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USAID/MEXICO MUNICIPAL DEVELOPMENT THROUGH INFRASTRUCTURE FINANCING ACTIVITY: A PERFORMANCE EVALUATION

MARCH 6, 2019

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Contracted under AID-OAA-M-13-00017

E3 Analytics and Evaluation Project

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Prepared for the United States Agency for International Development, USAID Contract Number AID-OAA-M-13-00017, Task Order Number REQ-EGEE-13-000174, Evaluation of the USAID/Mexico Clean Energy Activity: Design and Work Plan

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ACRONYMS

BB	Bond bank
CAPA	<i>Comisión de Agua Potable y Alcantarillado</i> (Quinta Roo's water and sewer utilities corporation)
CENACE	<i>Centro Nacional de Control de la Energía</i> (The National Energy Control Center)
CFE	<i>Comisión Federal de Electricidad</i> (Federal Electricity Commission)
CNBV	<i>Comisión Nacional Bancaria y de Valores</i> (National Banking and Securities Commission)
CRE	<i>Comisión Reguladora de Energía</i> (Energy Regulatory Commission)
dTS	Development and Training Services, Inc.
EC-LEDs	Enhancing Capacity for Low Emission Development Strategies Initiative
EDII	Evensen Dodge International, Inc.
FONDEN	<i>Fondo de Desastres Naturales</i> (Natural Disaster Fund)
GDA	Global Development Alliance
GoM	Government of Mexico
IDEFIN	Institute for the Development and Financing of the State
INDETEC	<i>Instituto para el Desarrollo Técnico de las Haciendas Públicas</i> (Institute for the Technical Development of Public Treasuries)
IP	Implementing Partner
IPADE	<i>Instituto Panamericano de Alta Dirección de Empresa, de la Universidad Panamericana</i> (Pan-American University's business school)
MLED-II	Mexico Low Emissions Development II Program
NAFTA	North American Free Trade Agreement
NAST	National Association of State Treasurers
OECD	Organisation for Economic Cooperation and Development
PPP	Public-Private Partnership
PPIAF	Public-Private Investment Advisory Facility
PRI	<i>Partido Revolucionario Institucional</i> (Institutional Revolutionary Party)
RQ	Research Question
SDG	Sustainable Development Goals
SHCP	<i>Secretaría de Hacienda y Crédito Público</i> (Secretary of Finance and Public Credit)
SOF	Secretary of Finance
SoH	State of Hidalgo
SoM	State of Michoacán
SoQR	State of Quintana Roo
SoV	State of Veracruz
SOW	Scope of Work

SPV
USAID
USG

Special Purpose Vehicle
United States Agency for International Development
United States Government

ABSTRACT

The United States Agency for International Development (USAID) commissioned this evaluation to assess the effectiveness of Evensen Dodge International Inc.'s (EDII) Municipal Development through Infrastructure Financing Activity. The report examines EDII's contributions in: i) increasing funding for public works projects at the subnational level using good financial practices with appropriate legal structures to facilitate access to private capital at market rates; and ii) testing the development of bond banks as a method to achieve these goals. The report chronicles the five phases of the activity, discusses conclusions about the creation of new laws to govern financing and bond banks to promote infrastructure and in the last three years, to facilitate clean energy and crime prevention projects, and provides recommendations for decision-makers replicating the activity.

The data to answer eight evaluation questions came from activity documents and interviews with key stakeholders, including USAID and Evensen Dodge staff, Mexican government officials and activity beneficiaries.

The evaluation found that the 16-year USAID-EDII activity contributed significantly to the creation of a national legal framework to create bond banks and financial vehicles to respond to the needs of local governments. This framework became self-sustaining and can be replicated in other countries. The original goal of creating an institution that would become a single national bond bank was set aside. Instead, the activity supported the creation of the legal framework for a mechanism—the bond bank/Special Purpose Vehicle (BB/SPV) tool—that can be used at a national, state, or municipal level. Two state bond banks were created, in Hidalgo and Quintana Roo. The capacity building goal was partially completed. High personnel turnover at the local government level, when national government administrations change, is a constraint for creating a sustained workforce of staff trained in the use of the tool. The work of the last years of the activity restructured the debt for the state of Veracruz and introduced a new special purpose financing vehicle, the Accredited Trust. The Accredited Trust functions like a bond bank. EDII missed the mark in achieving stated objectives in the final agreement of the GDA to generate projects focused on clean energy and crime prevention.

The authors offer eight recommendations to USAID applicable to similar activities. Some support adjusting these activities to new global realities, others relate to macroeconomic conditions. One recommendation relates to management improvement opportunities.

