national systems based on IDB environmental and social safeguards during the preparation process, which concluded that the country systems applicable to project activities are equivalent and acceptable to the Bank.

¹² These capacities will be further strengthened with the resources and activities provided in the technical cooperation operation associated with this LBR.

C. Fiduciary risks

- 2.5 An institutional assessment of SEMARNAT and the implementing agencies was carried out using the Institutional Capacity Analysis Platform and Project Risk Management tool. These assessments concluded that the project's fiduciary risk is low (see [optional electronic link 3](#) and Annex III for more information).

D. Other project risks

- 2.6 In addition to the environmental and fiduciary risks, the risk analysis detected three medium-level risks, which are presented in Table 3 with their respective mitigation measures.

Table 3. Project risks

Type of risk	Risk	Mitigation activities
Public administration and governance	Inadequate interagency coordination among government entities involved, resulting in delays in reporting outcomes.	Preparing the program's Operational Guidelines. Presenting the operation, its objectives, and timeframes in the PECC Working Group and the Finance Working Group of the CICC as an agenda item.
	Change in the authorities involved in meeting PECC commitments.	Ensuring that Operational Guidelines are current and in operation. Hiring consultants to support SEMARNAT for the sake of continuity. Providing documentation and justification for the project based on the national priorities, according to the NDC (noting that the Paris Agreement, as a binding instrument, and the NDC contain Mexico's commitments to address climate change, so this project is related to the international commitments undertaken by Mexico).
Monitoring and accountability	The verification of results finds errors or inconsistencies.	Terms of reference of the quality verification firm. Strengthening SEMARNAT for efficient monitoring. Reaching an agreement among stakeholders as to the type of information to be reviewed/validated by the verification entity.

III. IMPLEMENTATION AND MANAGEMENT PLAN

A. Summary of implementation arrangements

- 3.1 **Borrower and executing agency.** The borrower will be Mexico, acting through the Department of Finance and Public Credit (SHCP). SEMARNAT will be the executing agency responsible for program implementation with the participation of CONAFOR and CONAVI as the implementing agencies of priority climate change actions. NAFIN, designated by the SHCP, will act as financial agent of the borrower for the administration and monitoring of fulfillment of the contractual commitments established in the loan contract.
- 3.2 **Execution mechanism.** SEMARNAT will be responsible for coordinating with the implementing agencies. In keeping with the existing procedure, SEMARNAT will

receive a six-monthly progress report on the achievement of planned outcomes from each of the implementing agencies and will record those outcomes in its monitoring system. To reinforce SEMARNAT's coordination capacity, it will be supported by technical assistance provided under technical cooperation operation ME-T1361 (ATN/OC-16456-ME, ATN/OC-16457-ME), whose objectives include strengthening SEMARNAT's monitoring systems and their coordination with those used by CONAFOR and CONAVI (see paragraph 1.23).

- 3.3 **Verification of results.** Verification of results for the purpose of disbursements will be conducted by an independent, specialized firm acting as an external evaluator of the achievement of results. The independent verification entity will deliver a results verification report to SEMARNAT prior to each disbursement request. The verification of the achievement of results will focus on two objectives: (i) issuing an opinion as to the accuracy, reliability, validity, and consistency of the information corresponding to the results; and (ii) determining the value of the outcome indicators established in each execution report. The firm will be engaged by the Bank according to the terms of reference previously agreed upon with SEMARNAT with the no objection of CONAFOR and CONAVI, and in compliance with the IDB policies for the selection and contracting of consultants. The terms of reference will explicitly state that the evaluation is a process to support the executing and implementing agencies throughout the execution of their commitments, so that prior to their verifications it can help review progress and provide recommendations, in order to address potential errors and inconsistencies in the results information in advance. This contract will be financed with resources from operational support technical cooperation operation ME-T1361 (ATN/OC-16456-ME, ATN/OC-16457-ME), to be executed by the Bank.
- 3.4 **Disbursement mechanism.** Upon verification by the independent verification firm (see paragraphs 3.2 and 3.3) that the results identified in the program Results Matrix have been achieved, SEMARNAT, through NAFIN, will submit the appropriate disbursement request to the IDB. The amount of the request will be proportional to the results achieved and independently verified. If the borrower requests retroactive financing of results achieved, such financing may not exceed 15% of the loan proceeds, as explained below in paragraph 3.6.
- 3.5 **Program Operational Guidelines.** The Operational Guidelines will describe the operation's strategy and execution conditions, including: (i) the project's organizational plan and the involvement of the implementing agencies of priority climate change actions and the financial agent; (ii) the technical and operational arrangements for its execution; (iii) the programming, monitoring, and results evaluation mechanism; (iv) LBR operational guidelines; (v) the detailed description of the outcome indicators, especially of those tied to disbursements; and (vi) the prevention and reporting mechanisms for integrity required by the IDB's Office of Institutional Integrity.
- 3.6 **Retroactive financing.** The IDB will recognize the financing of outcomes previously achieved (retroactive financing) as stated in document GN-2869-1, up to the equivalent of 15% of the total loan amount, for outcomes achieved from 2 October 2017 (project profile approval date) until eligibility date of the loan, provided that the development results achieved are included in the Results Matrix. This request is justified because the operation is part of a national program that has been financing actions to improve land management for the reduction of emissions and climate

change. The verification of such previously achieved outcomes will be performed as part of the first independent verification.

