



1. Project Data:		Date Posted : 09/15/2004	
PROJ ID: P074539		Appraisal	Actual
Project Name: Programmatic Environment Structural Adjustment Loan	Project Costs (US\$M)	202	202
Country: Mexico	Loan/Credit (US\$M)	202	202
Sector(s): Board: ENV - General public administration sector (50%), Other industry (15%), General water sanitation and flood protection sec (15%), Forestry (10%), General energy sector (10%)	Cofinancing (US\$M)	0	0
L/C Number: L7136			
	Board Approval (FY)		03
Partners involved :	Closing Date	10/31/2003	12/31/2003
Prepared by :	Reviewed by :	Group Manager :	Group:
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2. Project Objectives and Components			
a. Objectives			
This first operation (EnvSAL I) was envisaged as the first of three SALs to support Mexico's Environment and Natural Resources Program. The Bank decided to focus on two areas: "mainstreaming" of environmental concerns in four key sectors (water, energy, forestry and tourism); and, improving local environmental management through decentralization and public awareness.			
<u>For the Program as a whole:</u> To balance socio-economic development with environmental protection and improvement.			
<u>For this First Operation:</u>			
Sub-Objective A: Mainstreaming of Environmental Concerns in Sectoral Development Agenda			
1. Target setting and inter-institutional coordination.			
2. Water: a) national water program; and, b) increase incentives for conservation and resources for investment.			
3. Tourism: decrease over-exploitation of and increase investments in national tourism resources.			
Sub-Objective B: Improving the Effectiveness of Environmental Management Processes			
1. Decentralization of environmental management.			
2. Financing.			
3. Public participation and transparency.			
b. Components			
EnvSAL I had two tranches linked to specific actions in the water and tourism sectors, as well as on target setting and inter-institutional coordination, decentralization of environmental management (including financing), and public participation.			
c. Comments on Project Cost, Financing and Dates			
The two tranches consisted of US\$ 101.01 million each, disbursed in December 2002 and December 2003 respectively.			
3. Achievement of Relevant Objectives:			
This first operation (EnvSAL 1) made progress toward the overall Program objective and its specific targets were close to full achievement. All sub-objectives were achieved, possibly with the exception of Sub -Objective B.1, which will be evaluated during the planned OED assessment.			

All conditions for first tranche release were met prior to Board presentation . The projected date for the second tranche release was apparently not achieved . According to the ICR, the second tranche release required waivers on three points, which were approved by the Board, as required under OD 8.60, on December 18, 2003. One of the waivers was a technicality, while the other two were of more substance related to Sub -Objective B.1, i.e., the lack of independent certification of certain functions (2 out of 10) of the environment agency, as a prelude to decentralization of those functions to the states . Certification was originally described in the PD as a key element of the decentralization that is central to the overall Program . At project closing, however, the ICR indicated that "the Government has decided to de-link certification from the decentralization process " (in discussing this ICR Review, the region clarified that the current strategy is "demand-driven decentralization", the pace of which is determined by the readiness and commitment of various states). As this is only briefly discussed in the short Simplified ICR format, the OED assessment will analyze whether this de-linking is a material departure, which remains unclear .

4. Significant Outcomes/Impacts:

1. Increase in the revenues from "water fees" collected at the municipal level and their return to the municipalities to finance "hydraulic works" (presumably water supply and sewerage systems"). Such collections increased from 24% of the "concessional water use by volume" to 58% by the time of the second tranche release . In discussing this ICR Review, the region indicated that the improved collection of water fees represents an important behavioral change, given that the legal requirement for such charges were generally ignored in the past . Taking into account ongoing basin studies to scale up this initial experience, the OED assessment will evaluate the significance of this achievement in economic terms (resource conservation) and fiscal (generating funds for investment), as the present amounts involved do not seem large (\$44 million at present) in the context of Mexico's overall economy .
2. Establishment of inter-institutional coordination mechanisms between the environment agency and the energy, forestry, water and tourism sectors. This is clearly a key step in improved environmental management .
3. Improved public access to environmental information . Again, this is a pre-requisite to effective environmental management.
4. Preparation and publication of decentralization plans for "at least 20" states was a noteworthy achievement, given that decentralization is an important objective of the Program and the necessity of decentralization if Mexico is to upgrade its federal system of environmental protection .

5. Significant Shortcomings (including non-compliance with safeguard policies):

While the Bank's strategy of focusing this first operation on two areas (sectoral mainstreaming and improving local environmental management) appears to have been basically sound, some questions with program design arise partly because of the brief analysis in the PD . In discussing this ICR Review, the region indicated a number of studies that underpin program design, especially policy notes to the new administration in 2000 and the OECD study. The PD lists these studies but does not present their conclusions, hence, a comprehensive reference document similar to a Bank sector study is not available . The OED assessment will review the following issues :

The choice of lending instrument: The PD itself does not discuss which alternatives were considered, e .g., an investment loan (cf. the recently completed Northern Environment Project, which had considerable success in decentralizing environmental management); a SAL plus TA loan (as suggested by the ICR), or a policy-based loan with greater or lesser conditionality or number of tranches . The rationale for the final choices, which was reportedly the government's, was not apparent in the PD or the ICR . The region indicated that the alternatives considered during preparation were: an environmental management investment loan; an APL; an environmental SECAL; a single environmental SAL; and a programmatic environmental SAL with only one tranche in the first operation . The region further indicated that the discussion on choice of instrument was discussed and recorded at the EnvSAL's Concept Review Meeting, and that a SAL was chosen - rather than a SECAL - because environment is a "theme" in the Bank and now a sector, and because of the broad, multisectoral nature of the operation .