EXECUTIVE SUMMARY

This report presents the results of a performance evaluation commissioned by the United States Agency for International Development (USAID) of the Municipal Development through Infrastructure Financing Activity. The activity was implemented through a series of USAID Global Development Alliances (GDA) with Evensen Dodge International, Inc. (EDII) that began in 2002 and ended in July 2018. USAID contracted with Palladium to undertake the assessment which was conducted between November 2017 and July 2018.¹ The objective of the 16-year partnership was to increase Mexican private sector investment in essential infrastructure by helping a range of public entities improve their access to financing through Mexico's capital market.

The purpose of the evaluation was to assess the effectiveness of the GDA in facilitating municipal infrastructure financing through the development of bond banks, with a focus on what was achieved in the last years of the activity when the GDA added an orientation towards clean energy and crime prevention projects.

The report examines EDII's contributions in: i) increasing funding for public works projects at the subnational level using good financial practices with appropriate legal structures to facilitate access to private capital at market rates; and ii) testing the development of bond banks as a method to achieve these goals. The report chronicles the five phases of the activity, discusses conclusions about the creation of new laws to govern financing and bond banks to promote infrastructure and in the last three years to facilitate the development of clean energy and crime prevention projects, and provides recommendations for decision-makers replicating the activity.

The evaluation addresses eight research questions:

1. To what extent were the activities implemented as planned during the five main phases?
2. What were the main achievements and what were the main challenges?
3. How is the EDII Activity addressing the needs of target beneficiaries?
4. How effectively is EDII building the capacity of implementing partners and activity beneficiaries?
5. How does the activity support the objectives of Mexico's energy reform?
6. What can be achieved by the end of Phase Five?
7. Is the activity designed and implemented in a way that, once USAID leaves, the achievements remain and are consolidated?
8. What should be highlighted to replicate this Mexican experience in other countries?

The Palladium team used a mixed-methods approach to collect evaluation data. The methods used were: a desk review of 21 documents, 18 interviews with project managers and implementing partners, in depth analysis of EDII's work in three states, and interviews with local government stakeholders or beneficiaries at the

¹ The evaluation team was comprised of Santiago Lorenzo Alonso, Principal Investigator; Geraldina Villalobos Quezada, Evaluation Specialist; Nicholas Prichard, Research Analyst; and Janet E. Kerley, Project Director.
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regional government level.

ACHIEVEMENTS

The partnership between USAID and EDII fully achieved the key objective of providing local governments with increased access to financial markets. The activities resulted in establishing the national legal framework for bond bank creation, changes in subnational and regional legal frameworks, and starting bond bank/Special Purpose Vehicle (BB/SPV) financial mechanism in two States, Hidalgo (2007) and Quintana Roo (2007). EDII estimated that USD \$40 billion in state and municipal debt is now secured through a Master Trust structure and additional savings accrued from the better financial terms enabled from this trust. The activity succeeded in becoming self-sustaining as well as replicable, with debt restructuring successes promoting the newly created BB/SPV tool in several states. As the tool strengthens, it could help contribute to meeting the development demands of the local population. The work also demonstrated how good financial practices combined with appropriate legal structures can facilitate access to private capital at market rates.

EDII encountered challenges during implementation, such as institutional inertia, vested interests, and a lack of understanding of financial markets by local government staff and parliamentarians, among others. Honesty, patience, and expertise on EDII's part helped to overcome those obstacles. These challenges also required flexible and versatile management of the activity. Being adaptive and learning along the way proved to be an important strategy for EDII and USAID.

PARTIAL ACHIEVEMENTS

A key goal was the creation of a single national bond bank; over the period of the activity, no national bond bank was created. However, with the changes achieved in the legal framework, two state bond banks were created, and the State of Veracruz transaction introduced a new special purpose financing vehicle—the Accredited Trust—which, for the purposes of Mexican states and municipalities, functions like a bond bank.

These financial vehicles provided subnational and regional governments with additional resources to meet the infrastructure needs of their citizens. EDII estimated that about 28 million people benefited from infrastructure services provided by these new resources. However, the evaluation team did not have access to information to verify this number nor information on how this translated to answering the needs of the citizens, from the perspective of municipal residents. In terms of capacity building, EDII's work greatly improved officials' ability to use the BB/SPV tool. A constraint to sustaining the built capacity was the high turnover rate of government employees at each change in government. This occurrence, beyond the control of EDII, stalled the ability to create a sustained qualified staff.

EDII acknowledged that through the partnership with USAID they increased their own capacity and outreach. EDII gained the trust of other stakeholders as a result of working with USAID and being associated the USAID brand. Working with USAID also expanded EDII's network. For USAID, EDII has been a great ally in promoting and facilitating the opening of the market legal framework and enabling local governments to access financial markets. This goal was of strategic importance and beneficial for both parties in the GDA.

