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Mexico: Country Program Evaluation (2001-2006)

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FOREWORD

This evaluation report aims to provide factual information on the outcomes of the Bank's work with Mexico in 2001-2006, which could inform the Bank-country strategic relationship going forward. Chapter I reviews the macroeconomic setting and analyzes the main development challenges in the areas targeted by the Bank's programs. Chapter II examines the Bank's country engagement in both financial and strategic terms. Chapter III studies how this relationship is reflected in approved and executed programs. The last chapter discusses the country program outcomes, distinguishing cases in which the Bank can claim to have contributed value-added from those where this has not happened.

EXECUTIVE SUMMARY

Mexico is a paradigm case for a reflection on the type of relationship to be established with a middle-high income country which is financially sound and technically sophisticated but still faces development challenges. The latest economic analyses confirm the arguments advanced in this report, offering on balance a positive picture of Mexico's engagement in the international economy, but noting also that the ensuing benefits have not spread to all of the country's regions and social groups, resulting in the existence of two distinct Mexicos.[1] This key finding provides a focus for the ongoing dialogue on Mexican development policy, particularly in discussions of the International Forum on Public Policies for Development convened by the Organization for Economic Cooperation and Development (OECD) last year.[2] Apart from the historical challenge of catching up to other OECD member countries' living standards, Mexico also faces the fundamental challenge of preventing a large part of the country and its social and political fabric from being persistently left behind.

Recent data and trends corroborate this focus for discussion. Judged by its income distribution, economic structure, and political map, Mexico is not a country with regional inequalities or an unequal development paradox—it is virtually two distinct countries. National income distribution figures show that the northern portion of the country accounts for 85% of wealth generation, and 38% of the population lives below the poverty line—a stark contrast to southern Mexico, which generates under 15% of the nation's wealth and has a 56% poverty rate.[3] The distribution of party political preferences, revealed clearly after the July 2006 elections, reflects these two Mexicos today more than ever. The north is the middle-income Mexico, a modern export economy that generally supports the governing political party. The south is home to the Mexico of poverty and excluded campesinos discontent with the country's institutions. The traditional backdrop of political and institutional stability of continuous single-party government is now a thing of the past.

This evaluation of the Bank's 2001-2006 program with Mexico represents a second round of work done by this office to evaluate the strategic relationship between the Bank and the

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1 See *The Economist*, 26 April 2008: "A tale of two Mexicos. North and south."

2 The International Forum on Public Policies for Development, with permanent representation in the OECD as host, is sponsored jointly by the IDB, the World Bank, the OECD, and the United Nations Development Programme (UNDP). In its forum on competitiveness, it highlights the existence of two Mexicos and argues that the situation entails the risk that economic polarization between the north and south will accentuate social and political polarization in the years to come.

3 Data from the Mexican Statistics, Survey, and Information Bureau (INEGI), using the Mexican government's (asset-based) poverty definition. The corresponding figures for food poverty are 10.23% for northern Mexico and 25.61% for the south in 2006. Whereas 10% of the population shares roughly 1% of national income, the wealthiest 10% receive about 40%, and the wealthiest 1% account for 10%. This polarization is evident not only in income but also in the conditions that determine an individual's economic opportunities and life course from the moment of birth. The chance that a Mexican teen between 16 and 18 is attending school is just 23% in the poorest decile but almost 90% in the wealthiest one (source: John Scott, 2005). According to UNDP data, 95% of *municipios* in the lowest human development index decile are located in the south of the country.

country. The previous evaluation report (covering 1990-2000) expressed concern as to whether the Bank's engagement with Mexico was sufficiently relevant to help overcome existing development challenges, and it specifically highlighted the need to introduce a pro-poor tilt to Bank programs in Mexico and, in that domain, to develop a market niche in which the Bank could contribute technical value-added.

The present evaluation finds that the Bank's work with Mexico in 2001-2006 has done little to follow up on that recommendation. In economics, the term "market niche" means a specific segment of the market that represents a business opportunity because it is not being reached by the regular supply of products or services generally on offer.[4] Far from developing a strategy to identify market niches thus defined, in 2002 the Bank produced a country paper setting out a wide range of generic proposals for intervention in multiple sectors, but with no focus on developing potential comparative advantages. In practice the country paper seldom drove subsequent programming decisions. If this evaluation had to identify an institution that has endeavored to build a strategy around market niches to position itself as a relevant player for the long term, it would be the World Bank. Over the last few years, a deliberate World Bank strategy of identifying niches to build a long-term strategic partnership with Mexico and develop a differentiated advisory product has resulted in an expansion of that organization's Mexico portfolio. In fiscal 2006 this was the World Bank's largest portfolio worldwide and, at US$1.8 billion, almost as large as the IDB's.

Today, as a new country strategy is being developed for the six-year span from 2007 to 2012, the Bank's relationship with Mexico is at a particularly critical juncture. The country is planning to reduce its external dollar debt, the cost competitiveness of doing business with the IDB is no longer a given, and the World Bank's position as an alternative financing source appears to have strengthened. With a view to guiding the Bank's future engagement with Mexico, this report offers an answer to a fundamental question: in which cases, and under what circumstances, were IDB-supported programs in 2001-2006 fruitful for the country, on balance—looking at both lending and nonlending contributions, to address the specific requirements of a client such as Mexico?

To that end, and in follow-up to a specific request made at the outset of this evaluation by the Public Credit Unit of Mexico's Ministry of Finance, this evaluation will focus on outcomes and the value added by the Bank. As an assessment of outcomes, the analysis looks at value added to intervention outcomes, in terms of enhanced outcomes achieved by virtue of the authorities' having taken ownership of the advisory and other support services provided by the Bank. The analysis of value-added in this evaluation entailed the following: (i) definition of key elements for achieving outcomes in each intervention, based on their evaluability; (ii) review of documents relating to the provision of advisory services or nonlending products by the Bank, based on available managerial documentation; (iii) verification of the use of the advisory services and the tie-in to decision-making, based on information provided by the authorities involved or by the Management of the Bank; and

[4] Definition from Ramón Tamames, *Diccionario de Economía y Finanzas*, 13th edition, Alianza Editorial, 2006.

(iv) a cross-analysis of the contents of advisory services provided by the Bank with outcomes of each intervention.

This evaluation report thus encompasses the three core elements of the Bank's strategic relationship with Mexico: *relevance, outcomes, and value-added.* It distinguishes interventions which positively (a) addressed a major challenge and proposed what can be judged to be relevant measures to address it; (b) delivered their outputs and the expected outcomes; and also (c) received advice or nonlending products from the Bank which added value to the outcomes obtained.

The analysis shows that the Bank's work during the period examined here has for the first time demonstrated the possibility of establishing a relationship which in some measure simultaneously satisfies those three characteristics. The predominant element of the portfolio in 2001-2006 was the Mexican government's *Progresa-Oportunidades* program, which accounted for 42% of total disbursements during the period. This program marks a positive change in the Bank's strategic partnership with Mexico and a positive image of the Bank both in terms of relevance and in terms of some of the outcomes achieved, along with a degree of tangible technical value added by the Bank. Other interventions in the financial area, such as *Finrural*, in the energy efficiency area and, to some extent, in the housing sector, provide cases where the Bank has added value to the outcomes achieved.

Detailed analysis of the available documentation on these cases in which the Bank has developed a substantial portfolio based on its technical credibility in a given sector shows that the latter has not been part of a formal strategy but has been associated with the particular staff members in charge or idiosyncratic circumstances of the country. In the case of *Oportunidades*, the Bank may have found a market niche in a particularly relevant area, namely keeping the program operational, especially in terms of targeting and better redistribution of social expenditure. Nonetheless, it has not been able to translate this creation of market position into a strategy for consolidating a differentiated product with lasting prospects, or for linking lending and nonlending supports based on the presence of permanent teams of experts.

In contrast, other programs in the sovereign guaranteed portfolio in 2001-2006 are anchored in the pattern pointed out in the previous OVE evaluation. These are of little relevance, particularly where their poverty impact is concerned; their outcomes are difficult to evaluate and the technical value added by the Bank is intangible or hard to pin down.

During the span examined here the Bank's private-sector window maintained its historical limited presence. More recently—beyond the period of this evaluation—there has been a record upsurge in the size of this portfolio, with an average approval level over the last two years seven times the figure for the past 10 years. The private-sector share of approvals has grown to considerable proportions—47% in 2006 and 62% in 2007. As in the public-sector portfolio cases noted, this private-sector portfolio performance sends a positive signal as to its future scale-up possibilities under the constraint of adding value to development outcomes, considering the size of this market and the opportunities it offers.

As a general conclusion, OVE believes the Bank should pursue an essential reflection on the type of strategic relationship that should be developed with a medium-high income country such as Mexico, which has one foot in the OECD but the other trapped in persistent pockets of poverty. On the basis of the analysis done, the evaluation fully endorses the recommendations made by this office in its previous country program evaluation (CPE), which remain valid, not having elicited any change in the Bank's strategy roadmap. Both the positive findings of this evaluation of the Bank's experience, and World Bank experience during these years, corroborate the aptness of focusing on development of relevant market niches as a means of scaling up sovereign guaranteed lending, backed now by incontrovertible data on the reaction of demand and its viability. The most recent experience of the private-sector window also points up upward flexibility and value creation opportunities that remain undertapped given the size of this market.

Taking account of these findings, and with a view to maximizing relevance and outcomes in middle-high income countries that still face considerable challenges, this evaluation proposes the following adjustments to the previous OVE recommendations.

Recommendation 1: A market niche strategy. Building on the experience of the *Oportunidades* program and other practical lessons learned from the previous cycle, tailor programming to the needs of a middle-high income country, with a view to maximizing the value added by the Bank, so as to underpin long-term strategic engagement in the sectors in question and make financing a subordinate function. To achieve that, it would be necessary to:

a. Identify market niches according to client demands, and tailor the use of nonreimbursable technical cooperation resources and the Bank's human resource management to them, to enable the Bank to develop advisory products that add value to its intervention outcomes; and
b. Focus the lending portfolio on a small number of loans, generalize the financing modalities trialed during the period that achieve a substantial reduction in project transaction costs, and seek innovative, client-needs-driven financing vehicles.

Recommendation 2: A financing approach adapted to dissimilar conditions. Provide differentiated support, both in public-sector lending and nonsovereign guaranteed finance, to address the various needs of a middle-high income country that has persistent but largely geographic development disparities. To achieve that, it would be necessary to:

a. Instill a systematic pro-poor tilt in the Bank's supports, particularly its public-sector portfolio, grounded in a diagnostic of specific needs in this area for each intervention sector and emphasizing the specific needs of the southern states; and
b. Act on the increasing opportunities for scaling up private-sector window financing, under a logic of development value-added in the economic growth and competitiveness area.

I. The Country Setting and Development Challenges

1.1 Mexico has been the only Latin American member of the OECD for more than 12 years now. Although the country currently has one of the highest per capita incomes in Latin America (over US$11,500 in 2006), income is not growing fast enough to catch up to the living standards of other OECD member countries. The challenge of narrowing Mexico's external development gap is matched by the need to close its domestic gap: roughly half the population is living in poverty, particularly in rural zones, and the proportion living in extreme poverty in the south of the country is 2.5 times higher than in the central and northern states. The country's economic structure can be stylized in terms of an agricultural sector that accounts for 5% of GDP but generates one fifth of all employment, and an oil sector that generates barely 1% of GDP but is crucial as a generator of foreign currency and the source of one quarter of the nation's tax revenue. The industrial sector makes up 26% of the economy but generates over 80% of the country's exports. Services are the largest sector, representing two thirds of the economy.[1] To put the present evaluation in context, the next section summarizes Mexico's economic, social, and political evolution over the last few years and reviews the behavior of the development challenges previously identified as priorities by the Bank, from the specific standpoint of the 'two Mexicos.'

A. Recent economic trends

1.2 Over the last few years, Mexico has solidified its position as a middle-high income economy, and its increasing access to diversified financial markets provides a backdrop for its current financial relations with the Bank. The financial markets' perception of Mexico has improved, thus enabling it to secure better terms for its sovereign debt. The economy's positive performance on the public finance side has also allowed it to significantly reduce its borrowing requirements.

1.3 Between 2000 and 2001 three rating agencies[2] upped Mexico's long-term foreign-currency debt to investment grade. The upgrade meant that its debt has since been considered low risk, i.e. little likelihood of financial default. In practical terms, promotion to investment grade among other things has meant access to a range of institutional funds in the advanced economies, substantially easing liquidity constraints and the likelihood of external shocks. Mexico's sovereign risk indicators have also continued to trend favorably compared to those of other emerging economies. In fact, the Mexican economy remained virtually unshaken during major episodes of financial instability between 2001 and 2005.[3]

1.4 This change in Mexico's risk perception also reflects a number of changes that have occurred in the country's economic fundamentals, particularly the liberalization of the economy under the North American Free Trade Agreement (NAFTA). For example, the composition of the Mexican export basket has changed significantly over the last decade: exports have grown in volume terms and have also diversified, with a relatively larger industrial share and less volatility in terms of total volume. The major inflows on Mexico's balance of payments have become a relatively stable financing source, making the country's external accounts more sustainable and generating positive dynamics in public-debt management and the country's fiscal position.

1.5 In this setting, the economy's annual growth rate has averaged less than 4% since the 1995 crisis. Only in 2006 did growth reach 4.8%, thanks to solid export and investment performance. But the most recent forecasts see a slowing of economic activity, with potential growth rates around 3.5% or 4%. With Mexico's population rising 1.3% per year, those rates are insufficient to keep problems of poverty and inequality in check. The growth rates recorded are still too low to bring about significant changes in poverty levels or development for the majority of the population.[4]

1.6 Conditions of vulnerability persist in Mexico and threaten the economy's long-term stability. The country's close trading relationship with the United States means that its economy tends to mirror industrial activity in its northern neighbor. The correlation between Mexican and U.S. GDP (based on a sample of the five previous years) increased from -0.46 in 1994 to 0.82 in 2005. Total factor productivity (TFP) has been declining since 1980.[5] Areas cited as barriers to competitiveness, with implications for the economy's productivity, include energy, telecommunications, social security, and the labor market.

1.7 A more positive outlook does not mean the risk of imbalances has disappeared, especially considering that the fiscal and external sectors are highly dependent on the price of oil and the nonoil tax effort has not been very successful.[6] In the fiscal domain, the public finance situation has little slack, considering its reliance on oil revenues (which accounted for 40% of government revenues in 2005) and the growing demand for essential spending on education, health, poverty alleviation, and infrastructure. The public sector posted a cash deficit of 1.2% of GDP in 2002, the highest since 1998. Nonetheless, the situation has gradually improved, thanks to payroll expenditure cuts and higher oil prices. Federal government revenues from oil duties rose from 2.2% of GDP in 2002 to 5.6% in 2005, more than offsetting the near two-percentage-point drop in tax revenues over that interval.[7]

1.8 In the external sector, oil export earnings and remittances from Mexican workers abroad were also crucial for reducing the balance of payments deficit on current account, which at end-2005 stood at 0.7% of GDP, a more than two-point improvement over 2002. Oil exports account for nearly two thirds of export growth between 2000 and 2005. In addition, although Mexican exports have lost some of their U.S. market share to China, the United States still absorbs 85.7% of Mexico's total foreign sales, down from 88.1% in 2002.[8] Maquila exports have held broadly steady at less than 13% of GDP since 2001, although the maquila sector trade surplus remains close to 3% and is crucial for the current account balance. Remittances climbed from 1.6% of GDP in 2002 to 2.5% in 2005. The capital account has been in surplus in recent years thanks to inflows of foreign direct investment (FDI) and a sharp increase in portfolio investment between 2002, when the net flow was negative, and 2005, when it topped US$10 billion, attracted by a securities market offering high yields and the interest rate spread with respect to the

United States. All of this has enabled the Mexican economy to continue accumulating international reserves, which by end-2005 had grown to US$75 billion.

B. Development challenges

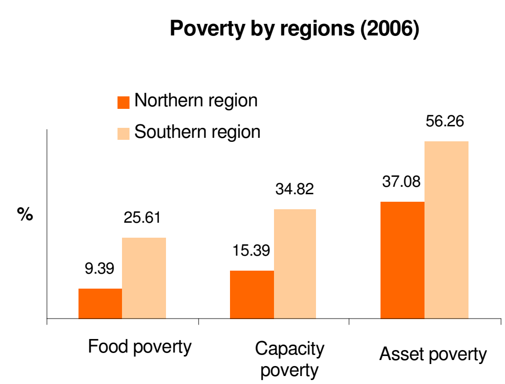
1.9 As a framework for evaluating the Bank's country program, this section looks at recent trends in the most important development challenges in the domains identified by the Bank in its country strategy, namely social development and poverty, regional integration, modernization of the State and decentralization, and barriers to private-sector competitiveness.

1. Social development and poverty

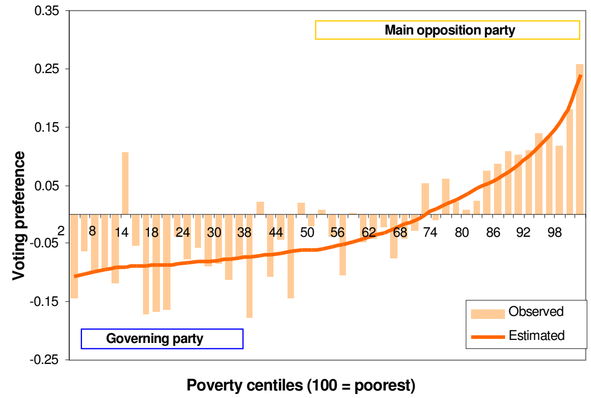
1.10 Mexico's economic growth has not been strong enough to make a significant impact on reducing poverty and inequality gaps, and its social policies are insufficient to correct the resultant disparities. In this area, the country faces major social and labor policy challenges. Employment rates are below the OECD average, while the rate of self-employment is one of the highest. During the last few years of moderate growth, formal wage earning employment has stagnated and at end-2005 was still at end-2000 levels.

1.11 During this interval of poor performance of formal employment, the labor force grew by a cumulative 4 million people, i.e. average annual growth of 2% (INEGI, 2004 and 2005). As too few formal jobs were created, labor supply pressure pushed up informal employment (which rose to 43.5% in 2004, surpassing the formal employment rate of 40.1%) and fueled further worker migration to the United States.[9] The existence of a very large informal sector has served as a buffer in times of crisis, but the highly precarious jobs it provides means that average labor productivity is very low—about one third of average productivity in OECD countries (OECD, 2005).[10] Improving the quality of human capital poses a challenge to unlock the country's growth potential and raise its income levels. The high proportion of low productivity jobs often—albeit not exclusively—reflects inadequate human capital.

1.12 While some headway has been made in reducing overall poverty levels over the last 10 years, official poverty indexes for 2006 concentration in the country's southern stat higher than the OECD average. Mexico's differentiation, deeply rooted in difference factors.[11] Mexico has the most unequal incor and has made relatively modest progress on Gini coefficient estimated using current hous 0.46 in 2004.[12] The two highest income decil (money and nonmoney), whereas the two l total. Compounding this is the fact that so limited, so poverty is reproduced from one ge

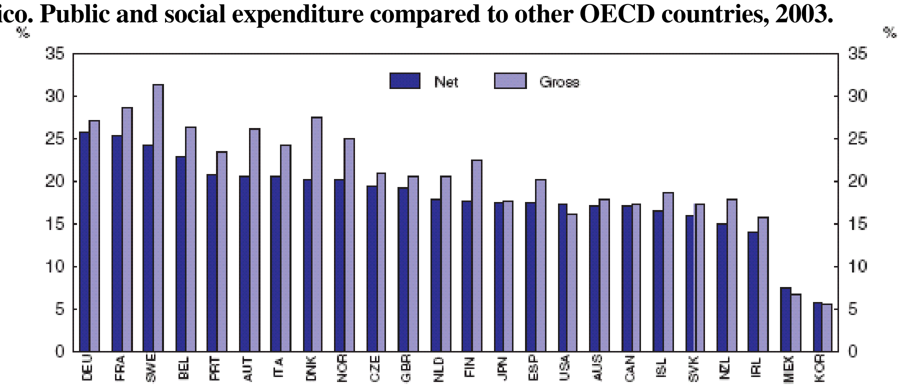


1.13 This persistent inequality and the regi
two distinct Mexicos also generates
confirmed by the distribution of votes
2006 presidential elections. An analy
those elections reveals a correlation ve
and voting patterns. Thus, *municip*
marginalization or high poverty rate
leading opposition party, whereas the
governing party.[13]



1.14 Mexico's social policy budget is belov
public funds for social development
security systems whose efficiency could be improved. This essentially makes for a two-tier system, in which the social security system proper covers workers in the formal sector, basically providing health insurance and pensions. Social assistance programs, on the other hand, benefit the population that is not otherwise covered, including urban informal-sector workers and their families and the poorest population groups that typically live in rural areas. As the benefits dispensed exceed contributions paid in, the system has historically been highly dependent on Treasury subsidies.[14] The two main assistance programs, *Progresa/Oportunidades* and *Seguro Popular de Salud*, have expanded over the last few years, but their budget is probably insufficient relative to the scale of the problem they face.[15]

Mexico. Public and social expenditure compared to other OECD countries, 2003.