- 3.7 **Procurement execution.** Procurements will follow the procedures of the procurement system used by the executing agency or implementing agencies. See Annex III for more information.
- 3.8 **Financial management.** Project disbursements and external audits of project financial information will be conducted according to the agreements established in Annex III.
- 3.9 **As special contractual conditions precedent to the first disbursement of the loan proceeds: the borrower, acting through the executing agency, will provide evidence of the following to the Bank: (i) the entry into force of the program Operational Guidelines;¹³ and (ii) the signature of the project mandate and execution agreement between the borrower, the executing agency, and Nacional Financiera (NAFIN), as the financial agent for the loan, since the Government of Mexico has expressly requested this as a condition precedent to disbursement.**
- 3.10 Prior to any disbursement of the loan proceeds, the Bank will engage an independent firm or consulting services to verify the program outcomes, under the terms of reference previously agreed upon with SEMARNAT, so that an effective mechanism is in place to verify the outcomes achieved during program execution, as required by the LBR policy.

B. Summary of arrangements for monitoring results

- 3.11 **Monitoring arrangements.** The program will adopt IDB supervision mechanisms. The monitoring strategy for the program will include: (i) defining protocols for external verification of the achievement of disbursement indicators; (ii) holding at least two meetings per year (tentatively in April and October) for a technical and operational review of the program's progress, solutions to problems, and risk mitigation (including an update to the risk analysis that will be made in the last meeting of each year). Relevant institutional actors and the IDB will participate in these meetings and then duly disseminate the management agreements reached; (iii) generating six-monthly progress and planning reports, including results achieved and problems encountered in each of the components, and tracking program performance against the Results Matrix, at least, as of the second year that the program is in effect; and (iv) using the management tools mentioned in the Monitoring and Evaluation Plan ([required electronic link 2](#)) and agreed upon at the launch workshop. These tools will allow for the planning of activities and processes to achieve the physical outputs and intermediate and final outcomes.
- 3.12 **Arrangements for evaluation of results.** Given the features of an LBR, where disbursements are associated with results achieved, the program will rely on performance reports verified through an independent, external firm. These six-monthly reports will be used to confirm that commitments have been fulfilled, and targets met. The verification firm will also be asked to perform a final evaluation that includes an ex post economic analysis.

¹³ If SEMARNAT and the Bank agree on the Operational Guidelines prior to signature of the loan contract, this condition may be removed from the signature copy of the loan contract.

- 3.13 The final evaluation will attempt to verify whether the Results Matrix indicators have been achieved, and which targets were exceeded or not met. If not met, the reasons will be examined, and lessons learned specified that could be useful for future projects. At the same time, the ex post economic analysis will be performed once the last loan disbursement has been made, using the same methodology employed in the ex ante analysis. It will seek to verify the economic viability of the project. Both documents will be important for the preparation of the project completion report.