Absence of enforcement components: The OED assessment will analyze enforcement aspects that remain to be implemented in the Program, as enforcement or pollution fees and fines were not included in designing the policy package for this first operation .

Policy Package v.s. Size of the Loan: The policy package adopted for this first operation appears rather modest compared with the size of the loan, consisting mainly of legal amendments and administrative actions, with the possible exception of improved collection of water fees . The OED assessment will evaluate the meaningfulness of these measures, particularly in terms of Government commitment to long-term reform. OED will also analyze whether the initial, modest amount of water fees collected was offset by forgiveness of past arrears and the return of the funds to the municipalities as matching grants for new investments .

Governance Issues: The EnvSAL 1 did not mention or attempt to address systemic governance issues like frequent reorganizations and cumbersome budgetary procedures which impeded, for example, the Northern Border Environment Project. The region noted that such problems are often brought on by poor performance by the states and that this issue was better addressed via other channels, an issue which the OED assessment will address .

Subsidies: The EnvSAL 1 did not do much about the environmental impact of subsidies in fuel, power, water and

agricultural inputs. Though valuable work is planned for the second and third operations, this does not appear to include the question of subsidies, reduction of which would appear to be a normal objective for a SAL .

Safeguards. The OD 8.60 in effect at appraisal considered it good practice for Bank staff "to review environmental policies and practices in the country, take account of any relevant findings and recommendations of such reviews in the design of structural adjustment programs, and identify the linkages between various reforms proposed and the environment". The Bank's analysis of these in the PD was rather pro forma and did not for example, trace through the effects of improving collection of water fees on water resources management . In fact, water conservation benefits are claimed, whereas one might expect that the recycling of the fees as capital grants might encourage municipalities to use more water. Admittedly, given the modest content of the policy package in this first operation , it is hard to see that major social or environmental impacts would have occurred during its short timeframe . The subject is not addressed in the ICR and will be pursued in the proposed PPAR (see below).

6. Ratings :	ICR	OED Review	Reason for Disagreement /Comments
Outcome :	Satisfactory	Satisfactory	The operation met nearly all its objectives, modest as they were.
Institutional Dev .:	Substantial	Modest	ID objectives related mainly to decentralization and "mainstreaming" through the ITWGs. The ICR does not provide sufficient evidence of substantial, tangible institutional achievements and benefits. (The Region subsequently commented that the ITWGs are fully functioning and adequately staffed, providing opportunity for inter-institutional cross-fertilization across sectors.)
Sustainability :	Likely	Likely	However, there is no detailed discussion of the subject in the ICR. In fact, several things are mentioned which cast doubt on sustainability: the Government's abandonment of independent certification; the reluctance of the ITWGs to meet; and, Government scepticism with the ITWGs and their outputs. Nevertheless, the Government's recent decision to move ahead with the second operation may signal a renewed commitment to the Program and thus point to the sustainability of the gains made in the first operation.
Bank Performance :	Satisfactory	Satisfactory	However, despite the Bank's devoting substantial resources to program and loan design and implementation and the complexity of the issues addressed, a number of questions remain, especially regarding program design (see Section 5).
Borrower Perf .:	Satisfactory	Satisfactory	However, the sluggish performance of ITWGs, second thoughts on certification, and the lack of progress reports . are apparent shortcomings which need further investigation.
Quality of ICR :		Satisfactory	

NOTE: ICR rating values flagged with "*" don't comply with OP/BP 13.55, but are listed for completeness.

7. Lessons of Broad Applicability:

1. Documentation on "new-style" programmatic operations, especially in new areas like the environment, need to balance the discussion of process with more information on the underlying substance - in this case, issues like subsidies, water fees, certification, decentralization plans etc .
2. In the case of Mexico, Bank lending is not additional to the government's budget and merely substitutes for other funds. This would appear to severely limit the Bank's leverage and make it challenging to address the more difficult

policy questions.

8. Assessment Recommended? Yes No

Why? As the first use of the programmatic SAL instrument in the environmental area, this operation deserves more in-depth review than a Simplified ICR. Questions to pursue include, *inter alia*:

- How adequately do the Program and the first loan address Mexico's environmental priorities? Does the Program need to be revised?
- How committed is the Government to the original Program? Are there or should there be new priorities?
- What exactly is third party certification, did it add value in this operation, should the missing certifications be pursued and what is the Bank's view of the government's decision not to continue with certification?
- How much has been achieved under decentralization of environmental management functions to the states under this operation and other Bank activities?
- Did the first operation have any negative social or environmental impacts?

9. Comments on Quality of ICR:

The Simplified ICR complies with and is longer than what the (recently-issued) guidelines call for, and covers all the basic facts on the project and its achievements. However, due to format limitations, a number of questions remain unanswered by the Simplified ICR, which will be pursued in the proposed assessment (see above)