Source: OECD, SOCx database.

2. Regional integration

1.15 Mexico's global economic engagement over the last two decades has been generally positive on the foreign trade and foreign investment sides, but the ensuing benefits have not been equally distributed across all the country's regions and social groups.[16] Deeper integration has mainly availed states in the northern band and center of the country, whereas southern states have remained largely sidelined. Four Mexican states—Baja California, Coahuila, Chihuahua, and Nuevo León—together accounted for 60% of the country's export growth in 1993-2003; at the other end of the scale, 16 states together contributed just 1%.

1.16 Similarly, over three quarters of FDI inflows between 1994 and 2005 went to the Federal District and four states (Nuevo León, Baja California, Chihuahua, and Mexico State, in descending order), while 19 other states together received just 3% of the total.[17] In contrast, states with the highest incidence of poverty and, generally, the lowest human development indexes have not shared either in export growth or in attracting foreign capital. This situation raises the risk that north-south economic polarization could accentuate the country's social and political divide in the coming years. The emphasis on "top-down integration" contained in the Puebla-Panama Plan (PPP) has not yet produced the expected results.[18]

1.17 Lack of competitiveness in the southern states also restricts this subregion's engagement in international markets. In terms of competitiveness, Mexico's southern states generally display shortcomings in the coverage and costs of telecommunications, electricity, and transport infrastructure and logistics services. Low productive investment in the south also means less availability of human capital and scant commercial bank presence. The competitiveness environment and the type of production fabric affects firms' capacity to grow and participate in international trade. Reducing the competitiveness gap and connecting small-scale Mexican industry to the manufacturing export markets developed in recent years is both an opportunity and a challenge for the country's industrial and integration policy.

3. Modernization of the State and decentralization

1.18 Mexico has earned a reputation for fiscal probity, and the new Fiscal Responsibility Law is expected to solidify prudent fiscal management. The Tax Reform Law passed by Congress on 14 September 2007 makes changes to the tax structure. These reforms, the revenue effect of which is estimated at 2.3% of GDP, could help to make fiscal sustainability less reliant on oil revenues. Expenditure responsibilities have been rapidly devolved to the states and *municipios*, particularly in recent years; in fact, revenues received by the states for investment have exceeded the budgeted amounts. In this setting, intergovernmental fiscal relations are a key aspect in which there is room to improve expenditure efficiency. On the revenue side, the year-on-year growth of transfers and recourse to public and private borrowing may have given some subnational governments less incentive to exercise taxing power and capacity. On the expenditure side, the state and municipal shares increased from less than one third in 2000 to over 40% in 2005, although there is limited control over the use of funds.[19]

1.19 The tax reform aims to stimulate state and municipal revenue generation by linking the increase in transfers to the states' economic growth and their tax collection performance and revamping transfers to the states.[20] An outstanding challenge is to create an institutional framework that enables the federal government to tailor its economic and social development policy work to the specific needs of the country's different regions.

4. Essential services for improving competitiveness

1.20 Development banking services play an important role in the Mexican financial sector, since they represent a considerable part of the consolidated commercial banking system.[21] In 2001 the legal framework governing development banking was amended, as part of the National Development Financing Program (Pronafide), through the enactment of the Credit Institutions Law and amendments to the banks' charters. There is also evidence that development banks' management autonomy has increased, corporate governance has improved, and the powers and responsibilities of the institutions' boards of directors have expanded, among other changes. As a result, development banks now offer a varied range of products and are run with a managerial focus on financial results. Accordingly, the subsidies that were the norm in decades past have been virtually banished. Nonetheless, in practice it is common to see development banks competing with private commercial institutions in different market niches and, in their zeal for profits, they exclude certain sectors that do not have access to credit.[22]

1.21 Among services that are essential for the economy's competitiveness, the energy and communications sectors have remained virtually unchanged. The political economy of reform is a key issue for making headway on structural change in Mexico. In the case of electricity services, the sector is dominated by the vertically integrated public National Energy Commission (*Comisión Nacional de Electricidad—CFE)* and a smaller firm, Luz y Fuerza del Centro (LFC). The Mexican Constitution gives the State exclusive rights to supply electricity as a public utility. While amendments to the Public Electricity Services Law in 1992 allowed private investors into the power generating sector, it requires them to sign 25-year sale contracts with CFE or LFC. The presence of a dominant player in the generating segment; power pricing and, in particular, the investment needed to meet expected demand increases without straining the power grid, are among the challenges awaiting in the coming years.

1.22 Major challenges for social infrastructure services concern glaring disparities in scope and coverage. Most home finance in Mexico is provided by private lending institutions that target the higher income brackets (incomes between three and nine minimum wages or higher), while the poorer segments usually have very limited access to home loans.[23] As for water and sanitation service coverage, the latest data show that the situation has improved in recent years but coverage is still insufficient.[24] Rural areas continue to display significantly lower potable water indexes than those of urban zones (70.6% rural coverage compared to 95.1% in towns and cities). There are also significant differences in terms of geographic distribution, with the greatest service gaps in the southern states, particularly in smaller communities.[25] Sanitation and sewerage services have also expanded somewhat, although coverage estimates for 2003 (77.2% overall) continue to reveal significant differences between rural areas (38.5%) and urban communities

(90.4%). The figures are worse still if one considers the proportion of wastewater that is treated before being disposed of: just 23.6%.

1.23 All diagnostics of the state of the environment in Mexico suggest that the country has not yet managed to break the link between economic growth and environmental pressure. The latest policy analyses point up different pressures on resources by region and social segment. Firstly, there is pressure exerted on natural resources by the urban population of the center-north of the country, compounded by a concentration of industries in zones that are already severely degraded. Secondly, such studies draw attention to the relationship between poverty and environmental degradation and its association with changes in land use, expansion of the agricultural frontier, and biodiversity loss.

II. PROGRAMMING

2.1 The 2002-2006 country strategy paper did not propose an intervention niche in which the Bank could contribute greater value-added, or define an overarching objective. The strategy is therefore mapped out as a broad set of potential interventions around the following four objectives:[26]

a. Social sector and poverty reduction. Help to reduce poverty through transfer programs, with actions targeted on extreme poverty in the southern states.

b. Integration. Support the Puebla-Panama Plan as a way of raising productivity in the southern states, exploiting their links with Central America.

c. Modernization of the State and decentralization. Help the country preserve public order, rights and freedoms, provide honest and efficient governance, and decentralize expenditure efficiently.

d. Lowering of barriers to private-sector competitiveness. Help the government reduce constraints to private-sector competitiveness.

2.2 This section evaluates the Bank's engagement with Mexico around those four objectives. Firstly, financial relations between the Bank and Mexico are analyzed, as a dominant factor, followed by an analysis of the strategic relationship developed through preparation of the country paper and project approvals.

A. The financial relationship between the Bank and Mexico

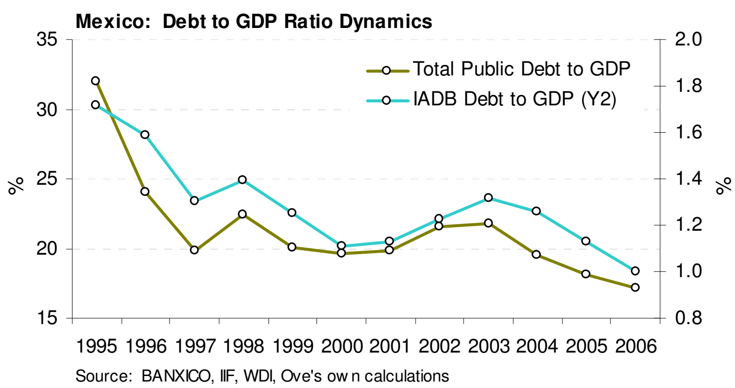
2.3 While Mexico is a very important client for the Bank in terms of portfolio volume, considering the size of the country's economy and the financial resources managed by the public sector the Bank's financial contribution to Mexico is relatively modest. As a result of this asymmetric relation, the Bank's stance vis-à-vis its engagement has tended to be passive, thus diminishing its influence in developing a more strategic relationship.

2.4 From the IDB standpoint, Mexico is an important client not only because of the size of its total borrowing from the Bank but also because of the annual volume of financial flows generated by the debt stock. For example, on average between 2002 and 2006, 15.2% of all approved loans, 17.7% of total disbursements, and 16.2% of all financial income received were generated by the Mexico loan portfolio. At end-2005, the cumulative total of Mexico's IDB loan portfolio amounted to US$7.9 billion—one sixth of the Bank's Ordinary Capital portfolio at that date. In 2006, Mexico reduced its debt to multilateral agencies by prepaying US$9 billion, and this decreased its IDB financing portfolio to US$4 billion. If one includes funds other than Ordinary Capital resources, plus loans to the private sector, Mexico's active portfolio with the IDB represented 14% of the Bank's total active portfolio in late 2006.

Active portfolio as a proportion of the Bank's total active portfolio: selected countries	Mexico	Argentina	Brazil	Colombia
Ordinary Capital loans	9%	24%	22%	4%
Loans to the private sector	18%	1%	37%	5%

2.5 In contrast, from Mexico's standpoint the Bank's role as a funding provider today is not fiscally significant. The importance of the Bank as an international funding source for Mexico has declined sharply in the recent past and is currently modest. It is illustrative that IDB disbursements to Mexico in 2006 represented just 0.12% of total Mexican public sector income and 0.82% of public capital expenditure. Moreover, in recent years the country has steadily reduced the size of its IDB debt as a proportion of GDP.

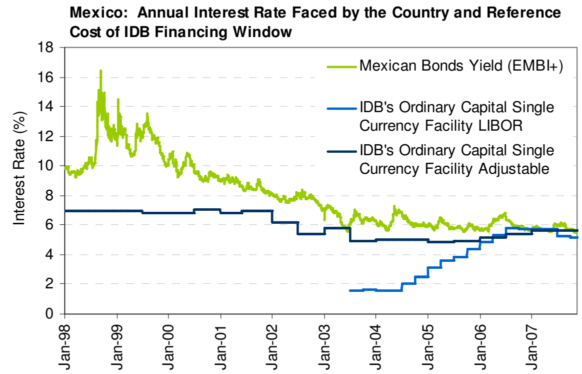
2.6 The progressive reduction of the Bank's importance as a funding agent for Mexico can be explained by a number of financial factors. To cite two of these: (i) the Mexican economy has reduced its gross foreign currency borrowing requirement, thus decreasing the total size of the market, and (ii) the Bank has become a relatively more costly funding source than other alternatives available to the Mexican public sector.



2.7 The reduction in Mexico's borrowing needs reflects the same factors that produced a change in risk perception and a positive trend in the main financial flows into the Mexican economy. In this regard, the recent performance of the private savings balance[27] and current account balance—adjusted for foreign investment flows—as an estimation of gross macroeconomic financing needs is trending up. The natural implication of this is that Mexico has less need for external financing, at a time when the terms it is able to secure on international capital markets also have improved considerably.

2.8 At the same time, the Bank has become less cost competitive as a financing source than other alternatives available to the Mexican public sector. For most of the period 2002-2006 the interest rate structure offered by the Bank was on a par with the terms Mexico obtained on new long-term debt offerings. Over the last decade Mexico has substantially expanded the range of potential external financing sources for its economy, thus obtaining greater access to international liquidity, even in periods of volatility.[28]

2.9 In this setting of less competitive pricing in a shrinking market, developing a strategic relationship based on the creation of nonfinancial value becomes critical. The following section analyzes the Bank's strategic approach and programming during the period, from the standpoint of its nonfinancial value-added.



Source: Bloomberg, IDB's Finance Department

B. The strategic relationship between the IDB and Mexico

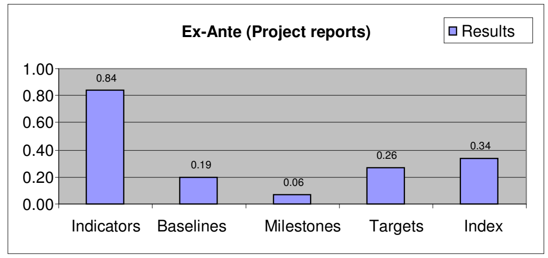
2.10 A financial relationship of this type—asymmetric and increasingly less competitive in financial terms—made for a programming relationship that entailed reactive behavior on the Bank's part. Consequently, during the period examined here, programming decisions were seldom country strategy-driven. Proof of this is the limited quality of the 2002-2006 programming documents, in terms of their evaluability, and their low predictive capacity, in terms of anticipation. It is only reasonable that the Mexican Treasury authorities should base their decisions on incentives aligned to the financial import of same; this does not necessarily favor prioritization of the Bank's program. In such a context, the strategic relationship that is created comes to depend on proactive behavior by the Bank.

1. Evaluability

2.11 An analysis of the country strategy's evaluability, both in terms of programming and portfolio review, shows that the relationship that the Bank formally established with Mexico does not provide a framework of evaluable outcomes that can be monitored, managed on the basis of outcomes and country portfolio risks. Application of the country strategy evaluability methodology shows that no indicators had been identified for the outcomes being pursued or the targets sought in any of the areas in which the Bank decided to intervene. The overall evaluability index of the outcome matrix in the country strategy with Mexico was 0.16, below the Bank average of 0.18,[29] and with considerable differences between individual programming areas.

Ex ante Evaluability Index summary (CP-OVE)					
Objectives	**Indicators**	**Baselines**	**Milestones**	**Targets**	**Index**
Social reform/poverty	4	4	0	3	0.55
Integration	0	0	0	0	0.00
Modernization of the State	0	0	0	0	0.00
Decentralization	1	1	0	1	0.15
Competitiveness	1	1	0	0	0.05
Total	**6**	**6**	**0**	**5**	**0.16**

2.12 A complementary way to obtain benchmarks to evaluate programming quality involves repeating the evaluability exercise for each project ultimately approved. The resulting evaluability index, which gauges the degree to which project objectives have measurable outcome indicators, baselines, milestones, and targets, averages 34%.



2. Anticipation

2.13 As was pointed out in the previous OVE evaluation, the Bank's strategy with Mexico fails to define how and in what measure the Bank aims to contribute to the country's development outcomes, and the strategy serves as an umbrella document that broadly defines type of financing, objectives, and strategic focus. Information on the future programming of the country paper's project pipeline also had limited predictive capacity. The anticipation rate of the 2002-2006 project pipeline (just 31% in terms of number of projects and 50% in terms of amount) is significantly lower than the equivalent index found in a sample of previous country program evaluations.[30]

Sector	Anticipation rate (Number of projects)	Anticipation rate (Base case scenario amounts)	Anticipation rate (High scenario amounts)
Decentralization	40%	80%	63%
Integration	0%	0%	0%
Poverty	29%	57%	55%
Private sector	38%	11%	41%
Total	31%	49%	51%

2.14 Thus, the relationship that the Bank has traditionally established in country strategy development exercises has been an open one, with much volatility in programming decisions during the cycle. Under these conditions, the Bank's country strategy with Mexico has not fulfilled its essential purpose of pursuing outcomes-driven strategic engagement with the country, either when formulating country programs or in decisions taken during the cycle.

3. Risk management

2.15 The country strategy also identified a number of generic risks that appear to be disconnected from its thrust and for which no mitigation or monitoring measures were proposed. The section on risks did not anticipate the major fiscal management elements that would come to drive subsequent programming definitions. The country paper was approved in April 2002, when the fiscal reform was already running out of steam, ultimately to be shelved; this posed the greatest obstacle to delivery of the government's commitments in the 2001-2006 administration. Whereas the World Bank anticipates this risk in its strategy and rates it as substantial, the IDB does not explicitly name it as a risk in the corresponding section. By drastically affecting the expenditure plan it may have had a significant effect on de facto programming.

2.16 A comparative analysis of the risks identified by the IDB and the World Bank's risk matrix in the same period (Report 23849-ME) also shows that the IDB strategy failed to identify some risks that were relevant for its programming. One was the political risk of failing to forge the requisite consensuses to advance on reforms in sectors such as energy, telecommunications, the justice system, and the labor market, which ultimately materialized, affecting sectors in which both institutions had interventions programmed. The World Bank's strategy also explicitly addresses the challenge of adding technical value to its portfolio.

4. Relevance analysis by sector

2.17 To judge by its scant action anticipation capacity, the programming contained in the country strategy was not representative of the Bank's potential strategic relevance, nor did it drive programming and lending decisions. In view of this, the relevance analysis in this section does not focus on that strategy paper exclusively but analyzes also the relevance of the intervention proposed and the Bank's contribution to the programs that were ultimately approved.

a. Social sector

2.18 The Bank's strategic decision to target its interventions on poverty alleviation, with special emphasis on human capital development and better functioning labor markets, was a relevant proposition that gave the Bank the opportunity to add its support to a line of targeted expenditure programs to aid the most disadvantaged segments of the population.[31] During the period examined here the Bank was able to participate in a family of programs run by the Mexican government, such as *Progresa-Oportunidades, Procampo,* and *Habitat*, aimed at relieving rural and urban poverty, with complementary focuses depending on their specific adjustment needs, relative fiscal weight and political importance.[32]

2.19 This is not the case in the education and health sectors where, although the proposals identified relevant issues such as efficiency, quality, and regional equity in the supply of those services, the program failed in practice to translate into any significant Bank presence in these sectors.[33] In fact, apart from *Oportunidades*, the Bank was virtually absent in the social service supply sphere, with the single exception of the Community Education Program which only makes a complementary contribution to solving the problem of inequity in education supply.

2.20 The employment and social security sectors offer no examples of relevant interventions by the Bank. The strategy does make a priority of labor market reform pursuing a logic of greater flexibility and recognition of contingent liabilities arising from the social security system. Despite having played a role in this sector for over

20 years, the Bank's program during the period reviewed here had less influence than in the previous programming cycle, having focused its support for the sector on the operation of some specific employment instruments such as vocational training or employment information. The challenges diagnosed in terms of adaptability of the labor force to the dynamic markets of the open economy model, and the need to strike a better balance between the regulations needed for the formal employment sector, barriers to productivity, and the prevalence of incentives for informal employment, are still there.[34]

b. Regional integration

2.21 In the country paper the Bank aligned its strategy thrust in this sphere on the Puebla-Panama Plan (PPP) initiative, taking the specific stance that to alleviate the relatively severe poverty of Mexico's southern states it would be useful to support development initiatives in these states and integration projects with Central America.[35] This strategy approach introduces a positive element of concern with raising productivity levels in southern Mexico. At least where the Mexico portfolio is concerned, the programs envisaged under the PPP umbrella failed to gain approval. Furthermore, the Bank's analytical work on integration, by way of its nonlending products, focused on other aspects relating to the FTA with North America.[36] The specific trade focus proposed by the strategy has not borne fruit in terms of trade growth, and both the southern Mexican states and the Central American economies have revealed their preference for other markets.

c. Modernization of the State and decentralization

2.22 The country strategy proposes a series of interventions to improve efficiency, government accountability, and the regulation of markets for services that are essential for the economy, but in practice these proposals have not elicited any financial support from the Bank.[37] Despite the magnitude of the challenges involved in adapting State structures to socioeconomic needs, the Bank's participation has been limited, with the single exception of a recently approved PRODEV program.

2.23 In the decentralization domain, which ties in closely to the current political challenge of reducing geographic disparities, the country strategy places the emphasis on expenditure efficiency and mobilization of own resources, including local taxes, along with governance and legal framework improvements.[38] The Bank has been supporting the decentralization process through a multiphase program to strengthen state and municipal governance and financial capacities, but the number of states and *municipios* proposed by the program for capacity strengthening is too small to plausibly claim that an intervention of this type is relevant given the challenges identified in this area.

d. Barriers to private-sector competitiveness

2.24 With regard to lowering barriers to efficient private-sector development, the strategy identifies challenges in several sectors and proposes actions in the financial sector, liberalization of services that are essential for the economy, basic services and social infrastructure, and the environment.[39] In the financial domain, the Bank did not undertake any specific studies aimed at heightening the presence of development banks to open up the market to sectors or entities that do not now have access to credit, or making the most of their subsidiary role as, in fact, the government itself had proposed.[40] The competition between the development bank sector and private commercial banks is fairly evident in several market niches, such as small and medium-sized enterprises, or subnational governments. Given the importance of this issue in Mexico's financial and production sectors, and development banks' weight in the IDB portfolio, the strategy's proposals for addressing these challenges proved insufficient.