Development Effectiveness Matrix		
Summary		
I. Corporate and Country Priorities		
1. IDB Development Objectives	Yes	
Development Challenges & Cross-cutting Themes	-Social Inclusion and Equality -Climate Change and Environmental Sustainability	
Country Development Results Indicators	-Beneficiaries of improved management and sustainable use of natural capital (#)* -Households benefitting from housing solutions (#)*	
2. Country Development Objectives	Yes	
Country Strategy Results Matrix	GN-2749	i) Promote the orderly, safe, and sustainable growth of cities, and ii) Support the implementation of national climate change policy mechanisms fostering adaptation measures taking a long-term approach.
Country Program Results Matrix		The intervention is not included in the 2017 Operational Program.
Relevance of this project to country development challenges (If not aligned to country strategy or country program)		
II. Development Outcomes - Evaluability	Evaluable	
3. Evidence-based Assessment & Solution	6.6	
3.1 Program Diagnosis	2.4	
3.2 Proposed Interventions or Solutions	2.4	
3.3 Results Matrix Quality	1.8	
4. Ex ante Economic Analysis	7.0	
4.1 The program has an ERR/NPV, a Cost-Effectiveness Analysis or a General Economic Analysis	4.0	
4.2 Identified and Quantified Benefits	1.5	
4.3 Identified and Quantified Costs	1.5	
4.4 Reasonable Assumptions	0.0	
4.5 Sensitivity Analysis	0.0	
5. Monitoring and Evaluation	7.5	
5.1 Monitoring Mechanisms	2.5	
5.2 Evaluation Plan	5.0	
III. Risks & Mitigation Monitoring Matrix		
Overall risks rate = magnitude of risks*likelihood	Medium	
Identified risks have been rated for magnitude and likelihood	Yes	
Mitigation measures have been identified for major risks	Yes	
Mitigation measures have indicators for tracking their implementation		
Environmental & social risk classification	B.13	
IV. IDB's Role - Additionality		
The project relies on the use of country systems		
Fiduciary (VPC/FMP Criteria)	Yes	Financial Management: Budget, Treasury, Accounting and Reporting, Internal Audit. Procurement: Price Comparison, Contracting Individual Consultant, National Public Bidding.
Non-Fiduciary		
The IDB's involvement promotes additional improvements of the intended beneficiaries and/or public sector entity in the following dimensions:		
Gender Equality		
Labor		
Environment		
Additional (to project preparation) technical assistance was provided to the public sector entity prior to approval to increase the likelihood of success of the project	Yes	Technical Cooperation ME-T1361 is being processed to support the execution of component 3 and strengthen the institutional capabilities of SEMANART, CONAVI and CONAFOR.
The ex-post impact evaluation of the project will produce evidence to close knowledge gaps in the sector that were identified in the project document and/or in the evaluation plan		

Note: (*) Indicates contribution to the corresponding CRF's Country Development Results Indicator.

The objective of this Results-Based Loan (LBR) is to support the Government of Mexico in the improvement of territorial management for the reduction of emissions and vulnerability to Climate Change (CC). To achieve this objective, the project will implement three components: 1) Territorial management in the housing sector; 2) Territorial management in the forestry sector; and 3) Inter-institutional coordination.

The documentation provides a good diagnosis of the problems and weaknesses that the country faces in terms of territorial management linked to CC, including institutional weaknesses on the part of the Secretary of the Environment and Natural Resources (SEMARNAT), who coordinates the design and execution of the national CC policy based on the National CC Strategy.

The LBR focuses on supporting two of the sectors that affect greenhouse gas (GHG) emissions in the country: housing and forestry. The objective is to improve the targeting of these two sectors towards areas of higher priority, which will be done with the participation of the National Forestry Commission (CONAFOR), and the National Housing Commission (CONAVI), who will be the agencies that implement these priority actions on CC.

The solution proposed by the LBR is in line with the problems identified. The results matrix (RM) reflects the objectives of the program and shows an appropriate vertical logic, although there are some indicators that can be added to better close the vertical logic. One of the two top-level indicators reflects the goals agreed upon to fulfill Mexico's commitments to the Paris Agreement. The outcome indicators reflect expected changes in terms of better targeting by the two supported sectors. The indicators linked to disbursement (ILD) include the necessary means for their verification; the documentation indicates that a consultancy will be hired for the external verification of these results. The lower level indicators reflect the design of each component. The RM includes SMART indicators at the level of impacts, results, and products with their respective baseline values, targets, and means to collect the information. However, there are some results and product indicators that can be improved, since they are not SMART. Empirical evidence is cited on the effectiveness of similar interventions similar supported by the forestry sector, however, although the references cited for the housing sector are informative, it is unclear if they are for interventions similar to those supported by the LBR.

The economic analysis is based on a cost-benefit analysis (CBA). In general, the benefits and costs are well identified, although the assumptions are not always well supported. The CBA yields a IRR of 14%. Sensitivity analyses are performed according to possible changes in the values of two important variables. The minimum values for these variables are identified so that the IRR is equal to 12%; the results are reasonable given the assumptions used.

The monitoring and evaluation plan proposes an evaluation using two methods: 1) ex post cost-benefit analysis; and 2) reflexive evaluation for the results indicators. The reflexive evaluation will provide important information, since it will be possible to see if the LBR triggered a greater targeting in the two sectors relative to the baseline.

The risks identified in the risk matrix seem reasonable. The risks include mitigation actions and compliance indicators, although this is only for the three risks classified as Medium Risk, and not for the four risks classified as Low Level.