2.25 In terms of services that are essential for the economy, the reforms expected in certain sectors addressed in the strategy did not take place, and this constrained the Bank's action. In the energy sector, a Bank objective was to support reforms in the electric power sector, to gradually open it up to competition and private capital, both in the generating segment and in transmission and distribution.[41] The liberalizing approach of the programming contrasts with the supports actually delivered, which did not constitute a concrete, relevant response to that objective. The Bank has provided support through its private-sector window for a number of power generating projects which—as simultaneous progress on sector reform did not occur as planned—may have helped consolidate the dominant market position of the public electricity company. In contrast, the financing of the energy efficiency program, not envisaged in the strategy, proved to be a relevant experience for promulgating new energy efficiency standards. The rural electrification programs envisaged in the strategy did not come in for Bank support.

2.26 In the case of basic services and social infrastructure, though the Bank's intervention had proposed relevant objectives for narrowing the access gap between rich and poor, the programs executed for the water, sanitation, and housing sectors have not firmly positioned the Bank as a relevant player to help overcome institutional inertia and constraints in the respective markets. In the water and sanitation sector particularly, the Bank proposed to support regulatory and institutional framework strengthening through technical cooperation operations, loans, and sector dialogue, aimed at increasing operating efficiency, as well as pricing of water resources and the associated revenue collection. The Bank programs ultimately approved have partially pursued this programmatic aim through a coverage expansion approach.

2.27 On the environmental front—a priority for the Mexican government and one of the Bank's four defined action priorities[42]—the strategy addresses environmental issues only tangentially.[43] Aside from a brief general mention, it does not make a detailed situational analysis highlighting the need to work on environmental issues and prioritizing measures on which the Bank could have targeted its support.

5. Follow-up on learnings from the previous evaluation (1990-2000)

2.28 OVE's evaluation (CPE) of the 1990-2000 country strategy set out a framework of macroeconomic issues and key development challenges for Mexico, highlighting the apparent paradox of sustained economic growth but high levels of poverty and inequality, and outlining the challenge facing the Bank in its country work. Apart from the specific area of poverty alleviation programs, this evaluation finds that many of the previous CPE conclusions are also applicable to the Bank's engagement with Mexico during the period examined here. Table 1 of Annex A sets out the conclusions and recommendations of the previous evaluation, distinguishing those that are still applicable from items in which improvements have been made, and indicating the paragraphs of this report that confirm those findings.

2.29 In brief, the present evaluation notes that practically all the conclusions relating to the Bank's strategic focus and development effectiveness remain applicable to the current program, confirming the above-noted features of a nonstrategic country engagement. In particular, the recommendations made in the previous CPE do not appear to have elicited any proposal by the Bank to alter the tenor of its country engagement. As noted below, if this evaluation had to identify an institutional actor that has responded to the recommendation to develop a strategy around niches of long-term relevance, stressing the value-added of the advisory assistance provided, it would be the World Bank.

6. Strategic position vis-à-vis other multilaterals

2.30 As mentioned above, in the recent past the Bank appears to have lost its competitive edge as a cheap source of external financing for the Mexican public sector. Moreover, the 2000 recession has set a precedent, since it produced neither a shutdown of financial markets for Mexico, as traditionally happened with this type of episode, nor any significant increase in the use of the IDB as an external lender of last resort. While these factors may regain importance, under current conditions there is no doubt that the differentiating factor explaining the strategic relationship between multilaterals and Mexico is the value created by their nonfinancial contribution.[44] Over the last few years, multilaterals have adopted a variety of strategies in their work with Mexico, anchored in the creation of attractive, differentiated products devised in conjunction with line ministries, which offer tangible advantages for improving the quality of expenditure and connect sector-level and Finance Ministry incentives.

2.31 The World Bank's 2001 evaluation (*Mexico: Country Assistance Evaluation*, June 2001—OED) concluded that the fundamental challenge was to bolster its nonfinancial value-added. An analysis of subsequent *Country Partnership Strategies* makes it possible to reconstruct a sequence for development of a technical advice product that made the World Bank's Mexico program the largest in its global portfolio in fiscal 2006, with US$1.8 billion in lending.[45] According to World Bank strategy papers, the key steps were as follows:

Step 1: Highly selective definition of relevant niches for financial and nonfinancial services, stressing the creation of a long-term strategic partnership.

Step 2: Establishment of permanent teams of experts and concentrated investment of grant resources in the selected sectors.

Step 3: Engagement in, and intellectual contribution to, policy debate and decision-making in the selected sectors, tailoring advisory products to the specific conditions in the Mexican market.

Step 4: Negotiation of loans in the selected areas, in this case particularly policy loans, ensuring a prominent presence in the sector based on the technical credibility earned.

2.32 The World Bank's experience confirms that a market niche development strategy to grow a lending portfolio is feasible in a market such as Mexico's. In economics, the term "market niche" means a specific segment of the market that represents a good business opportunity but is not being reached by the regular supply of products or services generally on offer.[46] There are two critical considerations in developing a market niche strategy: the size of the market segment and the differentiation of the product on offer. The table below compares the IDB's positioning to that of the World Bank in its main areas of engagement, based on a combination of the program's financial weight in the respective subsector and the availability of a differentiated technical backstopping advice product.

Strategic position of the IDB and the World Bank: A comparison

Product - Intervention area	Financial weight in subsector	Differentiation of technical offering
IDB		
Oportunidades – poverty	√	√
Procampo – rural development	√	
Community education - education		
Active policies - labor market		
FORTEM - states and *municipios*	√	
Water and sanitation	√	
World Bank		
Educational management - education	√	√
Finance and growth - competitiveness	√	√
Environmental management policies -environment	√	√
Water and sanitation		

Source: Compiled by the authors.

2.33 The Bank may have established a prominent position and a market niche in the case of the *Oportunidades* program, in an area that is particularly relevant to the need to target and better redistribute social expenditure. Nonetheless, this market position gain has yet to translate into the formation of permanent teams of experts, development of a differentiated product with durability prospects, or Bank delivery of technical advisory products with ownership assumed.

III. THE PROGRAM

3.1 This section describes the Bank's program with Mexico executed between 2001 and 2006. Inasmuch as the program depicts the tenor of the Bank's country engagement, we analyze also the extent to which the support provided is consonant with the Paris Declaration principles to which the Bank and Mexico subscribe, as a starting point for the outcomes evaluation.

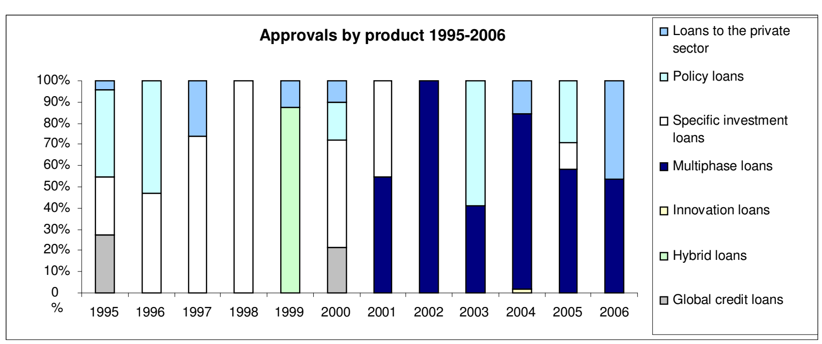
A. The financed program

3.2 In terms of the strategic areas defined in the programming, 65% of Bank funding approved between 2001 and 2006 was for interventions in the social and poverty domain, through investment loans exclusively. Funding for the competitiveness area (lowering barriers to efficient private-sector development) was provided mostly through policy loans (PBLs); investment and private-sector lending accounted for 25% of the resources. The remaining 12% of approvals were for decentralization support, entirely through investment project loans.

Strategic area	Investment loans		Policy loans		Private- sector loans		Technical cooperation		MIF TC		MIF loans		Small Projects		Total		%
	US$000	No.	US$000	No.	US$000	No.	US$000	No.	US$000	No.	US$000	No.	US$000	No.	US$000	No.	
Poverty/social	3,617,400	8	-	-	-	-	6,190	22	6,935	8	5,250	1	7,474	13	3,643,249	52	65%
Competitiveness	110,000	2	900,000	2	255,000	3	1,651	18	40,328	27	5,075	1	-		1,312,054	53	23%
Decentralization	650,000	3	-	-	-	-	738	2	-	-	-		-		650,738	5	12%
Modernization of the State	-	-	-	-	-	-	450	1	-	-	-		-		450	1	0%
Integration																	0%
Total	**4,377,400**	**13**	**900,000**	**2**	**255,000**	**3**	**9,030**	**43**	**47,263**	**35**	**10,325**	**2**	**7.474**	**13**	**5,606,492**	**111**	**100%**

3.3 In terms of lending products, the bulk of the Mexico portfolio in 2002-2006 consisted of investment loans (78% of resources, 13 projects), followed by PBLs (16% of total lending) and a very low private-sector lending share (5%). The investment-lending share is up from the previous cycle (from 65% to 80%), while the PBL share has dropped from 30% to 16%.

3.4 Regarding the use made of the different products, the portfolio has become less diversified and more concentrated in multiphase loans. The latter provide the Bank and the country the



chance to work long-term in a sector using a phased execution approach that facilitates the necessary adjustments and makes for a more flexible program. These instruments also shorten the time needed for second-phase design and approval, which is done through simplified processes. From the government standpoint, a proliferation of these instruments reveals a preference for lower credit fees and greater flexibility for in-process changes in the terms of the relationship. Since 2006 there has been an unprecedented revival of the private-sector window portfolio, which historically has been modest. The fact that this trend was confirmed in 2007 provides a positive signal on the possibilities for scaling up that lending, considering the size of the market for private-sector finance.

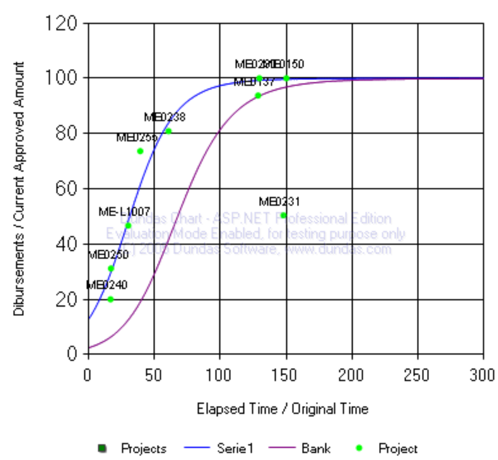
3.5 As for the Bank's nonlending products (NLPs), one third supported macroeconomic research as an input for the Report on Economic and Social Progress in Latin America (IPES) and the country strategy. Of the other products, 34% mainly funded social project and program evaluations[47] and the other 25% was for research on regional integration issues, mainly relating to NAFTA.[48] The number of NLPs approved for Mexico is significantly smaller than for other countries with similar portfolios (Argentina, Brazil, or Colombia).

B. Portfolio efficiency

3.6 This section looks at the efficiency with which the country program was executed, in terms of financial product delivery times. Project preparation times and eligibility conditions, as well as disbursement conditions, affect projected funds flows for the interventions and hence their returns. As discussed in more detail below, the times it takes to prepare a project, reach disbursement eligibility, and release the first disbursement have not improved over the immediately preceding cycle (1995-2000), whereas implementation times, measured by the disbursement rate relative to the original timeline, come close to optimal performance.

3.7 The *average project design time* (from profile to approval) is 12 months, but there are differences between different product types: multiphase projects were designed in eight months on average, PBLs took 12 months, and investment projects 18 months.[49] In all products, a long time elapses between *approval* and *eligibility for first disbursement*—12 months on average,[50] which is three months longer than in the previous cycle (1995-2000). These operations processing times are longer than the Bank average of nine months.

3.8 Once the preparation stage is complete and a loan has been declared eligible for disbursement, *disbursement performance* has been efficient. An analysis of that performance at end-2006, taking as a measure the percentage of loan proceeds disbursed against the planned timeline for



their execution in the project design, shows a positively performing portfolio, adhering very closely to what was programmed. This situation—unique compared to other countries evaluated—is largely attributable to efficient execution of programs without ex ante Bank supervision.

C. Contribution to fulfillment of the Paris Declaration principles

3.9 Mexico and the IDB subscribe to the Paris Declaration principles. An analysis of the Declaration's indicators reveals Mexico's high degree of fulfillment of the indicators within its control. The following table summarizes the findings of the analysis undertaken for the present evaluation, indicating how consistently the Bank has supported Mexico in fulfilling the Declaration's commitments in its country work during this most recent programming period.

Consistency of the IDB program with Paris Declaration commitments (2010)

Indicator		Consistent	Partially consistent
Ownership			
1	*Countries have operational national development strategies*	*	
Alignment			
2	*Country procurement and public financial management systems are reliable*		*
3	*Aid flows are aligned on national priorities*	*	
4	*Support for capacity strengthening*	*	
5a	*Use of country financial management systems*		*
5b	*Use of country procurement systems*		*
6	*Avoidance of parallel project implementation units*	*	
7	*Aid disbursements are more predictable*	*	
8	*Aid is untied*	*	
Harmonization			
9	*Use of program-based approaches*		*
10	*Use of shared analysis among multilaterals*		*
Managing for results			
11	*Performance monitoring through the country's results-oriented frameworks*		*
Mutual accountability			
12	*Mutual assessment of progress in implementing aid effectiveness commitments*		*

3.10 The Bank's program has been consistent with the *ownership* objective and largely consistent with the objective of *aligning* the program on the country's priorities and budgetary management. On issues relating to *harmonization*, IDB support has been partially consistent with a program-based approach and coordination among multilaterals. With regard to the *managing for results* and *mutual accountability* objectives, the evaluability features of the program and of individual projects do not offer an image consonant with those commitments. With perspective, our analysis points up a number of areas on which the Bank could focus to act more in consonance with these principles, particularly in the case of a country with Mexico's capacities: (i) consistent use and transfer of responsibilities for fiduciary management and the national governance system, and (ii) consistent use and bolstering of the country's results-based management and performance monitoring systems with a program-based approach.

3.11 With regard to the delegation of *fiduciary management*, although efforts have been made in the last few years, arrangements vary from one project to another, and it has been impossible to corroborate the existing rationales for the differing treatment of government entities that are subject to the same country internal control system. Thus, while large projects such as *Oportunidades* or FORTEM have received treatment that has been pioneering for the Bank, involving full delegation of ex ante fiduciary management in investment projects, other operations, such as the Community Education Program or labor market projects, have been subject to tighter direct controls. In this regard, the "New Framework for Supervision of Fiduciary Aspects" initiative proposed in November 2007 signals a positive change, though the view of this evaluation is that these measures ought to have been consistently applied to the whole portfolio during the previous programming period.

3.12 With regard to support for strengthening the country's *results-based management systems,* over the period examined here the Bank played very little part in implementation of the Presidential Targets System but has had a more active presence since 2005 in promoting results-based budget management by the government. To follow up this line of work, a technical cooperation operation for development effectiveness (PRODEV) was approved in mid-2007, which is designed to help further the transition to a budget management system that incorporates information on outcomes and to solidify a strategic partnership between the Bank and the country in this domain.

IV. PROGRAM OUTCOMES

4.1 This chapter assesses the country program outcomes and the value added to them by the Bank. This being an evaluation of outcomes, the analysis defines value-added rigorously, as enhancing outcomes of interventions in the country, achieved when the authorities assume ownership of the advice provided by the Bank. The following tools were used to analyze value-added in this evaluation: (i) definition of crucial elements for achieving outcomes in each of the interventions, based on their evaluability analysis; (ii) review of documentation on the delivery of advisory services or nonlending products by the Bank, based on managerial documentation; (iii) validation of the use of the advice and the tie-in to decision-making, based on information provided by the authorities involved or by the Management of the Bank; and lastly (iv) a cross-analysis of the content of the advisory services provided by the Bank with the outcomes attained in each of the interventions.

4.2 The analysis findings offer an answer to the fundamental question as to whether there is empirical evidence that the Bank added value to program outcomes and, if so, how and under what conditions. In contrast, and for learning purposes, we note also cases in which, according to the documentary evidence, the Bank's technical advice did not put a project on an outcome-enhancing track. This evaluation credits only value-added that contributes to outcomes. The following paragraphs briefly examine the Bank's actions in each of the sectors specified in the country strategy. The detailed evidence and data underpinning the opinions expressed can be found in the support documents appended to this report.

A. Social development and poverty reduction

4.3 The Bank's strategy for the period reviewed here is based on a broad-ranging diagnostic of Mexico's poverty situation and the relative inefficiency of certain social policies. The strategy proposal reflects this by including actions across virtually the entire spectrum of targeted sectors, to help:

a. Reduce extreme poverty, enhance equity, and make progress toward greater equality of opportunities (paragraphs 4.8 and 4.9).

b. Improve the efficiency of public education services delivery and target these services more equitably, particularly at the secondary school level (paragraph 4.10).

c. Increase the efficiency and quality of health and social protection services (paragraph 4.11).

d. Make the labor market more flexible and pursue social security reform (paragraphs 4.12 and 4.13).

e. Develop microenterprise (paragraph 4.14).

4.4 The Bank acted in the first of these five focus areas through a set of loans aimed at poverty reduction, notably *Oportunidades* (ME-0244 and ME-L1007), *Procampo* (ME-0213), and *Habitat* (ME-0255). In the second area, the Bank's action was tangential, through the *Community Education* program (ME-0238), a satellite public education policy program. In the third domain, the health sector, the Bank did not engage in the supply-side issues mentioned in its strategy, although it did help with demand stimulation for populations living in extreme poverty, in the framework of the *Oportunidades* program. In the fourth action area, the labor market, the *Training and Employment Support* and *Competencies-Based Human Resources Development* (ME-0233) programs focus on active employment policy issues other than the labor market and social security reform actions initially proposed. Lastly, in the microenterprise sphere, the Bank did not approve the programmed *Microenterprise Assistance* loan but did engage in that sector through the MIF and the Small Projects Facility. In the following paragraphs we analyze program outcomes and the value-added the Bank contributed in sectors in which it did engage, approving programs during the period evaluated here.

1. Social development and poverty

4.5 The family of pro-poor programs (*Oportunidades, Procampo,* and *Habitat*) involves an unprecedented concentration of Bank resources on issues relating directly to reducing rural and urban poverty alike. During the period examined here the Bank added its support to programs which have been top priorities for the Mexican government, as indicated by the fact that all three programs are included in the Presidential Targets System for 2001-2006.[51] As discussed in detail in Support Document A1 of this report, the three cases involve programs wholly designed by the Mexican government for which the Bank has provided a minority share of funding; but, particularly in the case of *Oportunidades*, Bank staff can be credited with having contributed a measure of tangible technical value-added.

4.6 The *Oportunidades* program (ME-0244, US$1 billion, and ME-L1007, US$1.2 billion) is an example of a relevant strategic partnership between the Bank and a member country. The documentation analyzed shows that the Bank has contributed a measure of value-added, particularly in work to maintain that program's operating rules and sharpen its targeting as its coverage expanded, and support for its proposals on impact evaluation for its results-based management.[52] As discussed below, while it is possible to document the Bank's outcome-associated technical contribution during the discussion of the first loan, it is hard to isolate value-added at the time of the proposal for the program's second stage designed in 2005. To look at outcomes, this analysis starts from the objectives defined in the loan documents and the associated indicators and metrics; referencing these we evaluate the outcomes obtained and the value added to them by the Bank.

Outcome synopsis: *Oportunidades*

Operation design				OVE evaluation	
Objectives (ME-0244; ME-L1007)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Improve food consumption, health, and education opportunities for families living in extreme poverty (direct effects).	√	√	√	√	√
Increase human capital accumulation to reduce the intergenerational transmission of extreme poverty (intermediate effects).	√	√	√	√	√

4.7 *Oportunidades,* one of the most evaluated projects in existence, is recognized as a benchmark for poverty reduction policy in Mexico for its redistributional efficiency alone.[53] In fact, the precision of its beneficiary targeting is unmatched in any previous food subsidy or other government program.[54] Official reports on the program leave no doubt as to its relative resource-distribution efficiency: increased coverage and sharper targeting.[55] This program, in which the Bank has had a minor participation, has dispensed subsidies to populations suffering from food poverty with over 65% accuracy in beneficiary selection and an inclusion error of less than 10%.[56]

Food poverty	Reduction attributable to *Oportunidades*		
	2002	**2004**	**2006**
Nationwide	-1.0	-1.2%	-1.7%
- Urban	0.0%	-0.3%	-0.3%
- Rural	-2.6%	-2.6%	-4.0%
Regions			
North	-0.3%	-0.8%	-0.7%
- Urban	0.0%	-0.3%	-0.1%
- Rural	-1.4%	-2.7%	-2.8%
Center	-0.8%	-1.2%	-1.5%
- Urban	0.0%	-0.3%	-0.5%
- Rural	-2.3%	-2.8%	-3.3%
South	-2.2%	-1.5%	-3.2%
- Urban	-0.1%	-0.6%	-0.2%
- Rural	-3.6%	-2.3%	-5.3%

Source: OVE analysis, from INEGI data.