RESULTS MATRIX

Project objective:	To support the Government of Mexico in improving land management to reduce emissions and vulnerability to climate change.
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EXPECTED IMPACT¹

Indicator	Unit of measure	Baseline value	Base year	2018	2019	2020	2021	End of project	Means of verification	Baseline comments	Definition/estimation methodology
Outcome 1: Greater urban density											
Impact 1: More urban dwellings in central areas	Percentage of new dwellings registered within central perimeters	32.3	2017	32.9	33.5	34.1	34.7	34.7	Housing registry in the National Housing Information and Indicators System (SNIIV)	The baseline corresponds to the months from January to July 2017.	This indicator represents the proportion of dwellings registered in perimeters U1 and U2, in relation to the total number of dwellings registered in the SNIIV.
Outcome 2: Lower emissions from deforestation and forest degradation											
Impact 2: LULUCF emissions	MtCO ₂ e/year	26.6	2013	N/A	N/A	N/A	N/A	23.9	Biennial update reports (BURs) and National Communications	[a]	The definitions and methodologies used for this indicator correspond to those of the National Monitoring, Reporting, and Verification System (SNMRV) for the LULUCF sector, operated by CONAFOR.

^a Notes for Impact indicator 2:

Greenhouse gas emissions from gross deforestation and forest degradation refers to the sum of annual GHG emissions from gross deforestation, defined as conversions from forest land to other uses (grassland, cropland, settlements, and other land), and annual GHG emissions from forest degradation, consistent with the National Inventory of Greenhouse Gas Emissions for the Land Use, Land Use Change, and Forestry sector of the First Biennial Update Report to the United Nations Framework Convention on Climate Change (INECC and SEMARNAT, 2015). The National Inventory of Emissions of Greenhouse Gases and Compounds (INEGyCEI)-LULUCF for the BUR was prepared by CONAFOR and INECC using the National of Monitoring, Reporting, and Verification System for the LULUCF sector.

The indicator is expressed in megatons of carbon dioxide equivalent per year (MtCO₂e/year)

The baseline corresponds to the evaluation of the indicator for 2013, according to the INEGEI-LULUCF of the BUR, as follows:

GHG emissions from gross deforestation: 24.8 MtCO₂e/year

GHG emissions from forest degradation: 1.8 MtCO₂e/year

Baseline (2013): 26.6 MtCO₂e/year

The baseline will be updated based on information from the Sixth National Communication to the UNFCCC, which includes the INEGyCEI for the LULUCF sector, with the update of the historical period for 1990-2015. This INEGyCEI-LULUCF presents substantial improvements with respect to all previous inventories, including the uncertainties associated with the estimates of GHG emissions and absorptions.

The evaluation of the indicator target must be consistent with the National Communications and/or BURs, as well as with the methodologies of the National Monitoring, Reporting, and Verification System.

¹ The Results Matrix has been prepared assuming an exchange rate of 19.0 Mexican pesos = US\$1. The outputs and outcomes tables show the values in the year that they are measured and reported (and, where applicable, verified). Two semiannual output and outcome reports are expected per year: the first one in March, with the outcomes obtained in the second half of the previous year, and the second one in September, with the outcomes obtained in the first half of the year in course. For the first year (2018), the first report will contain (for the disbursement indicators) the outcomes obtained between 2 October 2017 (date of approval of the project profile) and the RBL eligibility date.

The target is a 10% emission reduction by the end of the project. This target is equivalent to the targets set for similar initiatives, such as the Forests and Climate Change Project. The NDC target of -14 MtCO₂e/year by 2030 refers to the entire LULUCF sector, which includes emissions from the six main categories established by the Intergovernmental Panel on Climate Change (IPCC) (forest land, cropland, grassland or pasture, wetlands, settlements, and other land). Interactions among these six categories include conversions such as "grasslands to agriculture" or "perennial agriculture to settlements," which are outside the public policy purview of CONAFOR and the scope of the project. The NDC targets for the LULUCF sector are being reviewed by CONAFOR and INECC. The results of that review could impact the target stated here. The baseline figures presented here are methodologically consistent with the Forest Reference Emission Level (FREL) for Mexico (submitted to the UNFCCC in 2014 and evaluated by UNFCCC experts in 2015). The FREL evaluated only includes gross deforestation activity. The FREL is a historical average for 2000-2010 equivalent to 44.38862 MtCO₂e/year. As a reference, the gross deforestation emissions included in the FREL for 2010 is 27.28675 MtCO₂e/year. The value of the indicator to assess compliance with the target will be obtained using the National Monitoring, Reporting, and Verification System, and must be consistent with the National Communications, with the BURs and, where appropriate, with their Technical Annexes (REDD+ National Reports). Trend analysis approaches or other statistical modeling approaches may be used. The IDB nonreimbursable technical cooperation resources will be used, in part, to strengthen the National Monitoring, Reporting, and Verification System, including consulting services to assess compliance with the target.