4.8 The evaluation team found documentary evidence of a technical contribution by the Bank to this program, particularly in its assistance for maintaining the program's operating rules, including a scoring system for well-targeted distribution of resources. The plausible reduction in inclusion error before urban population groups became *Oportunidades*-eligible and in the virtual doubling of the program's coverage over the last six years entail a significant fiscal saving.[57] Sharper targeting has been decisive in achieving direct program effects in the form of higher incomes[58] and food consumption[59] as well as improved education and health indicators among the beneficiary population. A comparison, by regions, of the distribution of food poverty with and without the program shows a reduction of poverty in the southern states that is significantly greater than the national average, thus confirming the program's net north-to-south redistributional effect.[60]

4.9 The program beneficiaries' fulfillment of education- and health care-related conditions has had an impact on the sector's main indicators, with infant mortality falling by 11% and secondary school attendance rising by an average of 10%, in addition to a smaller impact on primary school attendance.[61] Other studies identify possible positive externalities captured by the program in terms of development of local markets,[62] increases in migration and remittances,[63] and the benefiting populations' resilience to unexpected exogenous shocks.[64]

4.10 Nonetheless, the intermediate effects in the form of human capital accumulation to reduce the intergenerational transmission of poverty—the core premise for the transitory character of *Oportunidades*—are not assured, since they depend on other programs and policies forming part of a cohesive strategy and a sustained economic growth environment.[65] *Oportunidades* unquestionably has generated demand for health and education services, but this has not been matched by an improvement in the quality of services on offer to the most deprived population groups. The challenge going forward, and for maximizing *Oportunidades'* intermediate effects, is to adapt health and education policy or production development policies to tap the captive market created by fulfillment of the program's conditionalities.

4.11 The *Procampo* program (ME-0213, US$500 million) is another example of a relevant strategic partnership with the country, in a program wholly designed by the Mexican government. As in the program discussed above, and for all the financial supports to Mexico, the loan proceeds do not add to budget lines for ongoing Mexican government initiatives. Unlike that previous case, however, this evaluation has not found evidence of a distinguishable Bank technical contribution to elements that are crucial for the good operation of the program to deliver its outcomes. The program analysis focused on the objectives set out in the loan document and the respective indicators and metrics, which OVE looked at to assess whether the outcomes sought were delivered and whether the technical assistance provided added value to them.

Outcome synopsis: *Procampo*

Operation design				OVE evaluation	
Objectives (ME-0213)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Reduce the incidence of poverty among small farmers (intermediate effect).	√	√			
Improve productivity and increase agrifood exports (direct effect).	√	√			

4.12 The *Procampo* program was created in 1994 as a temporary support to farmers to help them cope with the envisaged liberalization of the agriculture sector under NAFTA. It was the Bank's 2001 program that set as a core objective the reduction of poverty incidence among farmers, but the Bank did not succeed in adding value by introducing any specific change in *Procampo's* previously defined operating rules or specific transfer criteria so as to better target resources. Consequently, as far as *Procampo's* intermediate poverty reduction effect is concerned, the evaluation found that the program targeted 30% of its resources on population groups suffering from food poverty, with an inclusion error close to 50%.[66] Unlike *Oportunidades*, the analysis of *Procampo* finds no evidence of north-south redistributional effects.[67]

Food poverty	**Reduction attributable to *Procampo***		
Nationwide	**2002**	**2004**	**2006**
Rural	-1.3%	-1.2%	-0.8%
Regions			
North - Rural	-1.4%	-2.0%	-1.3%
Center - Rural	-1.2%	-0.5%	-0.9%
South - Rural	-1.4%	-1.8%	-0.7%

Source: OVE analysis, from INEGI data.

4.13 With regard to the productivity goal, as the reinvestment rate of the transfers received has been relatively low, the desired outcomes of increasing crop productivity and marketing do not appear to have been achieved. The *Procampo-Capitaliza* segment, the main objective of which was to provide beneficiaries with advance access to funds to capitalize their production units, has not achieved good outcomes either.[68] Consequently, creation of a system of incentives to raise productivity and switch to potentially more profitable crops remains a challenge for this sector.

4.14 The *Habitat* program (ME-0255, US$350 million) represents a relevant strategic partnership around the Mexican government's main vehicle to combat urban poverty. *Habitat* is a regular government program to which the Bank added its support in 2004. This evaluation has found no evidence of technical value added by the Bank as far as *Habitat* results-based management decision making is concerned. The premise for this multiphase program was that the findings of an evaluation of the first 18 months of execution would serve as inputs and triggers for the following phase. But, judging from the project documentation, the Bank's contribution of an evaluative design to make this exercise viable is debatable. The objectives set out in the *Habitat* loan document, together with the corresponding indicators and metrics, and findings as to achievement of the anticipated outcomes and the value added to them by the Bank, are shown below.

Outcome synopsis: *Habitat*

Operation design				**OVE evaluation**	
Objectives (ME-0255)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Expand social infrastructure services in marginal urban areas (direct effect).	√	√	√	√	
Reduce poverty and improve the living conditions of the beneficiary population (intermediate effect).	√		√		

4.15 In terms of *Habitat's* direct effects, this evaluation finds that the original program design specified a careful mechanism for targeting zones in most need of assistance. Data from the Ministry of Social Development (Sedesol) show that 77% of the program's investments are in communities classified as disadvantaged and very disadvantaged. Building on good targeting, according to the evaluations done, the outcomes obtained in terms of expansion of infrastructure services were as expected for this type of intervention and equivalent to outcomes in similar Bank-funded programs: greater access to sewer systems than in communities not assisted by the program, and marginal changes in water supply access. Access to electric power did not increase as a result of the program, though this might be explained by the high level of coverage at the outset.

4.16 The evaluations done do not provide data on the intermediate effects expected from the program. For example, its effects on property values were not measured, the employment and income outcomes cannot be considered conclusive, and there is no information available on the program's specific outcomes for vulnerable groups, impact on maternal and child health, or environmental outcomes, as envisaged in the design. In the absence of basic data, a Bank value-added contribution to results-based management of the *Habitat* program—the rationale for its involvement by way of this phased program—has not materialized.

2. Education

4.17 Apart from the effects of an increase in demand associated with the *Oportunidades* program, the Bank's action in the education sector is confined to the *Community Education Program* (ME-0052, US$210 million). In the face of the challenge of enhancing equity in the supply of public education services in Mexico, which have been gradually decentralized under an arrangement of transfers to the states, this program has simply added to those ongoing efforts. Given their scope, it is impossible to isolate the program's impact. As explained in Support Document A2 of this report, this is a routine budgeted program in which partnering with the Bank did not help deliver outcomes.

Outcome synopsis: Community Education Program

Operation design				OVE evaluation	
Objectives (ME-0052)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Improve the coverage, quality, and efficiency of community education for low-income residents of isolated areas not served by the formal education system.	√		√		

4.18 As conveyed in its objective, a fundamental element for achieving outcomes in the Community Education Program is the capacity to respond flexibly to a changing target market, ensuring complementarity with the Ministry of Education and with state government education services, so as to keep the program operating in remote communities where it is still needed. The available documentation indicates that the Bank has not added value in terms of aiding the necessary adaptive management of the program, mainly for two reasons: (i) an emphasis on coverage indicators over targeting needs in a subsidiary relationship with the rest of the public education supply; and (ii) relative inflexibility in the (untimely) application of the financing matrix that made it impossible to fund a number of items that the executing agency considered necessary to achieve the outcomes.[69]

4.19 Information on the program outcomes shows that it was impossible to closely manage the necessary targeting of underserved localities since the requisite data are not available.[70] In terms of the quality of education delivered, the improvements recorded do not meet the target of a statistically significant 7% improvement in standardized test scores for primary students; the point estimate gives increases below 1%, which are not statistically significant.[71]

3. Labor market

4.20 The set of employment-related programs *(Labor Market Modernization, Training and Employment,* and *Competencies-Based Human Resources Development)* continue a more than 20-year tradition of multilateral presence in this sector. Nonetheless, as discussed in Support Document A3 of this report, the Bank's program during the period examined here departed from policy issues to concentrate more on specific intermediation and training projects with relatively limited coverage. The Bank's technical value-added to outcomes is down accordingly from its documented late-1990s contribution.

4.21 For outcome analysis purposes, this section focuses on the original objectives of the *Labor Market Modernization* (ME-0118, US$450 million), *Training and Employment (PACE)* (ME-0233, US$300 million), and *Competencies-Based Human Resources Development* (ME-0250, US$50.4 million) programs, namely:

Outcome synopsis: Employment

Operation design				**OVE evaluation**	
Objectives	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Consolidate active labor market policies and develop employment policy planning and delivery capacity (ME-0118).					
Promote (a) employability; (b) mobility; and (c) workforce productivity (ME-0233; ME-0250).	(a) √ (b) (c)	√	√	√	

4.22 The outcomes delivered in the area of *consolidating employment policies* have been limited, in a setting of substantial budget cuts.[72] The Bank's involvement has not elicited changes or adjustments in employment policy such as could overcome the challenges diagnosed, with a long-range perspective, and tailor policies to the different production fabrics and employment markets in northern and southern Mexico. As for value added by the Bank, there has been a net loss with respect to what the government credited for the previous cycle, the value-added contribution having been limited to support for the use of active labor market policy instruments, with a neutral showing in terms of employment policy making or debate and even less in terms of a broader employment policy.

4.23 This evaluation credits the *improved employability* outcomes given the programs' reach and job placement rates. Targets in terms of number of beneficiaries served were achieved and the average placement rate was only slightly below target. In contrast, the *intermediation systems* outcomes have not shown any significant coverage or placement impact. The new information tools (*Chambatel, Chambanet*) and employment exchanges have not achieved their targets of raising the placement rate of job seekers to 45%. During the first phase, for example, the Labor Exchange *(Bolsa de Trabajo)*—the main intermediation instrument—has found jobs for 30% of candidates.

4.24 For the *training* component in the employment support program (PAE), OVE performed an impact evaluation in 2005. Its findings show that, overall, the program has succeeded in raising employment rates, particularly in the modality of in-service training in large firms. There were other positive outcomes in the form of increases in formal employment. The placement outcomes sought with the *in-service employment training program* did not materialize.[73] The outcomes of *productivity improvement through training programs in microenterprises and small businesses (PAC)* have been constrained by major changes made to the program's focus, in which environment the Bank was unable to institute an effective technical dialogue. According to the original diagnostic, there was sufficient installed capacity to serve 50,000 firms a year; the goal was to gradually increase this to 100,000. The phase I target was changed in April 2003 to 13,041 firms; the program ultimately served only 5,694.

4.25 In the area of *job skills certification* through the application of competencies standards, the Bank picked up a previous World Bank-funded program; neither the IDB's rationale for participating in the project nor the value it added to revamp the original scheme were clear.[74] Some key drivers of the success of an intervention of this type, such as securing effective private sector leadership in standards setting, assuring effective adoption of the standards by the various upper secondary education institutions, and improving efficiency in the standard-setting and certification process, were not built into the Bank's proposal to make the outcomes deliverable.

B. Integration

4.26 In the regional integration domain, the Bank's strategy focused on *supporting the Puebla-Panama Plan (PPP)* as an innovative strategy to raise workforce productivity and help alleviate poverty in Mexico's southern states through initiatives for development and integration with Central America (paragraph 4.14). The Bank's lending program with Mexico did not follow through on support for the PPP as envisaged. Absent any such programs, no outcomes can be clearly attributed to the Bank's strategy with Mexico in this sphere.[75]

C. Modernization of the State and decentralization

4.27 The Bank's strategy is anchored in a general diagnostic of Mexico's challenges for modernization of the State, including aspects relating to all levels of government. Pursuant to that diagnostic, the proposed strategy included actions to help:

a. Improve the quality, transfer, and efficiency of government operations and delivery of public services (paragraph 4.16).

b. Modernize the justice system at the federal, state, and municipal levels (paragraph 4.17).

c. Improve the regulatory framework for privatization and decentralization processes in key sectors for the economy (paragraph 4.18).

d. Strengthen intellectual property and intellectual property rights regulation (paragraph 4.19).

e. Further decentralization, by revamping the legal and jurisdictional framework and strengthening tax, financial, and fiscal management in the states and *municipios* (paragraph 4.21).

4.28 The Bank's program implemented some actions in the fifth of those five action areas, with programs for *state and municipal strengthening (FORTEM)*. No Bank funding was furnished for the envisaged support for regulatory reform to enable policy and tax responsibilities to be delegated to subnational governments, modernize the justice system, or give incentives to competition in privatization processes. The outcomes of Bank programs in areas in which it did engage are analyzed below.

1. Strengthening of states and *municipios*

4.29 The *State and Municipal Strengthening Program (FORTEM)* fortifies a long-term strategic partnership with the government public works investment bank, Banco Nacional para las Obras Públicas (Banobras). Although the strengthening of subnational governments is a major challenge, particularly in terms of increasing transfers of resources, powers, and responsibilities, the program's low coverage, measured by the number of states and *municipios* assisted, makes the relevance of the strengthening objective debatable.

4.30 The individual FORTEM programs (ME-0208, US$800 million; ME-0231, US$300 million; ME-0256, US$200 million) were conceived as a hybrid program to be followed by a three-phase program, for a total of US$1 billion.[76] As discussed below, the Bank has not contributed value-added to bring about changes in lending policies and practices for Banobras projects, which show a bias towards lending to subnational governments that offer low financial risk rather than scaling up lending to the neediest states and *municipios* as the design proposed. With regard to state and municipal capacity strengthening, the Bank's value-added contribution to seeking the best institutional option for capacity-development advising is debatable. The objectives, indicators, and metrics defined for these programs, together with OVE findings on their outcomes and the value added to them by the Bank, are analyzed in detail in Support Document C1 of this report and summarized in the following table.

Outcome synopsis: FORTEM

Operation design				OVE evaluation	
Objectives	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Finance public works projects yielding high social returns in states and *municipios* (ME-0256).	√	√	√		
Support the decentralization process, strengthening and improving subnational government management capacity, and improve Banobras operational efficiency (ME-0208-ME-0231).	*	*	*		

* Indicators, baselines, and targets were defined only for a pilot plan in disadvantaged *municipios*.

4.31 The *public works financing* outcomes fell short of the anticipated levels.[77] The aim of giving credit market access to subnational governments that lacked such avenues was not addressed by the FORTEM operation. In fact, the program has shown a preference for financing investment projects in certain large states and *municipios* with low marginality levels. As for *institutional strengthening*, only five state governments and four municipal governments participated in the first program (ME-0208). In the second loan (ME-0231), 10 *municipios* with medium or high marginality levels were to participate in a pilot institutional strengthening plan. The program did not achieve these targets. With regard to the *internal restructuring of Banobras*, in particular, for which there were more than 50 proposed reform measures, there is no evidence that the modernization activities undertaken have helped enhance the quality of Banobras services or change its market position and its capacity or development of any potential comparative advantage as an institution-strengthening agent.

D. Barriers to private-sector competitiveness

4.32 Based on a cursory diagnostic that looked at barriers to competitiveness and other aspects relating to public services, the Bank's strategy envisaged unprioritized actions in various sectors to help:

a. Develop the financial sector by fostering competition between banks and improving the efficiency of the financial public sector and capital markets (paragraph 4.22).

b. Expand the housing market to lower-income groups (paragraph 4 23).

c. Reform the energy sector and open up electric power generation and distribution to private investment (paragraph 4.24).

d. Reform the transport sector, boosting private-sector participation in operation and construction (paragraph 4.25).

e. Pursue the sustainable management, use, and efficient distribution of water resources (paragraph 4.26).

f. Promote sustainable natural resource management and planned urban development (paragraph 4.27).

4.33 The Bank worked in the first of these originally planned action areas through a set of operations to support consolidation of the financial system (ME-0277, ME-0243, ME-0259, and ME-0240), and in the second area through a program to support the housing sector (ME-0137). In the third and fourth areas, Mexico requested Bank support, particularly through the private-sector window, for electric power generation projects, but not for power sector reform and liberalization. The Bank had no engagement in the transport sector over the period examined in this evaluation.[78] It worked only tangentially in the water resources area, backing a number of projects to expand water and sanitation services (ME-0150, ME-0212) but no water resources management operations. The Bank did not engage in any specific operations for the sustainable management of natural resources.

2. Financial sector

4.34 The family of programs supporting the financial public sector and financial market development, with investment projects as well as policy reform and MIF projects, distinguishes the financial sector, and particularly government-owned development banks, as a major activity sector for the Bank. As described in detail in Support Document C2 of this report, this is a sector in which the Bank added value to several outcomes, primarily in the process of creating Financiera Rural or the consolidation of Bansefi.[79] But, apart from the value added in these specific subsectors, there is no evidence of substantive technical supports or contributions as catalysts for development bank reform or financial market deepening. There is therefore no evidence of the Bank's having focused its efforts on the correction of market failures or delivery of financial services to hitherto excluded sectors.

4.35 To structure the analysis in terms of outcomes, this section focuses on the objectives of the following programs: *Consolidation of the Rural Financial System* (ME-0243, US$300 million), *Consolidation of the Financial System* (ME-0259, US$600 million), *Financing for Small and Medium-Sized Exporters* (ME-0240, US$100 million), and MIF projects (TC-0109022, ME-M1012, ME-M1004, and ME-M1017, for a total of US$7 million), as follows:

Outcome synopsis: Financial sector

Operation design				OVE evaluation	
Objectives	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Expand and consolidate the supply of rural finance services by reforming Financiera Rural (ME-0243).	√	√	√	√	√
Increase access to financing for small and medium-sized export enterprises (ME-0240).	√	√	√		
Promote the development of savings and loan institutions for the low-income population (MIF).	√	√	√	√	
Deepen financial markets and expand bank lending to the private sector (ME-0259).	√	√	√		

4.36 The outcomes of *expansion of rural finance*, and Financiera Rural (FR) reform in particular, show a positive trend, even though that operation's outcome targets are for 2008. With regard to the financial situation of FR, its indicators are sound and superior to those of Banrural, for example.[80] This evaluation found documentary evidence that the IDB, along with the World Bank, has added value in two fundamental aspects of the reform, helping to: (i) secure consensus on Banrural's liquidation as a process trigger, and (ii) drive the Financiera Rural reform process by way of the loan conditionalities.[81]

4.37 The outcomes of *access to financing for small and medium-sized export enterprises* are not available because at the time of this evaluation that operation had not begun executing. The evaluation questions the program's market-deepening outcome orientation: it proposes to work with a sample of 300 firms that have already used Bancomext the previous year and its monitoring indicators do not provide for inclusion of new enterprises without access to credit.

4.38 The outcomes of the *development of saving and loan institutions for the low-income population* and *consolidation of Bansefi* pursued by three consecutive MIF operations have been as envisaged.[82] In financial terms, Bansefi began posting surpluses and healthy indicators, notably the development bank sector's highest operational efficiency ratio and lowest average cost of funds ratio. The consolidation of this bank as a catalyst for efforts to reach vulnerable population groups in a financially sound way and using market mechanisms, represents MIF value-added to outcomes in this sector.

4.39 Outcomes attributable to the Bank's programs for *deepening financial markets* and *scaling up bank lending to the private sector* are more debatable. Since the 1995 crisis, policy reform programs have been funded to revive and develop the banking sector.[83] The value added by the Bank in this program is debatable since it is really only recognizing countries' own reform efforts, in exchange for which it provides an unrestricted loan.

3. Housing

4.40 With the *Housing Finance* program (ME-0137, US$505 million) the Bank added to a wide range of Mexican government initiatives to improve the efficiency of the nation's housing market.[84] As discussed in more detail in Support Document C3 of this report, this program involves joining forces with similar government programs in which the Bank has added value for more efficient management of the housing market, but has not added value in terms of developing a finance product tailored to lower-income population groups, which defined its specific market segment. The program's aims, indicators, metrics, outcomes, and value-added contribution are summarized below.

Outcome synopsis: Housing

Operation design				OVE evaluation	
Objectives ME-0137	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Improve the efficiency of Mexico's formal housing finance system.	√		√	√	√
Help expand the housing finance market to poorer segments of the population.[85]	√		√		

* The indicators and targets for the second objective were incorporated in the PPMR.

4.41 With regard to *efficient operation* of the housing market, the Bank's loan served to finance contingent liabilities arising from Mexico's former Bank Housing Finance and Operations Fund (FOVI), consistent with the new lending product of the mortgage finance company Sociedad Hipotecaria Financiera (SHF—PROSAVI), thus helping to improve a number of efficiency indicators.[86] As for the *expansion with equity* aim, in its original design the Bank's loan was preferentially targeted to low-income households, but the program encountered slim demand and intermediaries were reluctant to lend to low-income applicants. Although the targeting of subsidies on the poorest households was the program's defining feature at the outset, there is no documentary evidence that the Bank contributed analytical value-added to elements such as providers' opportunity costs or transaction costs, and demand-side risks under the incentive scheme proposed by the project.[87]

4. Water and sanitation

4.42 During the period encompassed by the country strategy the Bank approved an operation entitled *Institutional Development and Sustainability of Water Supply and Sewerage Services in Rural Communities II* (ME-0212, US$150 million) which marks a continuation of Bank support for the *PROSSAPY* program approved in 1998 (ME-0150, US$310 million).[88] Owing to the low disbursement level of the project approved during this period, its outcomes are difficult to assess. Nonetheless, it is possible to analyze outcomes and value added by the Bank for *PROSSAPY*, and also the consistency of the second-phase design approved in 2005. For value-added assessment purposes it is important to note the Bank's proposal to explicitly help sharpen the programs' targeting to reach the most underserved populations. However, as discussed in more detail in Support Document C4 of this report, the Bank has been unable to demonstrate a value-added contribution through a change in the incentives system of the institutions involved, to redirect funding towards works consistent with that intent. The following table summarizes the objectives with their indicators and metrics for the loans to *PROSSAPY,* the outcomes obtained, and their value-added.