EXPECTED OUTCOMES

Indicator	Unit of measure	Baseline value	Base year	2018	2019	2020	2021	Total EOP	Means of verification	Disbursement indicator (yes/no)	Observations
Outcome 1: Greater urban density											
Outcome 1a: Proportion of subsidies for new housing targeted in line with the climate change agenda	%	29.7	2017	30.2	30.8	31.4	31.9	31.9	Master Housing Registry	Yes	
Outcome 2: Lower emissions from deforestation and forest degradation											
Outcome 2a: Proportion of restored surface area targeting priority areas for adaptation	%	50.0	2017	50.5	51.5	52.5	53.5	53.5	Information provided by CONAFOR, including: - Basic information on subsidies related to the surface area and its geographic location. - The conclusion of works will be verified through work completion certificates found in the CONAFOR archives. - The eligibility of subsidies for the calculation of the indicator will be determined by overlaying the coverage of subsidy location (also found in CONAFOR's records on each request) and the geographic layer corresponding to priority criteria 1, "Restoration Priority," categories 1 and 2 (see p. 60 of CONAFOR , 2016, Operating Rules, 2017, http://bit.ly/PRONAFOR17).	Yes	Baseline information on the CONAFOR subsidies website (http://bit.ly/ApConafor), assuming that 50% of the supported area meets the targeting criteria.

Indicator	Unit of measure	Baseline value	Base year	2018	2019	2020	2021	Total EOP	Means of verification	Disbursement indicator (yes/no)	Observations
Outcome 2b1: Proportion of surface area incorporated into a sustainable forest management system targeting ENAIROS reactivation areas	%	67.0			69.0	70.4	71.7	71.7	Information provided by CONAFOR, which will include the lists of allocations by the State Technical Committees and the vector files for the supports. The list provided by CONAFOR will contain an identifier that specifies whether or not the support is located in reactivation areas. The lists of beneficiaries are published on the website of the institution.	Yes	The baseline calculation is based on the allocation as of end-September 2017 and corresponds to the reports of the matrix of outcome indicators reported to the Application Portal of the Department of Finance (PASH).
Outcome 2b2: Proportion of surface area with support for sustainable forest certification targeting ENAIROS reactivation areas	%	90.0	2017	90.9	92.7	94.5	96.3	96.3		Yes	The baseline calculation is based on the allocation as of end-September 2017.
Outcome 2b3: Proportion of surface area with forest cultivation and habitat improvement practices targeting ENAIROS reactivation areas	%	77.0	2017	77.8	79.3	80.9	82.4	82.4		Yes	The baseline calculation is based on the allocation as of end-September 2017 and corresponds to the reports of the matrix of outcome indicators reported to the PASH.

Indicator	Unit of measure	Baseline value	Base year	2018	2019	2020	2021	Total EOP	Means of verification	Disbursement indicator (yes/no)	Observations
Outcome 2c: Proportion of surface area incorporated into a PES system targeting high-priority areas to stop deforestation and reduce vulnerability	%	93.0	2017	94.9	96.7	98.6	100.0	100.0	Information provided by CONAFOR, including: - Basic information on subsidies related to the surface area and its geographic location. - CONAFOR archives contain information on the agreements. - The eligibility of subsidies for the calculation of the indicator will be determined by overlaying the coverage of subsidy location (also found in CONAFOR's records on each request) and the geographic layer corresponding to priority criteria 1, "Restoration Priority," categories 1 and 2 (see pp. 86 and 94 of CONAFOR , 2016, Operating Rules, 2017, http://bit.ly/PRONAFOR17).	Yes	Subsidies are given for a period of five years as of the date on which the surface area is incorporated. The indicator only measures the additional surface, so there is no overlap between consecutive years.
Outcome 3: Strengthened capabilities of the Government of Mexico to conduct monitoring and effective land management tied to the climate change agenda											
Outcome 3a: Submission by Mexico of a more ambitious NDC	Binary indicator	No	2017	No	No	No	Yes	Yes	UNFCCC NDC Registry (http://bit.ly/NDCregistry)	No	