Outcome synopsis: Water and sanitation

Operation design				OVE evaluation	
Objectives ME-0150, 1998, and ME-0212, 2005	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Improve access to water and sanitation services in rural communities, prioritizing poorer segments of the rural population.	√	√		√	
Promote reform of the rural water and sanitation system.	√		√		

4.43 In terms of improving *access to water and sanitation services*, the findings of the OVE analysis of targeting in the first *PROSSAPY* program (ME-0150) reveal that the project addressed a low proportion of localities with high and very high marginalization levels—just 1.7% and 4.2%, respectively. Likewise, an analysis by locality size found that small localities—home to the bulk of the population without full access to basic services—do not predominate.

4.44 OVE also evaluated the impact of the project by measuring the coverage of piped water, sewerage and sanitation services in "treated" communities (assisted by the project) compared to nontreated communities.[89] The available data show a significant change in coverage between 2000 and 2005. According to the evaluation findings, targeting issues aside, the program is having a positive impact in the localities it does serve, in conjunction with a number of other public and private sector changes that are improving service coverage.

4.45 The *system reform* outcomes were not associated to specific activities financed by the first loan, nor did they have metrics with which to evaluate outcome attainment. According to the original reform design, the federal level was to assume a regulatory role and sector management would be put in the hands of the *municipios*, accompanied by a rate restructuring. This evaluation finds no evidence of a technical contribution by the Bank to analyzing the political economy constraints of a reform of this type.

5. Energy

4.46 Highlights in this Bank action area are thermoelectric power generation projects financed through the private-sector window (PRI) without sovereign guarantees (Bajío ME-0225, Vitro ME-0228, and Monterrey III ME-0229) and the energy efficiency program funded through the public-sector window. The table below summarizes the objectives, indicators, and metrics in the loan documents and the project outcomes with their value added. Support Document C5 of this report provides further details.

Outcome synopsis: Energy

Operation design				OVE evaluation	
Objectives	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Expand electric power generation for the national grid or to supply some industries in northern Mexico (ME-0225; ME-0228; ME-0229).	√	√	√	√	
Reduce energy consumption by developing a market for high-efficiency devices (ME-0204).	√	√	√	√	√

4.47 The outcomes of the portfolio of nonsovereign guaranteed electric power generation projects, to scale up *installed capacity* and thus supply some industries in northern Mexico, have been those anticipated. Pending the sector reform promoted in the Bank's strategy, this group of operations nonetheless runs the risk of favoring the dominant market position of the Federal Electricity Commission (CFE), which raises questions about internal consistency with this objective and, ultimately, the value added by the Bank to achieve it. With regard to the environmental impact of the thermal power plants, the preliminary findings of the study of the carbon footprint of the funded generating projects[90] show that thermal power plant emissions in Mexico fall into the typical range for generating plants that use clean fuels and improved technologies. Accordingly, it is considered that these projects marginally improve the carbon intensity of the Mexican power grid.[91]

4.48 The outcomes of the *energy efficiency* program (ME-0204, US$23.4 million) lay in creation of an incentives system and financing and development of energy service companies to promote the use of high-efficiency devices (motors, compressors, lights). The program has added value for adoption of a Mexican energy efficiency standard for three-phase induction motors that permits only high-efficiency electric motors to be put on the market. The cumulative saving in terms of both electricity consumption and electricity demand as an immediate outcome of the project was also measured: the operation produced a cumulative saving of 5,274 GWh in consumption and 270 MW in demand as at 31 October 2004.[92]

V. CONCLUSIONS AND RECOMMENDATIONS

5.1 The conclusions and recommendations are set out in the executive summary at the beginning of this report.

Support Document A1: Social Development and Poverty

1.1 The family of pro-poor programs (*Oportunidades*, *Procampo*, and *Habitat*) involves an unprecedented concentration of Bank resources on elements relating directly to the challenge of reducing rural and urban poverty. The programs to which the Bank added its support during the period examined in this evaluation are top priorities for the Mexican government, all three of them being included in the Presidential Targets System for 2001-2006.[5] As discussed below, these are programs designed entirely by the Mexican government in which the Bank's financial participation is small, but, particularly in the case of *Oportunidades*, Bank staff can be credited with having contributed a measure of tangible technical value-added.

1.2 The Oportunidades program (ME-0244, US$1 billion, and ME-L1007, US$1.2 billion) is an example of a relevant strategic partnership between the Bank and a member country. The documentation analyzed shows that the Bank has contributed a measure of value-added, particularly in work to maintain that program's operating rules and sharpen its targeting as its coverage expanded, and through support for its impact evaluation proposal for its results-based management.[6] As discussed below, while it is possible to document the Bank's outcomes-associated technical contribution at the time of discussion of the first loan, it is hard to isolate value-added at the time of the proposal for the program's second stage designed in 2005.

1.3 To look at outcomes, this analysis starts from the objectives defined in the loan documents and the associated indicators and metrics. Referencing these, we assess the outcomes delivered and the value added to them by the Bank.

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5 The Presidential Targets System established a system for continuous tracking of outcomes of programs designated as priorities by the Office of the President of Mexico for each of the ministries directly involved, for the 2001-2006 government term.

6 The administrative arrangements agreed upon for this investment program with the Government of Mexico also give the latter responsibility for ex ante fiduciary supervision. As noted in chapter III of this report, this has resulted in positive comparative performance and a reduction in transaction costs associated with program implementation. In Mexico, the fiscal agent—in this case Nacional Financiera—assumes responsibilities.

Outcome synopsis: Oportunidades

Operation design				**OVE evaluation**	
Objectives (ME-0244; ME-L1007)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Improve food consumption, health, and education opportunities for families living in extreme poverty (direct effects).	√	√	√	√	√
Increase human capital accumulation to reduce the intergenerational transmission of extreme poverty (intermediate effects).	√	√	√	√	√

1.4 Oportunidades, one of the most evaluated projects in existence, is recognized as a benchmark for poverty reduction policy in Mexico for its redistributional efficiency alone. In fact, the precision of its beneficiary targeting is unmatched in any previous food subsidy or other government program.[7] Official reports on the program leave no doubt as to its relative resource-distribution efficiency: increased coverage and sharper targeting.[8] This program, in which the Bank has had a minor participation, has dispensed subsidies to populations suffering from food poverty with over 65% accuracy in beneficiary selection and an inclusion error of less than 10%.[9]

1.5 This evaluation found documentary evidence of a technical contribution by the Bank in this program, particularly in its assistance for maintaining the program's operating rules, including a scoring system for well-targeted distribution of resources. The Bank's technical assistance in 2002 helped institute a new formula for delivering resources to beneficiaries as from that date. The plausible reduction in inclusion error before urban populations became Oportunidades-eligible and in the virtual doubling of the program's coverage over the last six years has reduced losses and created a significant fiscal saving for each percentage point of reduction.[10] A simulation run for this evaluation to compare expenditure efficiency using the scoring formulas before and after the Bank's technical assistance shows a positive difference of about six percentage points in the distribution of Oportunidades resources in 2005.[11] From this exercise we also can conclude that,

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7 *Eficiencia Redistributiva de los Programas contra la Pobreza en México* (Redistributional efficiency of pro-poor programs in Mexico), CIDE, November 2005.

8 Office of the President of Mexico, 2006.

9 CIDE (2005), op. cit.

10 By definition, "inclusion error" means fewer resources available to poor beneficiaries which, added to other costs of programs that ultimately reach the poorest population groups, are a key element in calculating expenditure efficiency. In the case of the *Oportunidades* program, each percentage point reduction in inclusion error saves the Treasury US$30 million a year.

11 A technical limitation of this simulation exercise is the use of household survey (ENIGH) data for a regional analysis. The evaluation team intends to run an analysis of the use of the two formulas on the *Oportunidades* administrative database, to draw conclusive data on the fiscal saving attributable to better targeting of *Oportunidades* resources.

over time, targeting system accuracy can be improved by periodic review, something that was not availed when preparing the second phase of the loan.

1.6 Sharper targeting has been decisive in achieving the program's direct effects in the form of higher incomes and food consumption, as well as improved education and health indicators among the beneficiary population. The available data confirm the outcomes obtained from the infusions of money into households and their effect on income[12] and food consumption.[13] A regional comparison of the distribution of food poverty with and without the program reveals a reduction of poverty in the southern states that is significantly greater than the national mean, thus confirming the program's net north-to-south redistributional effect.[14]

1.7 The program beneficiaries' fulfillment of education- and health care-related conditions has had an impact on the sector's main indicators, reducing infant mortality by 11% and raising secondary school attendance by an average of 10%, in addition to a smaller impact on primary school attendance.[15] Other studies point to possible positive externalities captured by the program in terms of local market development,[16] increases in migration and remittances,[17] and beneficiaries' resilience to unexpected exogenous shocks.[18]

Food poverty	**Reduction attributable to *Oportunidades***		
	2002	**2004**	**2006**
Nationwide	-1.0%	-1.2%	-1.7%
- Urban	0.0%	-0.3%	-0.3%
- Rural	-2.6%	-2.6%	-4.0%
Regions			
North	**-0.3%**	**-0.8%**	**-0.7%**
- Urban	0.0%	-0.3%	-0.1%
- Rural	-1.4%	-2.7%	-2.8%
Center	**-0,8%**	**-1.2%**	**-1.5%**
- Urban	0.0%	-0.3%	-0.5%
- Rural	-2.3%	-2.8%	-3.3%
South	**-2.2%**	**-1.5%**	**-3.2%**
- Urban	-0.1%	-0.6%	-0.2%
- Rural	-3.6%	-2.3%	-5.3%

Source: OVE analysis, from INEGI data.

1.8 The foregoing notwithstanding, the program's intermediate effects in the form of human capital accumulation to reduce the intergenerational transmission of poverty—the key premise for the transitory character of Oportunidades—are not assured, since they depend on other programs and policies forming part of a cohesive strategy, as well as a sustained economic growth environment.[19] Firstly, the effects on schooling, as a proxy of human capital accumulation, are expected to

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12 The latest evaluations reveal a 16% reduction in the number of people living below the extreme poverty line in rural areas, and a slightly smaller reduction in urban zones. See Cortes, Solís, and Banegas (2006).

13 The impact on consumption is over 10%, particularly in the food segment. See Angelucci, Attanasio, and Shaw (2004) and Angelucci and De Giorgi (2006).

14 Based on data from household surveys for 2002, 2004, and 2006. Poverty defined in terms of net monthly per capita income, deflated at August each year. Urban: localities with populations of 15,000 and up.

15 Behrman, Sengupta, and Todd (2005).

16 Gertler, Martínez, and Rubio (2005).

17 Angelucci (2005) and Rubalcava and Teruel (2005).

18 Davis, Handa, and Soto (2001) and Davila and Levy (2003).

19 See Levy and Rodríguez (2005) and Levy (2006).

be progressive and show up in the long term.[20] Secondly if, as is the case now, human capital investment does not encounter a demand for higher-productivity employment, the Oportunidades beneficiaries will not be able to unlock the human capital accumulated and will need permanent income transfers.

1.9 Oportunidades unquestionably has generated demand for health and education services, but this has not been matched by an improvement in the quality of services on offer to the most disadvantaged communities. This evaluation has found no evidence that the program or its client roster have informed work to adapt complementary health or education programs. The challenge for the future, and for maximizing Oportunidades' intermediate effects, is to adapt health and education policy or production development policies to tap the captive market created by fulfillment of the program's conditionalities.

1.10 The Procampo program (ME-0213, US$500 million) is another example of a relevant strategic partnership with the country, in a program wholly designed by the Mexican government. As in the program discussed above, and for all the financial supports to Mexico, the loan proceeds do not add to existing budget lines for an ongoing Mexican government initiative. Unlike in that previous case, however, this evaluation has not found evidence of a distinguishable Bank technical contribution in facets that are crucial for the program's outcome performance. OVE's analysis focused on the objectives set out in the loan document and the respective indicators and metrics, which the evaluation team looked at to assess whether the outcomes sought were delivered and whether Bank technical assistance provided added value to them.

Outcome synopsis: Procampo

Operation design				**OVE evaluation**	
Objectives (ME-0213)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Reduce the incidence of poverty among small farmers (intermediate effect).	√	√			
Improve productivity and increase agrifood exports (direct effect).	√	√			

1.11 The Procampo program was created in 1994 as a temporary support to farmers to help them cope with the envisaged liberalization of the agriculture sector under NAFTA. It was the Bank's 2001 program that had set as a core objective the reduction of poverty incidence among farmers, but the Bank did not succeed in adding value by introducing any specific change in Procampo's previously defined operating rules or specific transfer criteria so as to better target resources. As a

[20] "Broadly speaking, it can be said that perhaps another 15 years are needed for more than half of the *Progresa* workforce to join the job market after completing their higher education." (Levy, *Productividad, Crecimiento y Pobreza en México*, 2006).

result, although—unlike previous price supports provided for the sector—the transfers also definitely benefit subsistence farmers, the distribution of the program becomes regressive in the higher deciles because the more land owned, the higher the transfers per farmer, and non-landowning farm workers are not included. Consequently, as far as Procampo's intermediate poverty reduction effect is concerned, our evaluation found that the program targeted 30% of its resources on populations suffering from food poverty, with an inclusion error close to 50%.[21] Unlike Oportunidades, the analysis of household survey data by geographic region for Procampo finds no evidence of north-south redistributional effects.[22]

Food poverty	**Reduction attributable to Procampo**		
Nationwide	**2002**	**2004**	**2006**
Rural	-1.3%	-1.2%	-0,8%
Regions			
North rural	-1.4%	-2.0%	-1.3%
Center rural	-1.2%	-0.5%	-0.9%
South rural	-1.4%	-1.8%	-0.7%

Source: OVE analysis, from INEGI data.

1.12 With regard to the productivity goal, as the reinvestment rate of the transfers received has been relatively low, the desired outcomes of increasing productivity do not appear to have been achieved. The evaluations done of Procampo corroborate that the beneficiaries perceive no direct improvement in marketing conditions for their crops. The Procampo-Capitaliza segment, the main objective of which was to give beneficiaries advance access to funds to capitalize their production units, has not delivered good outcomes either.[23] Lastly, in relation to the original purpose of supporting productive restructuring of crops most exposed to tariff reduction, the evidence suggests that crop selection has not been consistent with this criterion. Consequently, creation of a system of incentives to raise productivity and switch to potentially more profitable crops remains a challenge for this sector.

1.13 The Habitat program (ME-0255, US$350 million) represents a relevant strategic partnership around the Mexican government's main vehicle to combat urban poverty. As we explain below, Habitat is a regular government program to which the Bank added its support in 2004. This evaluation has found no evidence of technical value added by the Bank as far as results-based management decision making in the program is concerned. The premise for Habitat, a multiphase program, was that the findings of an evaluation of the first 18 months of execution would serve as inputs and, ultimately, as triggers for the following phase, which is currently being negotiated. But, judging from the project documentation, a Bank contribution of an evaluative design to make that exercise viable is debatable. The

[21] See CIDE (2005), op. cit.

[22] Based on data from household surveys for 2002, 2004, and 2006. Poverty defined in terms of net monthly per capita income, deflated at August each year. Rural: Localities with populations under 15,000.

[23] Only 11.4% of *Procampo* beneficiaries participate in this modality, and perceived benefits in terms of transforming production patterns and crop diversification are smaller than expected. No significant employment or export effect was observed. And, predictably, when all potential program benefits are subsumed in a single impact index there is an increasing positive correlation between number of hectares in a beneficiary's possession and the program's output impact index, and an inversely proportional correlation to the financial market access index.

objectives set out in the Habitat loan document, together with the corresponding indicators and metrics, and the evaluation team's findings as to delivery of the anticipated outcomes and the value added to them by the Bank, are summarized below.

Outcome synopsis: Habitat

Operation design				OVE evaluation	
Objectives (ME-0255)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Expand social infrastructure services in marginal urban areas (direct effect).	√	√	√	√	
Reduce poverty and improve the living conditions of the beneficiary population (intermediate effect).	√		√		

1.14 In terms of Habitat's direct effects, our evaluation finds that the original program design specified a mechanism for careful targeting of zones in most need of assistance. Data from the Ministry of Social Development (Sedesol) show that 77% of the program's investments are in communities classified as disadvantaged and very disadvantaged. Bearing in mind that residents of communities with these characteristics account for 7% of the total, Habitat's targeting performance is good: 77% of its investments are targeted on 7% of the most deprived communities. Nonetheless, the mechanics of the program that tilt it toward the geographic concentration of the poor could restrict a further broadening of its reach. Building on good targeting, according to the evaluations done, the outcomes delivered in terms of expansion of infrastructure services were as expected for this type of intervention and comparable to outcomes in similar Bank-funded programs, making for greater access to sewer systems than in nontreated communities and marginal changes in water supply access. Access to electric power did not increase as a result of the program, though this might be explained by the high level of coverage at the outset.

1.15 The evaluations done do not provide data on delivery of the intermediate effects sought by the program. For example, its effects on property values were not measured, nor its effects on unmet basic needs, though a study of this type would have been possible using census data, and the program had set targets in that regard. The employment and income outcomes cannot be considered conclusive, since the effects of changes in conditions could not be isolated using control groups. And there is no information available on the program's specific outcomes for vulnerable groups, impacts on maternal and child health in the beneficiary population, or environmental outcomes, as had been envisaged in the design. In the absence of fundamental data on housing conditions, health, employment, or income, a Bank value-added contribution to results-based management of the Habitat program—the rationale for its involvement by way of this phased program—has not materialized. In fact, to judge by the project documentation, the Bank did not contribute value-added to enable an evaluation of the first phase of the program, to inform work to fine-tune elements of the design of its next phase, which was recently approved.

Support Document A2: Education

1.16 Apart from the effects of an increase in demand associated with the Oportunidades program, the Bank's education-sector engagement in the period evaluated is confined to the Community Education Program (ME-0052, US$210 million). In the face of the challenge of enhancing equity in the supply of public education services in Mexico, which have been gradually decentralized under an arrangement of transfers to states with known distribution-quality problems, this program has simply added to those ongoing efforts; given their scope, it is impossible to isolate its impact. As discussed below, this is a routine government budgeted program in which, according to the documentation reviewed, partnering with the Bank did not help deliver outcomes.

Outcome synopsis: Community Education Program

Operation design				OVE evaluation	
Objectives (ME-0052)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Improve the coverage, quality, and efficiency of community education services for low-income residents of isolated areas not served by the formal education system.	√		√		

1.17 As conveyed in its objective, a fundamental element for achieving outcomes in the Community Education Program is the capacity to respond flexibly to a changing target market, ensuring complementarity with the Ministry of Education and with state government education services, so as to keep it operating in remote communities where it is still needed. The available documentation indicates that the Bank has not added value in terms of aiding the necessary adaptive management of the program, mainly for two reasons: (i) an emphasis on coverage indicators over targeting needs in a subsidiary relationship with the rest of the public education supply during the design and monitoring stage, and (ii) relative inflexibility in the (untimely) application of the financing matrix, which meant that a number of items that the executing agency considered necessary to deliver the outcomes could not be funded.[24]

1.18 Information on the program outcomes shows that it did not prove possible to institute careful management of the necessary targeting of underserved localities, since the requisite information is not available. Without this core information, coverage targets are meaningless because the target treatment universe is unknown.[25] Given the indicator fuzziness and using as a proxy the rate of rural school attendance which, in the long term, would reflect level of schooling of the rural population, OVE finds that although there has been an increase in attendance, it cannot be ascertained whether this was due to an increase in CONAPE or Education Ministry coverage or to attendance increases in then-existing schools.

Table: Rural school attendance			
	Total	**Male**	**Female**
2000 census			
Age 5 to 9	85.69%	85.57%	85.81%
Age 10 to 14	84.41%	85.75%	83.03%
2005 count			
Age 5 to 9	92.16%	92.10%	92.22%
Age 10 to 14	89.22%	89.56%	88.87%

1.19 In terms of the quality of education delivered, the improvements recorded do not meet the target of a statistically significant 7% improvement in primary students' standardized test scores; the point estimate gives increases below 1%, which are not

[24] The requirement to limit resources for payments and study grants to educational institutions (*Figuras Educativas—FEs*) had negative consequences for the program. These design failures are evidenced in the reallocation of funds towards payment to FEs and slow disbursement, which has taken implementation to the five-year limit: (a) In 2004, US$24 million was reallocated from "Contingencies" to "Subsidies and Transfers to FEs," increasing its share of the total loan amount from 54% to 65%; (b) in 2005, US$2.1 million was transferred from the "Inspection and Supervision Charge" line under "Financial Costs" to "Contingencies;" (c) in 2006, the US$2.1 million contingencies allotment, together with US$720,000 for audits, US$511,000 for evaluations, US$11.4 million for institutional strengthening (69% of the original budget), and US$24 million for nonrecurrent expenses of the rural community education component—a total of US$36.8 million—were transferred to "Subsidies and Transfers to FEs," raising that line to US$174 million, or 83% of the program's budget. Although these adjustments display the Bank's flexibility to facilitate implementation, they also evince an unrealistic design not well suited to CONAFE needs.

[25] The loan document sets several coverage targets: by the end of phase I, coverage rates are to increase 21% at the preschool level, 5% in primary education, and 45% for education services for adults who never completed the full basic education cycle. These targets were reset in the June/July 2004 administration mission, to 33%, -7%, and 249%, respectively. This change in targets bespeaks a planning failure, since the decrease in the 5-to-14 age group cited as the rationale is a secular trend.

statistically significant. These changes are less than the improvements recorded by public or private education comparators.[26]

Table: National means 2000-2005 Grade six primary, by educational stratum				
Educational stratum	**Mean**		**Difference**	**Significant**
	2000	**2005**		
(i) Reading comprehension				
Urban public	510.44	541.11	30.67	*
Rural public	480.76	503.1	22.34	*
Indigenous school	443.73	480	36.27	*
Community programs	467.7	471.93	4.23	
Urban private	572.7	628.37	55.67	*
(ii) Mathematics				
Urban public	512.96	534.23	21.27	*
Rural public	484.69	494	9.31	
Indigenous school	441.43	468.04	26.61	*
Community programs	466.71	470.43	3.72	
Urban private	547.26	597.27	50.01	*

Source: Comparative study of basic education in Mexico, INEE, 2005.

[26] As an indicator of the quality of education delivered, the project's logical framework targets a 7% improvement in Education Ministry standardized test results for CONAFE primary school students by the end of phase I. According to the PPMR, data published in November 2005 reported on primary education achievement in CONAFE community programs. That report compares 2000 and 2005 reading comprehension and mathematics scores of grade-six students, in the case of CONAFE equivalent to level-III students. The mean national reading comprehension score of sixth-grade students in community programs was 467.70 in 2000 and 471.93 in 2005, i.e. a 4.23-point improvement. In mathematics, the national mean was 466.70 in 2000 and 470.43 in 2005, an increase of 3.72 points. But the study reaches a different conclusion: regarding reading comprehension, "The most significant changes observed at the primary level are in private schools, followed by indigenous, urban public, and rural public schools. In community programs no significant changes are observed over these five years." In the case of mathematics, the report concludes that "The most significant changes observed at the primary level are in private schools, followed by indigenous and urban public schools. No significant changes were observed over that interval in community programs or in rural schools."

Support Document A3: Labor Market

1.20 The family of employment-related programs (Labor Market Modernization, Training and Employment, and Competencies-Based Human Resources Development) continue a more than 20-year tradition of multilateral presence in a top-priority sector. Nonetheless, in a sector characterized by structural problems in the operation of employment markets, and which is identified as one of the main gaps to be closed to overcome poverty, the Bank's program during the period examined departed from policy issues, to which it had given greater weight in previous programming spans, to concentrate on specific intermediation and training projects with relatively limited coverage. The Bank's technical value added to outcomes thus is down accordingly from its documented late-1990s contribution.

1.21 For outcome analysis purposes, this section focuses on the original objectives of the Labor Market Modernization (ME-0118, US$450 million), Training and Employment (PACE) (ME-0233, US$300 million), and Competencies-Based Human Resources Development (ME-0250, US$50.4 million) programs, namely:

Outcome synopsis: Employment

Operation design				OVE evaluation	
Objectives	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Consolidate active labor market policies and develop employment policy planning and delivery capacity (ME-0118).					
Promote (a) employability; (b) mobility; and (c) workforce productivity (ME-0233; ME-0250).	(a) √ (b) (c)	√	√	√	

1.22 The outcomes delivered in the area of consolidating employment policies have been limited, in a setting of substantial government budget cuts.[27] The Bank's involvement has not elicited changes or adjustments in employment policy such as might have overcome, in the long term, the challenges diagnosed, or tailored policies to the different production fabrics and employment markets in northern and southern Mexico. No progress has been made in improving employment policy planning capacity, regulatory reforms to increase worker productivity were not implemented, and the active policy set, which is the same as before, has been shown to be unsuited to the new labor market realities. As for value added by the Bank, there has been a net loss with respect to what the government credited in the previous cycle, the value-added contribution having been limited to support for the

27 For example, in 2002, 2003, and 2004, the Finance Ministry ultimately approved just 77%, 59%, and 55%, respectively, of the funding budgeted for the PACE program.

use of active labor market policy tools, with a neutral showing in terms of employment policy making or debate and even less in terms of a broader employment policy.

1.23 This evaluation credits the improved employability outcomes, given the programs' reach and job placement rates. The original program target was to serve just under five million people in three years, with an average placement rate of 33%. The following table shows that, although the expended budget was smaller than planned, targets were achieved in terms of the number of beneficiaries served, and the average job placement rate was only slightly below target.

Table 4.5. Employment Support Program (PAE) outcomes and targets (planned and actual)

		2002	2003	2004	2005	2006*	Total
Original forecast	Served	1,481,238	1,683,379	1,824,144	n.a.	n.a	4,988,761
	Placed	511,000	556,889	607,331	n.a	n.a	1,675,220
	Placement rate	34%	33%	33%	n.a	n.a	34%
Outcomes	Served	1,534,979	1,878,536	2,037,827	2,009,337	1,076,705	8,537,384
	Placed	530,300	508,471	587,094	532,850	281,977	2,440,692
	Placement rate	35%	27%	29%	27%	26%	29%

1.24 The intermediation systems outcomes reveal no significant coverage or placement impact. The aim was to serve 7.5 million people in nine years and significant coverage has been achieved, but National Occupation and Employment Survey data show that the proportion of job seekers making use of the national employment system is still small. Moreover, the quality of jobs on offer remains low, with wages below the average threshold that triggers social security contributions. The new information tools (Chambatel, Chambanet) and employment exchanges have not achieved their targets of raising the placement rate of job seekers to 45%. During the first phase, for example, the Labor Exchange (Bolsa de Trabajo)—the main intermediation instrument—has found jobs for 30% of candidates.

1.25 For the training component of the Employment Support Program (PAE), OVE performed an impact evaluation in 2005. This contrasted outcomes for beneficiaries' placement, job quality, and wages with a comparator group obtained from data from the Quarterly National Employment Survey (1998-2004). The evaluation concludes that, overall, the program did raise employment rates, particularly in the in-service training modality in large firms. The placement outcomes sought with the on-site employment training program did not materialize. That program had aimed to raise its placement rate from 70% to 80%. The outcomes were 70% for 2002-2004 and 53% for 2005 and 2006, which is explained by the diversification of intervention modalities, including some with lower placement rates.[28]

1.26 The outcomes of productivity improvement through training programs in microenterprises and small businesses (PAC) have been constrained by major changes made to the program focus, in which environment the Bank was unable to institute an effective technical dialogue. The change in the original intervention focus meant that the program steadily lost significance in terms of coverage. According to the original diagnostic, there was sufficient installed capacity to serve 50,000 firms a year; the goal was to gradually increase this to 100,000. But in April 2003 the phase I target was revised to 13,041 firms, and the program ultimately served only 5,694.

Table 4.6. PAC program forecasts and outcomes

	Indicator	2002	2003	2004	2005
Original forecast	Firms registered	40,000	45.000	50,000	n.a
	Workers registered	n.a	n.a	350,000(1)	n.a
	Courses	n.a	n.a	n.a	n.a
Revised forecast	Firms registered	15,000	13,636	13,041	n.a
	Workers registered	74,000	68,162	65,206	n.a
	Courses	37,000	33,616	32,168	28,064
Outcomes	Firms registered	16,320	8,592	5,694	6,913
	Workers registered	59,050	77,296	71,546	81,114
	Courses	32,445	21,089	25,260	28,064

Forecasts included in the PPMR. The changes were made in April 2003.

1.27 In the area of job skills certification through the application of competencies standards, the Bank picked up a previous World Bank-funded program. The IDB has previous experience, by way of MIF funding to develop a competencies certification system. Nonetheless, given the World Bank's decision not to continue funding the initiative, neither the IDB's rationale for participating in the project nor

[28] One of the goals in the project's logical framework was a 20% reduction in employers' recruitment costs and shortening of the job-search period for the unemployed. But, in the framework of evaluations performed in phase I, the only estimates available relate to time spent in job search. See OVE (2006), *Impact Evaluation of Job Training in Mexico*.

the value it added to revise the original scheme are clear.[29] Some key drivers of the success of an intervention of this type, such as securing effective private sector leadership in standards setting, assuring effective adoption of the standards by the various upper secondary education institutions, and improving efficiency in the standard-setting and certification process, were not built into the Bank's proposal to make the outcomes deliverable.

[29] The outcomes of the earlier World Bank-funded program were unsatisfactory. That agency's Implementation Completion Report (ICR) is more negative on the Technical Education and Training Modernization Project. Although that report was published a fortnight after the 2004 approval, the project report mentions that the IDB participated in the last World Bank project administration mission. At first glance, the ICR criticisms of the design are applicable to the IDB program design, in terms of the lack of a solid diagnostic of the program's relevance and feasibility—business community demand for training, private-sector commitment to the system, feasibility of modernizing higher technical secondary education by adopting these systems—and institutional implementing capacities. This is all the more important given the inherent institutional complexity of the project. The last Technical Education and Training Modernization Project administration mission did not have access to key studies such as would have provided fundamental information on impacts and performance of the employment competencies system. These studies were not produced by the IDB in the design stage, but rather are part of the program.

Support Document C1: Strengthening of States and Municipios

1.28 During the period examined in the evaluation the State and Municipal Strengthening Program (FORTEM) fortified a long-term strategic partnership with the government public works investment bank, Banco Nacional para las Obras Públicas (Banobras). Although the strengthening of subnational governments is a major challenge, particularly in an era of increased transfers of resources, powers, and responsibilities, the program's low coverage, measured by the number of states and municipios assisted, makes the relevance of the strengthening objective debatable.

1.29 The individual FORTEM programs (ME-0208, US$800 million; ME-0231, US$300 million; ME-0256, US$200 million) were conceived as a hybrid program to be followed by a three-phase program, for a total of US$1 billion.[30] As discussed below, the Bank has not contributed value-added to bring about changes in lending policies and practices for Banobras projects. These policies are skewed toward lending to subnational governments that offer low financial risk, rather than providing a desirable expansion of credit to the more disadvantaged states and municipios. Regarding the strengthening of state and municipal capacities, any Bank value-added contribution to seeking out the best institutional alternative for a capacity-development advisory system is debatable. The objectives, indicators, and metrics defined for these programs, together with OVE findings on their outcomes and the value added to them by the Bank, are outlined below.

Outcome synopsis: FORTEM

Operation design				OVE evaluation	
Objectives	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Finance public works projects yielding high social returns in states and municipios (ME-0256).	√	√	√		
Support the decentralization process, strengthening and improving subnational government management capacity, and improve Banobras operational efficiency (ME-0208-ME-0231).	*	*	*		

* Indicators, baselines, and targets were defined only for a pilot plan in disadvantaged municipios.

30 The Bank's primary support and role in decentralization has been through Banobras. The Bank has funded three operations in recent years. The first, in 1999, contained an investment component and a fast-disbursing component. The fast-disbursing portion included measures to reform Banobras, ranging from credit policies to human resources. The investment component was intended to finance subnational government projects, but it too contained provisions to strengthen financial and administrative management in those governments, particularly relating to implementation of the newly created social-expenditure budget line called *Ramo 33*. No specific indicators are identified for the investment component.

1.30 The public works financing outcomes fell short of the targets.[31] The aim of giving market access to subnational governments that lacked such finance avenues was not addressed by the FORTEM operation. In fact, the program has shown a preference for financing investment projects in certain large states and municipios with low marginality levels. For example, the program was revised to enable the State of Jalisco to use the remaining resources for a single project. The following table shows that, apart from Tlanepantla, the municipios that have used Bank resources for FORTEM have very low marginality rates.

Table: Marginality rate of participating municipios

Municipio	Poverty (%)	Population (thousand)	Marginality
Morelia	6.3	684	Very low
Uruapan	14.6	279	Very low
Tlanepantla	11.2	6	Medium
Puebla	8.0	1,486	Very low
Nuevo Laredo	6.5	336	Very low
Median (Mexico)	29	11.8	Medium

1.31 As for institutional strengthening, only five states—Veracruz, Jalisco, Durango, Oaxaca, and Quintana Roo, and four municipios—Nuevo Laredo, Tlanepantla, Morelia, and Puebla—participated in the first program (ME-0208). In the second loan (ME-0231), 10 municipios with medium or high marginality levels were to participate in a pilot institutional strengthening plan. The program did not achieve these targets. In fact with 80% of funds committed, only two operations had been undertaken with the State of Jalisco, one with Guanajuato, and one with the municipio of Uruapan. Although improvements are observed in the three subnational governments that participated in the program, outcomes fell far short of the targets, and even the strength of ownership and commitment of the Guanajuato and Uruapan authorities has been questioned in evaluations done of the program. With regard to the internal restructuring of Banobras, in particular, for which there were more than 50 proposed reform measures, there is no evidence that the modernization activities undertaken have helped enhance the quality of Banobras services or change its market position and its capacity or development of any potential comparative advantage as an institution-strengthening agent.

1.32 A second phase of FORTEM was approved in July 2006 for US$200 million (ME-0256), when 45% of the loan had been disbursed and 80% committed. Fulfillment of conditions for triggering the second phase was made easier by the fact that the planned improvements only had to be verified in three subnational

[31] Although the *municipio* coverage targets were attained, funds were not targeted on *municipios* with high marginalization levels as envisaged in the loan document. According to the Banobras Annual Report, in 2005 the institution serviced 531 *municipios* (a record for this bank), which denotes a certain level of maturity and financial soundness. The authorities acknowledge that, despite this record Banobras performance, about 1,600 *municipios* still have no viable finance alternatives.

governments and not in the 15 initially envisaged. The innovative feature of the second phase is more flexible conditions to access credit (including local currency loans) and greater emphasis on technical assistance.

Support Document C2: Financial Sector

1.33 The family of programs supporting the financial public sector and financial market development, with investment projects as well as policy reform and MIF projects, distinguishes the financial sector, and particularly government-owned development banks, as a major activity sector for the Bank. As analyzed below, this is a sector in which the Bank added value to some outcomes, primarily in the process of creating Financiera Rural or the consolidation of Bansefi.[32] But, apart from the value added in these specific subsectors, there is no evidence of substantive technical supports or contributions as catalysts for reform of the development banks worked with or for financial market deepening. In its support for the larger development banks there is therefore no evidence of the Bank's having focused its efforts on the correction of market failures or delivery of financial services to hitherto excluded sectors.

1.34 To structure the analysis around outcomes, this section focuses on the objectives of the following programs: Consolidation of the Rural Financial System (ME-0243, US$300 million), Consolidation of the Financial System (ME-0259, US$600 million), Financing for Small and Medium-Sized Exporters (ME-0240, US$100 million), and MIF projects (TC-0109022, ME-M1012, ME-M1004, and ME-M1017, for a total of US$7 million), as follows:

Outcome synopsis: Financial sector

Operation design				OVE evaluation	
Objectives	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Expand and consolidate the supply of rural finance services by reforming Financiera Rural (ME-0243).	√	√	√	√	√
Increase access to financing for small and medium-sized export enterprises (ME-0240).	√	√	√		
Promote the development of savings and loan institutions for the low-income population (MIF).	√	√	√	√	
Deepen financial markets and expand bank lending to the private sector (ME-0259).	√	√	√		

1.35 The outcomes of expansion of rural finance, and Financiera Rural (FR) reform in particular, show a positive trend, even though that operation's outcome targets are for 2008. Commercial bank lending to the agriculture, forestry and fisheries sector increased from 19.666 billion pesos in 2004 to 20.968 billion pesos in 2005, and had reached 20.142 billion pesos in June 2006. These figures point to buoyant lending in the market, although it only represents 1.6% of the commercial bank

[32] Nonetheless, the World Bank's contribution to that institution has been greater in volume terms, having financed basic services infrastructure.

credit portfolio. There is also evidence that private commercial banks are gaining ground as first-tier actors while Financiera Rural continues to expand its business volume with credit unions. With regard to the financial situation of FR, its indicators are sound and superior to those of Banrural, for example.[33]

1.36 This evaluation found documentary evidence that the IDB, along with the World Bank, has added value in two fundamental aspects of the reform, helping to: (i) secure consensus on Banrural's liquidation as a process trigger, and (ii) drive the Financiera Rural reform process by way of the loan conditionalities.[34] In 2002, the IDB and the World Bank sponsored a seminar that attracted broad representation from key political actors in the sector. This helped in the forging of consensuses around a number of political and technical issues needed to implement structural reform in the sector, resulting in unanimous Senate approval of the reforms.

1.37 The outcomes of access to financing for small and medium-sized export enterprises are not available because at the time of this evaluation that operation had not begun executing. As a background issue: backing the Bank's contribution in supporting an institution like Bancomext is problematic, given its financial situation and the announcement—at the time the loan was signed—of its prospective merger with Nacional Financiera (NAFIN) owing to its duplication of functions. This evaluation questions the market-deepening outcome orientation in the program design: it proposes to work with a sample of 300 businesses that have already used Bancomext the previous year and its monitoring indicators do not provide for inclusion of new enterprises without access to credit.

1.38 The outcomes of the development of saving and loan institutions for the low-income population and consolidation of Bansefi pursued by three consecutive MIF operations have been the ones sought.[35] At end-2000 the community saving and loan institutions had formed 14 federations, and the National Banking and Securities Commission was in the process of approving its oversight arrangements,

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[33] June 2006 figures show net earnings of 226 million pesos. The bank has reserves in excess of the required provisionings and some of its financial ratios are superior even to development bank numbers, such as a loan loss provisioning index of 232%, capital to risk-weighted earning assets (min.) of 6.8%, an operational efficiency index of 3.9%, and an ROA of 2.2%. Others are slightly below that standard, such as a 3.5% arrears rate and an ROE of 2.2%.

[34] The PBL conditions did address issues of the subsidiary role of the State and strive to come up with the best solution. The first-tier function of FR was justified politically and technically by the sudden disappearance of Banrural and the existence of an unsatisfied market. It was clearly stated that the Bank's program aimed to reduce the number of distortions, not completely eliminate them. The gradual disappearance of that function was also envisaged, to eventually concentrate on second-tier functions. Lastly, a potentially controversial issue was addressed involving subsidized interest rates and the promotion of private-sector intermediary engagement in rural areas. Particularly noteworthy was the Bank's assistance for the pricing of all credit products based on the cost of capital, operational and administration costs, and risk spread.

[35] In 2002 the MIF financed technical assistance to help 1,000 institutions adapt to current legislation, for the technological upgrading of Bansefi, and for development of new savings products. In 2005, it funded preliminary steps for the sale of Bansefi equity to community saving and loan sector operators; and in 2006 it supported the creation of a pension fund management company (AFORE) for people who have no retirement pension fund.

thus contributing to a reduction of informality in the sector. Bansefi plays a key role as "bank for the savings and loan banks," centralizing payments systems and obtaining scale economies for the benefit of its members (e.g. negotiating a lower commission for remittances). In financial terms, Bansefi went on to post surpluses and healthy indicators, including the highest operating efficiency index of all development banks (8.14% in March 2006) and the lowest average cost of funds ratio (2.34%). The outcomes of IDB and World Bank support to Bansefi can be credited for their impact on the supply of financial services to low-income sectors, many of them in rural areas. The consolidation of this bank as a catalyst for efforts to reach vulnerable populations in a financially sound way and using market mechanisms, represents MIF value-added to outcomes in this sector.

1.39 Outcomes attributable to the Bank's programs for deepening financial markets and scaling up bank lending to the private sector are more debatable. Since the 1995 crisis, policy reform programs have been funded to revive and develop the banking sector.[36] The value added by the Bank in this program is debatable since it is really only recognizing countries' own reform efforts, in exchange for which it provides an unrestricted loan. In this case particularly, the conditions set are certainly important for continuing to deepen the Mexican financial market, but it is hard to distinguish any value added by the Bank in obtaining such outcomes.

[36] In 1995, a US$750 million PBL was approved to help Mexico recover from the late-1994 crisis. In 2000 the Bank approved a US$250 million sector loan to continue supporting the recovery and development of the banking sector. More recently, in August 2005, a US$600 million PBL was approved to deepen financial markets.