OUTPUTS

Outputs	Unit of measure	Baseline value	Base year	2018	2019	2020	2021	Total EOP	Means of verification	Observations
Outcome 1: Greater urban density										
Output 1a: Number of subsidies for new housing targeted in line with the climate change agenda	Dwellings	35,631	2017	38,642	25,889	37,629	29,324	131,484	Master Housing Registry	
Output 1b: Number of households benefited by housing solutions	Number of households benefited	35,631	2017	38,642	25,889	37,629	29,324	131,484	Master Housing Registry	
Outcome 2: Lower emissions from deforestation and forest degradation										
Output 2a: Restored surface area in priority areas for adaptation	Thousands of hectares	47.87	2017	48.35	49.31	50.27	51.22	199.15	Information provided by CONAFOR, including: - Basic information on subsidies related to the surface area and its geographic location. - The conclusion of works will be verified through work completion certificates found in CONAFOR archives. - The eligibility of subsidies for the calculation of the indicator will be determined by overlaying the coverage of subsidy location (also found in CONAFOR's records on each request) and the geographic layer corresponding to priority criteria 1, "Restoration Priority," categories 1 and 2 (see p. 60 of CONAFOR, 2016, Operating Rules, 2017, http://bit.ly/PRONAFOR17).	Baseline information on the CONAFOR subsidies website (http://bit.ly/ApConafor), assuming that 50% of the supported area meets the targeting criteria.
Output 2b1: Surface area incorporated into a sustainable forest management system targeting ENAIROS reactivation areas	Thousands of hectares	234.50	2017	236.85	241.54	246.23	250.92	975.52	Information provided by CONAFOR, which will include the lists of allocations by the State Technical Committees and the vector files for the supports. The list provided by CONAFOR will contain an identifier that specifies whether or not the support is located in reactivation areas. The lists of beneficiaries are published on the website of the institution.	The baseline calculation is based on the allocation as of end-September 2017 and corresponds to the reports of the matrix of outcome indicators reported to the Application Portal of the Department of Finance (PASH).

Outputs	Unit of measure	Baseline value	Base year	2018	2019	2020	2021	Total EOP	Means of verification	Observations
Output 2b2: Surface area with support for sustainable forest certification targeting ENAIROS reactivation areas	Thousands of hectares	225.00	2017	227.25	231.75	236.25	240.75	936.00		The baseline calculation is based on the allocation as of end-September 2017.
Output 2b3: Surface area with support for forest cultivation and habitat improvement practices targeting ENAIROS reactivation areas	Thousands of hectares	123.20	2017	124.43	126.90	129.36	131.82	512.51		The baseline calculation is based on the allocation as of end-September 2017 and corresponds to the reports of the matrix of outcome indicators reported to the PASH.
Output 2c: Surface area incorporated into conservation systems (PES) located in high-priority areas to put a stop to deforestation and reduce vulnerability	Thousands of hectares	291.90	2017	298	304	309	193	1,104	Information provided by CONAFOR, including: - Basic information on subsidies related to the surface area and its geographic location. - CONAFOR archives contain information on the agreements. - The eligibility of subsidies for the calculation of the indicator will be determined by overlaying the coverage of subsidy location (also found in CONAFOR's records on each request) and the geographic layer corresponding to priority criteria 1, "Restoration Priority," categories 1 and 2 (see pp. 86 and 94 of CONAFOR , 2016, Operating Rules, 2017, http://bit.ly/PRONAFOR17).	Subsidies are given for a period of five years as of the date on which the surface area is incorporated. The indicator only measures the additional surface, so there is no overlap between consecutive years.

Outputs	Unit of measure	Baseline value	Base year	2018	2019	2020	2021	Total EOP	Means of verification	Observations
Output 2d: Beneficiaries of improved management and sustainable use of natural capital	Number of beneficiaries	11,089	2017	11,215	11,437	11,659	11,239	45,550	CONAFOR report on the characteristics of the beneficiaries of reforestation and restoration, sustainable management, and PES programs, taking into account the eligibility criteria of each one of these programs for the purpose of this loan.	The baseline represents the allocated subsidies (including individual and collective beneficiaries), assuming that they are all individual, multiplied by an average family size of 3.7 people (the national average, according to the 2016 National Household Survey). The report will specify whether the subsidies are individual or collective, whether the beneficiaries are members of indigenous groups, and the proportion of men and women.
Outcome 3: Strengthened capabilities of the Government of Mexico to conduct monitoring and effective land management tied to the climate change agenda										
Output 3a: Strengthened National System for the Monitoring, Reporting, and Verification of Forestry Sector Greenhouse Gas Emissions and Absorption	%	0%	2017	40%	70%	100%	100%	100%	CONAFOR report ^[a]	
Output 3b: PECC monitoring system	Binary indicator	No	2017	Yes	Yes	Yes	Yes	Yes	Online system	
Output 3c: Monitoring System for the NDC Implementation Plan	Binary indicator	No	2017	No	No	Yes	Yes	Yes	Online system	

Outputs	Unit of measure	Baseline value	Base year	2018	2019	2020	2021	Total EOP	Means of verification	Observations
Output 3d: Methodology for assessing impacts on climate change derived from housing subsidies in diversified, central urban areas	Binary indicator	No	2017	No	No	Yes	Yes	Yes	Published methodology	

^a Additional notes for Output 3a.