Support Document C3: Housing

1.40 With the Housing Finance program (ME-0137, US$505 million) the Bank added its support to a wide range of Mexican government initiatives to improve the efficiency of the nation's housing market.[37] As discussed below, this program involves joining forces with similar government programs in which the Bank has contributed technical value-added for more efficient operation of the housing market, but it has not added value in terms of tailoring a finance product to the needs of lower-income Mexicans, its defined market segment. The program's objectives, indicators, metrics, outcomes, and value-added contribution are summarized below.

Outcome synopsis: Housing

Operation design				OVE evaluation	
Objectives (ME-0137)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Improve the efficiency of Mexico's formal housing finance system.	√		√	√	√
Help expand the housing finance market to poorer segments of the population. [38]	√		√		

*The indicators and targets for the second objective were incorporated in the PPMR.

1.41 With regard to efficient operation of the housing market, the program encountered a fundamental problem—competition with Mexico's workers housing authority, INFONAVIT, which reduced the demand for this loan product. Nonetheless, the IDB loan did serve to finance contingent liabilities arising from Mexico's former Bank Housing Finance and Operations Fund (FOVI), consistent with the new lending product of the mortgage finance company Sociedad Hipotecaria Financiera (SHF—PROSAVI), thus helping to improve a number of efficiency indicators.[39]

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[37] Government programs include subsidized loans through programs for private and public sector employees, such as the National Workers Housing Fund Institute (INFONAVIT) and the Housing Fund of the Social Security Institute for Government Employees (FOVISSSTE), both managed by the mortgage finance company Sociedad Hipotecaria Financiera (SHF). Other similar programs are the Mexican Social Housing Fund (FONHAPO) and funding through Limited Purpose Financial Companies (SOFOLES). National Housing Commission data show that the main player in the housing sector today is INFONAVIT (57% of new homes), followed by the programs of SHF (12%), FOVISSSTE (11%), SOFOLES (6%), and FONHAPO (5%).

[38] Initially the PPMR attempted to track efficiency outcomes (mortgage spreads) and equity outcomes (percentage of groups benefiting from the program by income level). But these data disappear in subsequent PPMRs, which only count outputs (number of housing units delivered), this being totally insufficient to verify delivery of the project's initial objectives of efficiency and equity.

[39] ME-0137 consists mainly of an investment component and a much smaller technical assistance component. It aims to achieve these objectives by consolidating the reform of the second-tier mortgage finance institution FOVI and by financing subsidies and mortgages. The original executing agency was Banobras, which was replaced by SHF in 2002.

1.42 As for the expansion with equity aim, in its original design the Bank's loan was preferentially targeted to low-income households. According to the program's operational arrangements, beneficiaries earning less than 3.5 times the minimum wage were eligible for income-geared subsidies, whereas beneficiaries with earnings above that threshold could receive credit but no subsidy. However, the program encountered slim demand and intermediaries were reluctant to lend to low-income applicants. This forced a change in the program's operating regulations, and the threshold was raised to five times the minimum wage.[40] The results show that either the ability of these funding mechanisms to expand the market into poorer sectors was overestimated in the operation's design, or else suitable instruments were not available. Although the targeting of subsidies on the poorest households was the program's defining feature at the outset, there is no documentary evidence that the Bank contributed analytical value-added to elements such as providers' opportunity costs or transaction costs, or risks that the characteristics of demand might not be achieved under the incentives scheme proposed by the project.[41]

[40] An equivalent decision was taken by the parallel World Bank program which started to finance the FOVI program a year earlier, with a similar diagnostic and components. But this change made explicit its decision to abandon the equity component and targeting objective.

[41] No evaluation has been done of this operation, but in 2006 the World Bank evaluated a similar program ("*Tu Casa*") using treatment and control groups. According to the study's authors, the findings show that the beneficiaries are living in nicer homes built with better quality materials, and are more satisfied with the quality of their dwellings. But the new neighborhoods are substantially worse: worse access to services, violence, distance from work, etc. The housing subsidies thus have an impact on housing quality but this impact is diluted by access to services.

Support Document C4: Water and Sanitation

1.43 During the period encompassed by the country strategy the Bank approved an operation entitled Institutional Development and Sustainability of Water Supply and Sewerage Services in Rural Communities II (ME-0212, US$150 million) which marks a continuation of Bank support for the PROSSAPY program approved in 1998 (ME-0150, US$310 million).[42] Owing to the low level of disbursement of the project approved in this period, its outcomes are difficult to assess. Nonetheless, it is possible to analyze outcomes and value added by the Bank for PROSSAPY, and also the consistency of the second-phase design approved in 2005. For value-added assessment purposes it is important to mention the Bank's proposal to explicitly help sharpen the programs' targeting to reach the most underserved populations. However, the Bank has been unable to demonstrate additionality through any change in the incentives system of the institutions involved, to redirect funding towards works consistent with that intent.

1.44 The following table summarizes objectives, indicators, and metrics for the loans to PROSSAPY, the outcomes delivered, and their value-added.

Outcome synopsis: Water and sanitation

Operation design				OVE evaluation	
Objectives (ME-0150, 1998, and ME-0212, 2005)	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Improve access to water and sanitation services in rural communities, prioritizing poorer segments of the rural population.	√	√		√	
Promote reform of the rural water and sanitation system.	√		√		

1.45 In terms of improving access to water and sanitation services in rural communities, thus far the Bank has not performed a rigorous review of outcomes in relation to service quality, coverage, and impact on the population's health indicators.[43] What can be said is that these projects suffer from internal design inconsistency, since service efficiency targets (cost per beneficiary) compete with matched-funding requirements and service coverage targets in poor rural areas.

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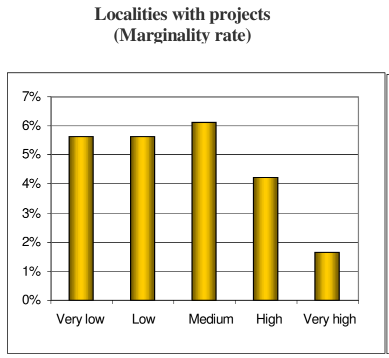
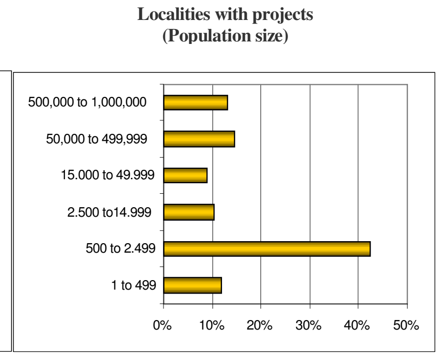
[42] Program for the Sustainability of Drinking Water and Sanitation Services in Rural Communities, managed by the National Water Commission of Mexico.

[43] The Bank's review mechanisms (PPMR and PCR) focus on the physical expansion outputs, which were largely achieved. But outcomes in terms of service quality, coverage, and health relative to the project's objective were not measured, despite the availability of census data for the water sector in Mexico, with which an impact evaluation and targeting analysis could be done for this type of operation.





1.46 The findings of the OVE analysis of targeting in the first PROSSAPY program (ME-0150) using locality data from the National Water Commission and the Mexican Statistics, Survey, and Information Bureau (INEGI—2005 Census) are presented in the charts below. According to the National Population Council marginality classification, a small fraction of localities with high and very high marginality rates were served by the project—only 1.7% and 4.2%, respectively. Likewise, by size of locality served, small communities—home to the bulk of the population without full access to basic services—do not predominate. Cities with over 50,000 residents were well served, and even large centers with populations over 500,000. Accordingly, the loan's implementation was inconsistent with its targeting, both in the prioritization of rural (and small) localities and in reaching the lowest-income communities.

1.47 OVE also evaluated the project's impact by analyzing potable water, sewerage, and sanitary facilities coverage in "treated" communities (served by the project) compared to nontreated communities (households with similar characteristics, not serviced by the loan).[44] Available data show a significant change in coverage between 2000 and 2005. The measures of "unmet basic needs" (UBN) calculated in 2005 by CONEVAL and replicated by OVE in 2000 show a 6% reduction in the number of households without indoor plumbing, 18% for households without sewer system hookups, and 6% for households without public piped water.[45] In other words, in the space of five years there has been rapid progress in the sector in terms of coverage. Treated municipios show larger reductions in UBN than nontreated

[44] It should be noted that the evaluation team had access only to 10% of the 2000 census findings and some 2005 municipal household and marginalization means (figures produced by the National Council for Social Development Policy Evaluation—CONEVAL). Consequently, the impact estimate obtained understates the *average treatment effect on the treated* (ATT effect) because only a fraction of the localities of a *municipio* were treated. The parameter more closely resembles what the impact literature refers to as *intent to treat* (ITT), which is the average treatment effect on a group when only a fraction of them actually received treatment. If one uses the algorithm proposed by Bloom et al. (2005) to weight the ITT by the fraction of localities treated, the impact parameter rises toward a 0.14-point reduction in sanitation unmet basic needs (a change from 0.011 to 0.140).

[45] The UBN measures were those calculated by CONEVAL: sanitary UBN is the percentage of inhabited private homes that do not have an indoor toilet; sewerage UBN is the percentage of inhabited private homes not connected to a drain system; water UBN is the percentage of inhabited private homes that are not connected to the public piped water system.

ones—almost one percentage point in sanitation and 1.2% for sewerage services.[46] Accordingly, the OVE impact evaluation findings indicate that, leaving aside the targeting problems that limit its outcomes, the program is having a positive impact in the localities it does serve, as one of a set of public and private sector changes which are improving the coverage of water and sanitation services.

1.48 The system reform outcomes were not associated to specific activities financed by the first loan, nor did they have metrics with which to evaluate outcome attainment. According to the original reform design, the federal level was to assume a regulatory role and sector management would be put in the hands of the municipios, accompanied by a rate restructuring. This evaluation finds no evidence of a technical contribution by the Bank to analyzing the political economy constraints of a reform of this type. Given the apparent scant progress toward the institutional reform objectives, for the subsequent period it was decided to change the focus through pilot projects (mainly with the ME-0253 loan). Nonetheless, the level of disbursement of this operation to date is relatively low, and the outcomes seem unlikely to be achieved.

[46] The lack of specific impact in the water sphere is curious, because the distribution of projects favors this sector in number terms and in amount invested. The number of water solutions funded varied between 33% and 60% of all projects, whereas sewerage and sanitation solutions varied between 10% and 18%, and technical-study funding accounted for 20%-40%. Conceivably the definition of water UBN, which uses household connection to public water supply systems as the yardstick, is unsuitable for measuring the impact of rural water projects. In fact, most such projects are small-scale solutions using wells, which seldom are completely hooked up to houses and are not counted in the UBN measure. We computed estimates using the least squares method, controlling for municipal variables, and the propensity score method. There were no significant differences between the parameters estimated by the different methodologies.

Support Document C5: Energy

1.49 Highlights in this Bank action area are three thermoelectric power generation projects financed through the private-sector window (PRI) without sovereign guarantees (Bajío ME-0225, Vitro ME-0228, and Monterrey III ME-0229) and the energy efficiency program funded through the public-sector window. The table below summarizes the objectives, indicators, and metrics in the loan documents and the project outcomes with their value added.

Outcome synopsis: Energy

Operation design				OVE evaluation	
Objectives	**Indic.**	**Baseline**	**Target**	**Outcomes achieved**	**Value added**
Expand electric power generation for the national grid or to supply some industries in northern Mexico (ME-0225; ME-0228; ME-0229).	√	√	√	√	
Reduce energy consumption by developing a market for high-efficiency devices (ME-0204).	√	√	√	√	√

* The baseline and targets for the second objective were incorporated in the PPMR.

1.50 The outcomes of the portfolio of nonsovereign guaranteed electric power generation projects, to scale up installed capacity and thus supply some industries in northern Mexico, have been those anticipated. Pending the sector reform promoted in the Bank's strategy, this group of operations nonetheless runs the risk of favoring the dominant market position of the Federal Electricity Commission, which raises questions about internal consistency with this objective and, ultimately, the value added by the Bank for its delivery. With regard to the environmental impact of the thermal power plants, PRI has analyzed the carbon emissions footprint of the generating projects financed,[47] which can guide future opportunities to monitor greenhouse gas emissions. The preliminary findings of this study show that thermal power plant emissions in Mexico fall into the typical range for generating plants that use clean fuels (natural gas)[48] and improved technologies (combined cycle), displaying good ratios of carbon emissions to electricity produced. Accordingly, it is considered that these projects marginally improve the carbon intensity of the Mexican power grid.[49]

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47 Using data such as the carbon content of fossil fuels combusted and composition of the power generation grid, according to the methodology of the Intergovernmental Panel on Climate Change (IPCC).

48 Nonetheless, it is worth noting the World Bank's comments in its analysis of the Mexican energy sector and the environmental implications of a lack of domestic natural gas to supply domestic demand unless there are further investments in this area (World Bank, 2001, p. 131).

49 For the moment it has only been possible to ascertain that CO_2 emissions, relative to the total cost of projects in the Bank's PRI portfolio, are comparable to the EBRD portfolio.

1.51 The outcomes of the energy efficiency program (ME-0204, US$23.4 million) lay in creation of an incentives system and financing and development of energy service companies to promote the use of high-efficiency devices (motors, compressors, lights). Despite the difficulty of ascertaining this project's impact on the country's total energy improvement needs, an evaluation performed by an independent consulting firm notes the progress made in transforming the market for efficient devices. For example, value has been added by the program for adoption of a Mexican energy efficiency standard for triple-phase induction motors that only allows high-efficiency motors to be put on the market. The cumulative saving in both electricity consumption and electricity demand as an immediate outcome of the project was also measured: the operation produced a cumulative saving of 5,274 GWh in consumption and 270 MW in demand as at 31 October 2004.[50] An indirect contribution was also made to reducing polluting emissions thanks to the electric energy saved as an environmental benefit of the operation, making it possible to reduce emissions equivalent to 3.8 million tons of CO2.

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50 This saving was counted in a cost-benefit analysis that looked at aggregate annual investment for the program and the price of avoided electricity consumption, setting a baseline for this type of innovative program.

ANNEX I
Analysis of Follow-up on Conclusions and Recommendations of the 1990-2000 Mexico Country Program Evaluation (CPE)

1. Conclusions of CPE 1990-2000	2001-2006 (*)	Paragraph
Relevance of programming/Program-based approach		
Lack of strategic prioritization: The “priorities” outlined in the CP were so broad that no project could be incompatible with them.	=	2.14
Low strategic anticipation capacity: Many loan operations that were envisaged were not undertaken. No indication as to the Bank’s comparative advantage relative to other multilateral lenders.	=	2.13
Limitations of the program-based approach: Projects were scattered through different sectors and had numerous stated objectives.	=	2.18
Reactive programming: The Bank’s program appeared to respond to project selection by the government.	=	2.9
No identification of a niche: The Bank’s program did not have a marked pro-poor tilt. Such a tilt could constitute a valuable focus for the Mexico program and a viable niche for the Bank.	=	2.37
Efficiency and effectiveness		
Low evaluability. The Bank does not collect information on progress made toward project outputs and outcomes. Very few projects defined their development objective.	=	2.11
Limited attribution: Indicators of effectiveness at the sector level are available and can be used in ascertaining performance, but changes in them could not be attributed confidently to Bank interventions.	=	2.11
Limited financial value-added: The Bank’s loan interest cost advantage relative to alternative financing is tending towards zero.	▽	2.8
Limited technical value-added: From the line ministries’ viewpoint, the net value of the Bank’s loans, defined as the value of knowledge transfer minus the value of the extra work involved in dealing with an international institution, is negative.	△	Ch. IV
Operations implementation		
Average implementation efficiency: Aggregate disbursement performance (time and cost) is just about the Bank’s average.	△	3.8
Flexibility of products and procedures: The Bank has increased its use of policy-based loans and other investment products that have an innovative design and disburse more quickly, and has made loan execution procedures more flexible by using ex post rather than ex ante monitoring control.	△	3.4
2. Recommendations		
Identify a market niche. The Bank should work with the country to identify a limited range of areas of action in which it can construct measurable goals, the achievement of which can be effectively monitored. Such a niche focus will enable the Bank to effectively marshal its resources to provide technical services in addition to financial services.	=	2.37
Strengthen transparency: A niche focus will make demonstrable outcomes and transparency possible, and accountability will make such outcomes likely.	=	3.11
Make the programming process a performance-based agreement with the country: The Bank should make country programming papers negotiated performance agreements with the government.	=	2.11

Improve project design and information on progress toward set goals. This will enhance accountability. Projects should provide comprehensive statements of objectives and define indicators, baselines, and the corresponding milestones.	=	2.12
Introduce a pro-poor tilt to all Bank operations. The Bank should consider instituting a demonstrable pro-poor tilt to subsequent interventions in any of the sectors that the Bank and the country agree upon.	=	Ch. IV
(*) Legend: = Still fully applicable. ▽ Evidence of improvement in at least one of the programming areas. △ Evidence of worsening.		

Endnotes

[1] Data source: OECD Economic Survey (Mexico), September 2007.

[2] Moody's, Standard & Poor's, and Fitch IBCA.

[3] This point can be illustrated by analyzing the correlation between Mexico's sovereign risk indicators and those of other countries in the region. Taking as a baseline the date of the first upgrade to investment grade, the degree of co-movement between Mexico's daily sovereign risk indicator and those of comparable countries decreased substantially and even turned negative over time. This is a clear sign of stability and the fact that the markets were beginning to view Mexican debt offerings as a different kind of asset that was attractive relative to comparable economies' debt.

Correlation coefficients between daily Mexican sovereign risk spreads and selected emerging market spreads, before and after the July 2000 upgrade to investment grade

	Argentina	Brazil	Venezuela	Turkey	EMBI+	EMBI+ Lat Am
2 years before	82.7%	91.4%	81.5%	84.5%	89.7%	94.3%
1 year before	88.5%	97.5%	65.9%	84.5%	93.4%	97.4%
1 year later	1.5%	1.9%	62.6%	49.8%	46.7%	17.7%
2 years later	-70.0%	6.9%	-11.0%	48.2%	57.5%	15.7%

Source: JP Morgan EMBI+ Index; OVE calculations.

[4] In its 2004 Country Assistance Strategy, the World Bank calculates that even with 3.5% yearly per capita growth it was unlikely Mexico could reach the Millennium Goal of halving extreme poverty between 1990 and 2015, *ceteris paribus*. To achieve this target, per capita growth would need to average 5% per year, which has not happened since the 1970s.

[5] According to the May 2005 IMF Working Paper WP/05/93, *GDP Growth, Potential Output, and Output Gaps in Mexico*, which includes a quantitative analysis through 2003, the reasons why TFP has not recovered despite the reforms enacted are as follows: (i) the reforms were incomplete in some sectors; (ii) there is still some degree of financial sector repression, and (iii) there are distortions in the labor market.

[6] Although the oil sector accounts for a smaller proportion of the economy than in other oil exporting countries (Mexican oil exports amounted to 4.2% of GDP in 2005, compared to a range of 15%-50% in

most large oil exporters), its effect on fiscal accounts is greater because Mexico's oil sector is entirely public and nonoil tax revenue is relatively modest. In 2005, nontax oil revenues (oil duties) equaled 61% of federal government nonoil tax revenue (which in turn amounted to 9.7% of GDP). In that year, PEMEX revenues equaled 36% of total public sector revenues, oil duty payments 26%.

7 Virtually three quarters of this reduction would be explained by the cut in gasoline tax to shield consumers from world price hikes, the other quarter by the lowering of income tax rates in 2004.

8 In its 2005 Article IV Review, the IMF calculated that Mexico and China are direct competitors in roughly half of the commodities they export to the United States, which represent nearly 75% of the exports of each of these countries to the United States.

9 The net annual flow of migrant workers to the United States is estimated to have grown more than fifteen-fold, from 26,000 yearly in the 1970s to nearly 400,000 people today (CONAPO, 2006)—one of the highest rates of labor emigration in the world. These figures mean that labor emigration has relieved some labor supply pressure in the Mexican job market. If the population that migrated each year to the United States had remained in the country's employment market, the rate of growth of Mexico's labor force would have been an estimated 0.7% higher (OECD, 2004).

10 In general, labor productivity growth—measured with National Employment Survey data—has been very low in recent years.

11 Miguel Székely *et al.* (2005). *Poniendo a la pobreza de ingresos y a la desigualdad en el mapa de México* (Putting income poverty and inequality on the Mexican map). Graduate School of Public Administration and Public Policy, ITESM. States with high poverty levels: Chiapas, Oaxaca, Guerrero, Veracruz, Puebla, Campeche, Yucatán, Hidalgo, and San Luis Potosí. States with medium poverty levels: Tabasco, Tlaxcala, Zacatecas, Michoacán, Mexico State, Durango, Nayarit, Querétaro, Guanajuato, Quintana Roo, Sinaloa, Jalisco, and Morelos. States with low poverty rates: Baja California, Federal District, Nuevo León, Baja California Sur, Chihuahua, Colima, Sonora, Tamaulipas, Aguascalientes, and Coahuila.

12 Sedesol (2006). *Sexto Informe de Labores* (Sixth report on activities), p. 114.

13 The relation between marginality and voting preference is observed also when *municipios* are ranked by poverty levels. This reveals a polarized voting pattern: the poorest *municipios*, with poverty rates above 30%, vote mainly for the leading opposition party. In *municipios* with poverty rates between 10% and 30% there is no dominant party preference; *municipios* with the lowest levels of poverty tend to vote for the governing party.

14 Only half the population has social security coverage. The *Seguro Popular* (public health insurance plan for people without insurance), a complementary program that is currently expanding its coverage, also faces a challenge to improve the quality of the corresponding health services. The expansion of the *Seguro Popular* scheme is a step forward, but its aim of universal coverage would involve a considerable cost to the Treasury, estimated at 0.8% of GDP annually.

15 The *Progresa-Oportunidades* program has been operating for over 10 years with a mission to break the intergenerational transmission of poverty. The *Seguro Popular de Salud* was launched in 2001 to cover basic health risks and prevent household economies from collapsing when unexpected illnesses occur.

16 For a detailed analysis of these issues, the Bank published the report *Has Globalization Deepened Income Inequality in Mexico?* authored by Fernando Borraz and Ernesto López Córdova (2004), Inter-American Development Bank (IDB), which served as a basis for the sector note entitled *Integración y Competitividad* (Integration and competitiveness) (IDB, Ernesto López Córdoba, 2006).

17 These figures only consider FDI flows into tradable sectors (agriculture, mining, and manufacturing industry). Information on the distribution of FDI by state may overstate the proportion received by the

Federal District, if the data reported refer to the tax domicile of the firm receiving the foreign capital rather than the domicile of establishments belonging to a firm that actually receive the flows in question. This tends to be more of a problem in the services sector.

[18] The Bank subscribed to this aspect of the PPP principles, making it a core objective of its integration support program to further productivity growth in the southern states by developing their links with Central America.

[19] Lack of accountability is a reasonable concern, e.g. in the case of funding programs such as FAIS for small-scale infrastructures, or FAEB for education.

[20] In the FAEB case, for example, the reform proposes that the increase in transfers be distributed among states according to school enrollments (and a quality index to be developed by the Education Ministry).

[21] March 2006 figures show that loans to the states made up 33% of consolidated commercial bank lending, a figure that jumps to 180% when only the government sector is considered. The system has 710 branch banks and employs 6,051 people. Development bank financial ratios are comparable to those of private commercial banks: an estimated arrears rate of 2% in June 2006 (compared to 1.8% for private commercial banks); a loan loss provisioning index of 220.4 (compared to 229.3), and a capital ratio of 16.2 (compared to 14.5%). The six institutions also produce net profits, with a return on assets (ROA) of 0.68% and a 9.32% return on average equity (ROE). Nonetheless, development bank lending still is biased toward the public sector, which is these banks' main client: in July 2006 the public sector captured 43.2% of development bank lending to nonbank sectors (33.2% excluding subnational governments). This pattern is corroborated by analyzing domestic corporate financing (not counting consumer and housing loans): at end-2005 development banks were providing a mere 2% of corporate finance (down from 4.3% in late 2001), or 8.4% when only bank credit is considered.

[22] The view of the Mexican government on these issues can be found in Pronafide, which states that development banks should promote soundly-based financing alternatives for projects that are not supported by capital markets and cannot borrow from commercial banks because of information problems, transaction costs or other market imperfections, always seeking to ensure that development bank interventions are second-tier and do not impair their capital.

[23] Since the 1994 withdrawal of private financial institutions from the housing market, substantial progress has been made in improving the operating efficiency of that market in Mexico, but enlarging it to reach low-income families is still a challenge.

[24] According to the report entitled *Situación del medio ambiente en México 2005* (State of the Environment in Mexico, 2005) (SEMARNAT), nationwide potable water coverage rose from 87.8% in 2000 to 89.4% in 2003 (above the estimated average for Latin America and the Caribbean, which is around 85%, according to UNEP data).

[25] An estimated 6.8 million rural residents do not have safe water supply systems and 10 million people are without adequate sanitation, according to the report *Agua potable y saneamiento: en busca de mayor cobertura, eficiencia, equidad y sostenibilidad* (Drinking water and sanitation: in pursuit of greater coverage, efficiency, equity, and sustainability). Policy Note - IDB, September 2006.

[26] Objectives defined in Annex I: Outcomes table in the document *Mexico. Country Paper* (CP-1305).

[27] Defined as the difference between the gross national saving rate and gross investment rate, as the rate of gross fixed capital formation.

[28] This fact, supported by prudential economic policy management, has provided Mexico with a financial cushion during episodes of crisis. In fact, in terms of duration and intensity the Mexican recession of 2000 can be considered the most benign economic slowdown in decades, pointing up the effectiveness of the new mechanisms for accessing liquidity at times of crisis.

[29] Compared to the analysis in document RE-309 (*Report on the evaluability of Bank country strategies*) the evaluability index of the strategy with Mexico is below average (0.18).

Country strategy	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**Average**	**Mexico**
Evaluability index	0.05	0.08	0.08	0.01	0.41	0.41	0.21	0.31	0.11	0.08	0.18	0.18	0.16

Source: Document RE-309

[30] The sample of CPEs reveals an anticipation rate with a median of 42% in number terms and 58% in terms of amount.

[31] Paragraph 4.8 of the document *Mexico. Country Paper* (CP-1305).

[32] These are the only three programs in the portfolio that were part of the system instituted by the Office of the President of the Republic for Monitoring the Presidential Targets.

[33] Paragraphs 4.9 and 4.10 of the document *Mexico. Country Paper (*CP-1305).

[34] In 2000, the World Bank (*Mexico: A Comprehensive Development Agenda for the New Era*) considered four aspects: protecting vulnerable groups, providing them with basic inputs to increase their productivity, removing labor market distortions and encouraging migration from the informal to the formal employment sector, and sensitivity to the needs of specific groups such as women and indigenous people.

[35] Paragraph 4.14 of the document *Mexico. Country Paper* (CP-1305).

[36] The PPP framework proposes eight initiatives, including the Meso-American Sustainable Development Initiative, anchored in the principles of the Meso-American Biological Corridor and the environmental priorities contained in the Environmental Plan of the Central American Region.

[37] Paragraphs 4.15-4.18 of the document *Mexico. Country Paper* (CP-1305).

[38] Paragraph 4.19 of the document *Mexico. Country Paper* (CP-1305).

[39] Nonetheless, the only outcome indicator it proposes concerns the capturing of private sector credit.

[40] The government's vision is laid out in Pronafide, where it states that development banks should promote soundly-based funding alternatives for projects that are not supported by capital markets and which, because of problems of information, transaction costs, or other market imperfections, cannot obtain commercial bank loans, endeavoring always to ensure that development bank interventions are second-tier and do not impair their capital.

[41] Paragraph 4.22 of the document *Mexico. Country Paper* (CP-1305).

[42] Eighth General Increase in Resources of 1994.

[43] In sharp contrast to the World Bank's approach outlined in 2001 and in its strategy for Mexico, which assumes that the objectives for other (sector level) issues cannot be achieved successfully unless environmental sustainability considerations are mainstreamed into the development agenda (World Bank, 2001, p. 117). Accordingly, the World Bank proposes to integrate environmental protection and economic development, overcoming the sector-specific approach to environmental issues to strike a balance between economic growth, poverty reduction, and environmental protection, as a basis for achieving sustainable development.

[44] As references to practice, in chapter V of this evaluation report we isolate the Bank's technical contribution to enhancing outcomes in programs where such contributions have been delivered.

[45] The World Bank's analytical and advisory work expanded from three reports produced between 1990 and 2000 to 20 reports between 2001 and 2007. These include eight economic reports (in the areas of fiscal transparency, social protection, public expenditure at the federal and subnational level); seven sector reports (in the areas of financial services, democracy, education, and competitiveness); four sustainable development reports (energy efficiency, renewable energy, and forest management); and the Country Financial Assessment.

[46] Definition from Ramón Tamames, *Diccionario de Economía y Finanzas*, 13th edition, Alianza Editorial, 2006.

[47] In the social area, NLPs are distributed as follows: two evaluations of the *Progresa* program (RES-SDS), one evaluation of the Small Projects Program (SDS), one OVE evaluation of benefits for indigenous peoples, two employment and labor market studies (SDS-RES), and one regional dialogue on social inclusion (SDS).

[48] In the integration area, four NAFTA-related studies were financed and two studies on inequality, all produced by the Integration Department.

[49] These preparation times are similar to those observed in Colombia or Brazil, but are twice as long as in Peru and three times longer than in Argentina.

[50] By lending product: 14 months for investment loans, 12 months for multiphase loans, and 8 months for budget support. One noteworthy finding is that in the case of multiphase loans, contrary to what one might expect, second phases take longer than first phases.

[51] The Presidential Targets System established a system for continuous tracking of outcomes of programs designated as priorities by the Office of the President of Mexico for each of the ministries directly involved, for the 2001-2006 government term.

[52] The administrative arrangements agreed upon for this investment program with the Government of Mexico also give the latter responsibility for ex ante fiduciary supervision. As noted in chapter III of this report, this has resulted in positive comparative performance and a reduction in transaction costs associated with program implementation. In Mexico, the fiscal agent—in this case *Nacional Financiera*—assumes responsibilities.

[53] Annex 1 contains a summary of the main evaluations examined for the outcome analysis presented in this section.

[54] *Eficiencia Redistributiva de los Programas contra la Pobreza en México* [Redistributional efficiency of pro-poor programs in Mexico], CIDE, November 2005.

[55] Office of the President of Mexico, 2006.

[56] CIDE (2005), op. cit.

[57] By definition, "inclusion error" means fewer resources available to poor beneficiaries which, added to other costs of programs that ultimately reach the poorest population groups, are a key element in calculating expenditure efficiency. In the case of the *Oportunidades* program, each percentage point reduction in inclusion error saves the Treasury US$30 million a year.

[58] The most recent evaluations reveal a 16% reduction in the number of rural dwellers living below the extreme poverty line and a slightly lower decline in urban areas. See Cortes, Solis, and Banegas (2006).

[59] The impact on consumption is over 10%, particularly for food. See Angelucci, Attanasio, and Shaw (2004) and Angelucci and De Giorgi (2006).

[60] Based on data from household surveys in 2002, 2004, and 2006. Poverty defined in terms of net monthly per capita income, deflated at August each year. Urban: localities with populations of 15,000 and up.

[61] Behrman, Sengupta, and Todd (2005).

[62] Gertler, Martínez, and Rubio (2005).

[63] Angelucci (2005) and Rubalcava and Teruel (2005).

[64] Davis, Handa, and Soto (2001); Davila and Levy (2003).

[65] See Levy and Rodríguez (2005) and Levy (2006).

[66] See CIDE (2005), op. cit.

[67] Based on data from household surveys for 2002, 2004, and 2006. Poverty defined as net monthly per capita income, deflated at August each year. Rural: Localities with populations below 15,000.

[68] Only 11.4% of *Procampo* beneficiaries participate in this modality, and smaller than expected benefits have been achieved in terms of transforming production patterns and crop diversification. No significant employment or export effect was observed. And, predictably, when all potential program benefits are subsumed in a single impact index there is an increasing positive correlation between number of hectares in a beneficiary's possession and the program's output impact index, and an inversely proportional correlation to the financial market access index.

[69] The requirement to limit resources for payments and scholarships to educational institutions (*Figuras Educativas—FEs*) had negative consequences for the program. These design failures are evidenced in the reallocation of funds towards payment to FEs and slow disbursement, which has taken implementation to the five-year limit: (a) In 2004, US$24 million was reallocated from "Contingencies" to "Subsidies and Transfers to FEs," increasing that share of the total loan amount from 54% to 65%; (b) in 2005, US$2.1 million was transferred from the "Inspection and Supervision Charge" line under "Financial Costs" to "Contingencies;" (c) in 2006, the US$2.1 million contingencies allotment, together with US$720,000 for audits, US$511,000 for evaluations, US$11.4 million for institutional strengthening (69% of the original budget), and US$24 million for nonrecurrent expenses of the rural community education component—a total of US$36.8 million—were transferred to "Subsidies and Transfers to FEs," raising that line to US$174 million, or 83% of the program's budget. Although these adjustments display the Bank's flexibility to facilitate implementation, they also evince an unrealistic design not well suited to CONAFE needs.

[70] The loan document sets out several coverage targets: at the end of phase I, coverage rates are to increase 21% at the preschool level, 5% in primary education, and 45% for education services for adults who never completed the full basic education cycle. These targets were reset in the June/July 2004 administration mission, 33%, -7%, and 249%, respectively. This change in targets bespeaks a planning failure, since the decrease in the age 5-to-14 population cited as the rationale is a secular trend.

[71] As an indicator of the quality of education delivered, the project's logical framework targets a 7% improvement in Education Ministry standardized test results for CONAFE primary school students by the end of phase I. According to the PPMR, data published in November 2005 reported on primary education achievement in CONAFE community programs. That report compares 2000 and 2005 reading comprehension and mathematics scores of grade-six students, in the case of CONAFE equivalent to level-III students. The nationwide mean reading comprehension score of sixth-grade students in community programs was 467.70 in 2000 and 471.93 in 2005, i.e. a 4.23-point improvement. In mathematics, the national mean was 466.70 in 2000 and 470.43 in 2005, an increase of 3.72 points. But the study reaches a different conclusion: regarding reading comprehension, "The most significant changes observed at the primary level are in private schools, followed by indigenous, urban public and rural public schools. In community programs no significant changes were observed over these five years." In the case of mathematics, the report concludes that "The most significant changes observed at the primary level are in private schools, followed by indigenous and urban public schools. No significant changes were observed during the period in community programs or in rural schools."

[72] For example, in 2002, 2003, and 2004, the Finance Ministry ultimately approved just 77%, 59%, and 55%, respectively, of the funding budgeted for the PACE program.

[73] One of the project's logical framework goals was a 20% reduction in employers' recruitment costs and shortening of the job-search period for the unemployed. But, in the framework of evaluations performed in phase I, the only available estimates relate to time spent in job search. See OVE (2006), *Impact Evaluation of Job Training in Mexico.*

[74] The outcomes of the earlier World Bank-funded program were unsatisfactory. That agency's Implementation Completion Report (ICR) is more negative on the Technical Education and Training Modernization Project. Although that report was published a fortnight after the 2004 approval, the project report mentions that the IDB participated in the last World Bank project administration mission. At first glance, the ICR criticisms of the design are applicable to the IDB's program design, in terms of the lack of a solid diagnostic of the program's relevance and feasibility—business community demand for training, private-sector commitment to the system, feasibility of modernizing higher technical secondary education by adopting these systems—and institutional implementing capacities. This is all the more important given the inherent institutional complexity of the project. The last Technical Education and Training Modernization Project administration mission did not have access to key studies containing essential information on the impacts and performance of the employment competencies system. These studies were not produced by the IDB in the design stage, but rather are part of the program. Accordingly, the Bank did not proceed on a solid foundation.

[75] In 2007 OVE is preparing an evaluation of the PPP, looking at the set of programs funded under that initiative.

[76] The Bank's primary support and role in decentralization has been through Banobras. The Bank has funded three operations in recent years. The first, in 1999, contained an investment component and a fast-disbursing component. The fast-disbursing portion included measures to revamp Banobras, ranging from credit policies to human resources. The investment component was intended to finance subnational government projects, but it too contained provisions to strengthen financial and administrative management in those governments, particularly relating to implementation of the newly created social-expenditure budget line called *Ramo 33*. No specific indicators are identified for the investment component.

[77] Although the *municipio* coverage targets were attained, funds were not targeted on *municipios* with high levels of marginalization as envisaged in the loan document. According to the Banobras Annual Report, in 2005 the institution provided services to 531 *municipios* (a record for this bank), which denotes a certain level of maturity and financial soundness. The authorities acknowledge that, despite this record Banobras performance, about 1,600 *municipios* still have no viable finance alternatives.

[78] In mid-2007, after the period encompassed by this evaluation, the private-sector window approved the first IDB operation in the sector (ME-L1015), a US$400 million partial credit guarantee for a toll-road concession in the state of Guadalajara, marking a revival of the private-sector portfolio in Mexico.

[79] Nonetheless, the World Bank's contribution to that institution has been greater in volume terms, having financed basic services infrastructure.

[80] June 2006 figures show net earnings of 226 million pesos. The bank has reserves in excess of the required provisionings and some of its financial ratios are superior even to development bank numbers, such as a loan loss provisioning index of 232%, capital to risk-weighted earning assets (min.) of 6.8%, an operational efficiency index of 3.9%, and an ROA of 2.2%. Others are slightly below that standard, such as an arrears rate of 3.5% and an ROE of 2.2%.

[81] The PBL conditions did address issues of the subsidiary role of the State and strive to come up with the best solution. The first-tier function of FR was justified politically and technically by the sudden disappearance of Banrural and the existence of an unsatisfied market. It was clearly stated that the Bank's

program aimed to reduce the number of distortions, not completely eliminate them. The gradual disappearance of that function was also envisaged, to eventually concentrate on second-tier functions. Lastly, a potentially controversial issue was addressed involving subsidized interest rates and the promotion of private-sector intermediary engagement in rural areas. Particularly noteworthy was the Bank's support for the pricing of all credit products based on the cost of capital, operational and administration costs, and risk spread.

[82] In 2002, the MIF financed technical assistance to help 1,000 institutions adapt to current legislation, for the technological upgrading of Bansefi, and for development of new savings products. In 2005, it funded preliminary steps for the sale of Bansefi equity to community saving and loan sector operators; and in 2006 it supported the creation of a pension fund management company (AFORE) for population groups that have no retirement pension fund.

[83] In 1995, a US$750 million PBL was approved to help Mexico recover from the late-1994 crisis. In 2000 the Bank approved a US$250 million sector loan to continue supporting the recovery and development of the banking sector. More recently, in August 2005, a US$600 million PBL was approved to deepen financial markets.

[84] Government programs include subsidized loans through programs for private and public sector employees, such as the National Workers Housing Fund Institute (INFONAVIT) and the Housing Fund of the Social Security Institute for Government Employees (FOVISSSTE), both managed by the mortgage finance company Sociedad Hipotecaria Financiera (SHF). Other similar programs include the National Trust Fund for Social Housing (FONHAPO) and funding through Limited Purpose Financial Companies (SOFOLES). National Housing Commission data show that the main player in the housing sector is INFONAVIT (57% of new homes), followed by the programs of SHF (12%), FOVISSSTE (11%), SOFOLES (6%), and FONHAPO (5%).

[85] Initially the PPMR attempted to track efficiency outcomes (mortgage spreads) and equity outcomes (percentage of groups benefiting from the program by income level). But these data disappear in subsequent PPMRs, which only cover outputs (number of homes delivered), this being entirely insufficient to verify delivery of the project's initial objectives of efficiency and equity.

[86] ME-0137 consists mainly of an investment component and a much smaller technical assistance component. It aims to achieve these objectives by consolidating the reform of the second-tier mortgage finance institution FOVI and by financing subsidies and mortgages. The original executing agency was Banobras, which was replaced by SHF in 2002.

[87] No evaluation has been done of this operation. In 2006 the World Bank evaluated a similar program (*"Tu Casa")* using treatment and control groups. According to the study's authors, the findings show that the beneficiaries are living in nicer houses built with better quality materials, and are more satisfied with the quality of their homes. But the new neighborhoods are substantially worse: worse access to services, violence, distance from work, etc. The housing subsidies thus have an impact on housing quality but this impact is diluted by access to services.

[88] Program for the Sustainability of Drinking Water and Sanitation Services in Rural Communities, managed by the National Water Commission of Mexico.

[89] It should be noted that the evaluation team had access only to 10% of the 2000 census findings and some 2005 municipal household and marginalization means (figures produced by the National Council for Social Development Policy Evaluation—CONEVAL). Consequently, the impact estimate obtained understates the *average treatment effect on the treated* (ATT effect) because only a fraction of the localities of a *municipio* were treated. The parameter more closely resembles what the impact literature refers to as *intent to treat* (ITT), which is the average treatment effect on a group when only a fraction of them actually received treatment. If one uses the algorithm proposed by Bloom et al. (2005) to weight the

ITT by the fraction of localities treated, the impact parameter rises toward a 0.14-point reduction in sanitation unmet basic needs (a change from 0.011 to 0.140).

[90] Using data such as the carbon content of fossil fuels combusted and composition of the power generation grid, according to the methodology of the Intergovernmental Panel on Climate Change (IPCC).

[91] For the moment it has only been possible to ascertain that CO_2 emissions, relative to the total cost of projects in the Bank's PRI portfolio, are comparable to the EBRD portfolio.

[92] This saving was counted in a cost-benefit analysis that looked at aggregate annual investment for the program and the price of avoided electricity consumption, setting a baseline for this type of innovative program.