Indicator values	Means of verification
40%: The National Monitoring, Reporting, and Verification System (SNMRV) has cartography with better spatial and temporal resolution to obtain the activity data in a coherent manner and with greater adherence to the principles of accuracy and completeness. (Expected compliance date: end-2020)	High spatial resolution maps of changes in forest coverage with a periodicity of at least two years, with national coverage and appropriate thematic resolution for reports according to the IPCC 2006 Guidelines.
20%: The SNMRV improves the estimates of GHG flows for the five basic reservoirs of the IPCC. (Expected compliance date: end-2020)	Technical documentation with protocols for estimating GHG flows for the five basic reservoirs of the IPCC
15%: The SNMRV has a methodological enhancement for estimating GHG emissions by REDD+ activities. (Expected compliance date: end-2020)	Technical documentation with protocols on methodological enhancements for estimating GHG emissions by REDD+ activities (with emphasis on forest degradation).
10%: The SNMRV has a mechanism for methodological alignment between the subnational and national levels, and improves its reports at the state level. (Expected compliance date: end-2020)	Methodological alignment model for GHG accounting between the national and subnational levels. Reports with improved state-level GHG inventories.
15%: The SNMRV has coherent tools in its modeling component (deforestation risks, mitigation scenarios, etc.) (Expected compliance date: end-2020)	Technical report on outcomes of the SNMRV modeling component.

FIDUCIARY AGREEMENTS AND REQUIREMENTS

Country:	Mexico
Project number:	ME-L1268
Project name:	Land Management to Achieve Results under the Climate Change Agenda
Executing agency:	Department of Environment and Natural Resources (SEMARNAT), with the participation of the National Forestry Commission (CONAFOR) and the National Housing Commission (CONAVI) as the implementing agencies of climate change actions
Fiduciary team:	Germán Zappani (VPC/FMP) and Ariel Rodriguez (VPC/FMP)

I. EXECUTIVE SUMMARY

- 1.1 The Government of Mexico has requested the Bank's support to improve the performance of the national climate change agenda, at the level of SEMARNAT, as well as in sectors that require considerable amounts of public investment and are a government priority.
- 1.2 The Bank will help strengthen SEMARNAT's capacities to coordinate the national climate change agenda by addressing weaknesses identified in the current institutional arrangement for financing, implementation, transparency, and the adjustment of targets. The IDB will also support climate change actions in the urban and forestry sectors, which are highly complex from a sector and land coordination perspective and have major climate change adaptation and mitigation programs in execution. Since the urban and forestry sectors are closely linked insofar as land-use policies guide their development, they need to be aligned with the priorities of the climate change agenda. Changing the way federal sector actions within the country are managed, to better integrate and align them with the climate change agenda, could potentially have a bigger impact on mitigating emissions and increasing climate change adaptation capacities. Such a change should be aimed at containing urban sprawl and reversing deforestation and forest degradation.

II. FIDUCIARY CONTEXT OF THE EXECUTING AGENCY

- 2.1 SEMARNAT, which will be the executing agency, coordinates the development and implementation of national climate change policy through the Interdepartmental Climate Change Commission (CICC). SEMARNAT is thus responsible for monitoring and advancing the Special Climate Change Program (PECC) as established in the General Law on Climate Change.
- 2.2 SEMARNAT also has systems, procedures, and specific functions in place to track the actions and results of each of the federal departments involved in the CICC

aimed at mitigating greenhouse gas emissions and adapting to adverse climate change impacts as part of the relevant national policy.

- 2.3 SEMARNAT will monitor the actions of the implementing agencies and report to the Bank on the outcomes obtained according to their specific programs.
- 2.4 In the forestry sector, climate change actions will be implemented through the National Forestry Program PRONAFOR, which helps owners of forest ecosystems take care of their forest resources and capitalize on them sustainably.
- 2.5 In this project, NAFIN will act as financial agent for the administration and monitoring of fulfillment of the contractual commitments established in the loan contract.

III. FIDUCIARY RISK EVALUATION AND MITIGATION ACTIONS

- 3.1 An institutional assessment of SEMARNAT and the implementing agencies was carried out using the Institutional Capacity Analysis Platform (ICAP) tool. This assessment concluded that SEMARNAT and the implementing agencies are subject to the audit, control, supervision, and monitoring mechanisms of government programs.
- 3.2 The ICAP also revealed that the implementing agencies execute budgetary expenditures for climate change actions. It was verified that these agencies are audited annually according to the International Standards on Auditing (ISA) by Bank-eligible external audit firms designated by the Civil Service Department (SFP). It was also determined that the audit reports prepared in 2015 and 2016 on the financial statements of the implementing agencies contained no qualifications and were delivered in a timely manner.
- 3.3 Based on the foregoing and the institutional assessments performed on SEMARNAT and the two implementing agencies, the fiduciary risk is regarded as low.
- 3.4 The Bank will use technical cooperation resources to engage an independent firm to verify that the results reported to SEMARNAT by the implementing agencies have been achieved. This verification report will be the basis for disbursements.

IV. CONSIDERATIONS FOR THE SPECIAL PROVISIONS OF THE LOAN CONTRACT

- 4.1 The applicable exchange rate for submission of the disbursement request will be the rate prevailing on the last business day of the month prior to submission of the disbursement request to the Bank.

V. AGREEMENTS AND REQUIREMENTS FOR PROCUREMENT EXECUTION

- 5.1 **Procurement execution.** Procurements will be conducted according to the procedures of the procurement system used by the executing agency and implementing agencies.
- 5.2 **Use of the executing agency's procurement system.** The procurement system of the executing agency and the two implementing agencies was evaluated by the Bank using the MAPS methodology and was deemed compatible with internationally accepted principles and standards for all procurement methods. The system will be used for the procurement of goods, nonconsulting services, and consulting services. Only the selection of the independent verification firm must follow the Bank's current

policies, since the financing comes from a technical cooperation project executed by the IDB.

- 5.3 **Retroactive financing.** The IDB will recognize the financing of outcomes previously achieved (retroactive financing) as stated in document GN 2869 1, up to the equivalent of 15% of the total loan amount, for outcomes achieved from 2 October 2017 (project profile approval date) until eligibility date of the loan, provided that the development results achieved are included in the Results Matrix. This request is justified because the operation is part of a national program that has been financing actions to improve land management for the reduction of emissions and climate change. The verification of such previously achieved outcomes will be performed as part of the first independent verification.
- 5.4 **Procurement supervision.** As the procurement system of the executing agency and implementing agencies will be used, Mexico's control and monitoring systems will be utilized for procurement supervision.

VI. FINANCIAL MANAGEMENT AGREEMENTS AND REQUIREMENTS

A. Programming and budget

- 6.1 The programs under the national climate change agenda of the implementing agencies are included in the budgets authorized by the country. Therefore, each public institution is required to perform comprehensive oversight in this area. This will be done through the Integrated Federal Financial Administration System (SIAFF) in place at the national level.
- 6.2 The implementing agencies' budget is authorized through an annual programming/budgetary exercise. The activities of programming, budget and expenditure control, accounting, and accountability based on financial information are governed by numerous regulatory provisions established primarily by the Department of Finance and Public Credit (SHCP). This ensures consistency in the registration and use criteria for the established systems.

B. Accounting and information systems

- 6.3 The implementing agencies perform budgetary and accounting control through the SIAFF. The SHCP has implemented the Accounting and Budget System (SICOP), which is the mandatory, comprehensive system for all federal public administration agencies for processing budgetary, payment, and accounting transactions and, in doing so, consolidating criteria for the recording and control of financial information. SIAFF and SICOP are institutional systems aligned with the SHCP and process transactions internally.

C. Disbursements and cash flow

- 6.4 The implementing agencies will report to SEMARNAT on the achievement of results of their climate change programs every six months using the agreed procedures and forms. This information will be reviewed by SEMARNAT in accordance with its procedures. Upon verification by the independent verification firm that the results have been achieved, SEMARNAT, through NAFIN, will submit the appropriate disbursement request to the IDB.

D. Internal audit and control

- 6.5 SEMARNAT and the implementing agencies have an internal control body with a director appointed by the SFP. This director is responsible for inspecting, overseeing, and implementing the good governance agenda based on transparency, accountability, and strict compliance with applicable regulations at each institution. The federal public expenditure control and evaluation exercise is conducted in keeping with the Federal Expenditure Budget, as well as the Federal Budget and Treasury Responsibility Law and its regulations.

E. External control and reports

- 6.6 **External audits.** SEMARNAT will prepare the project financial information as of the close of each fiscal year. An assurance review of this financial information will be requested, and will be performed by a Bank-eligible external audit firm to be engaged by the Bank. The financial information with the assurance review will be delivered to the Bank 120 days after the close of each fiscal year. The terms of reference for this review will be agreed upon by the Bank, SEMARNAT, and NAFIN.
- 6.7 For purposes of financial supervision, the Bank will rely on the audited financial statements of the implementing agencies reporting annually to the SFP as part of the country's national control system. The audited financial statements are submitted to the SFP within the first four months after the close of the year and are published on the government's public account website, as required by the country's Transparency Law.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-___/17

Mexico. Loan ____/OC-ME to the United Mexican States
Land Management to Achieve Results
under the Climate Change Agenda

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 United Mexican States, as borrower, for the purpose of granting it a financing to cooperate in the execution of the project "Land Management to Achieve Results under the Climate Change Agenda". Such financing will be for the amount of up to US\$600,000,000 from the resources 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.

(Adopted on __ _____ 2017)