A private sector partner and the U.S. Government have many coincidental interests; however, at some point, these can diverge. When the final USAID-EDII GDA was issued in 2015, the goals included an emphasis on developing financing for clean energy and crime prevention projects, which meant more focused work by EDII

in the generation of an adequate and bankable pipeline of such projects. During this period, EDII also undertook work to assist the State of Vera Cruz refinance their debt. EDII's work on the pipeline of clean energy and crime prevention projects appears to have been slow in producing results and may indicate there was a divergence of strategic interests.

MISSED OPPORTUNITIES

Stronger USAID activity oversight could have detected the diverging interests and ensured that EDII activities also focused on GDA objectives. This particular problem arose in the last stage of the long collaboration. Further, USAID management would have benefited from having a deeper understanding of the complexity of the Mexican financial markets and political priorities that led local governments in the final stage to prioritize financing for other infrastructure projects unrelated to crime prevention and clean energy or to choose traditional financing over the Bond Bank.

RECOMMENDATIONS

The authors made eight recommendations to USAID that relate to this activity, but which are applicable to similar activities. Some of them are recommendations that would support adjusting these activities to new updated global realities, others to macroeconomic conditions. A final recommendation relates to management improvement opportunities.

1. USAID should ensure alignment of the private sector partner in a GDA with USAID priorities, especially when there is a specific working emphasis beyond the vocation of the allied firm.
2. Partners should ensure buy-in and ownership by all key government actors at all levels.
3. Partners should engage—at an early stage—with local likeminded organizations (business and civil society) on raising the profile of clean energy projects in the local political agenda.
4. At the same time, partners need to recognize that the project pipeline responds to legitimate sovereign interests and needs. Therefore, creating partnerships with local stakeholders on clean energy, energy efficiency and crime prevention needs would have been a good step forward to identify more projects aligned with these objectives.
5. Improve accountability and transparency by using compulsory regulations in the bond bank design and setup.
6. Incorporate new climate risk tools to be used to conduct financial risk assessments in those projects to be financed by bond banks.
7. In an effort to ensure a process to improve USAID's oversight of activities, USAID should establish clear guidelines for reporting of progress and achievement of results from the different transactions and activities supported by USAID/Mexico. It is recommended that in future activities, partners, such as EDII, submit state or municipal level reports that include more evidence to support the actual outcomes achieved. These reports should present data on findings selectively and in an understandable manner; should organize data around objectives and major themes; and use charts and tables. Conclusions should be clearly connected to evidence on performance.
8. In future activities of this nature, it would be useful to identify themes (a learning agenda) on which

summary reports could be prepared periodically, to highlight key points from different types of transactions.

I. INTRODUCTION

This report presents the results of a performance evaluation commissioned by the United States Agency for International Development (USAID) of the Municipal Development through Infrastructure Financing Activity. The activity was implemented through a Cooperative Agreement and four Global Development Alliances (GDA) with USAID and Evensen Dodge International, Inc. (EDII) (Table I) that began in 2002 and ended in July 2018.² The objective of the 16-year alliance between USAID and EDII was to increase Mexican private investment in essential infrastructure by helping a wide range of regional and municipal public entities improve their access to financing through Mexico's capital market.

The report examines EDII's contributions in: i) increasing funding for public works projects at the subnational level using good financial practices with appropriate legal structures to facilitate access to private capital at market rates; and ii) testing the development of bond banks as a method to achieve these goals. The report chronicles the five phases of the project, discusses conclusions about the creation of new laws to govern financing and bond banks to promote infrastructure and clean energy development, and provides recommendations for decision-makers replicating the activity.

PURPOSE OF THE EVALUATION

The purpose of this performance evaluation was to undertake an external assessment of the USAID activity to establish a "model for municipal development through infrastructure financing in Mexico." The evaluation assessed the effectiveness of the performance of the GDA in facilitating municipal infrastructure financing through the development of bond banks, with a focus on what was achieved in the last three years when the GDA was oriented towards clean energy and crime prevention (Annex I: Evaluation Matrix and Evaluation).

The study assessed the relevance, effectiveness, and sustainability of the range of activities implemented through this mechanism, addressing the following eight research questions (Annex I: Evaluation Matrix and Data Analysis):

1. To what extent were the activities implemented as planned during the five main phases?
2. What were the main achievements and what were the main challenges?
3. How is the EDII Activity addressing the needs of target beneficiaries?
4. How effectively is EDII building the capacity of implementing partners and activity beneficiaries?
5. How does the activity support the objectives of Mexico's energy reform?
6. What can be achieved by the end of Phase Five?
7. Is the activity designed and implemented in a way that once USAID leaves the achievements remain and are consolidated?

² The evaluation team was comprised of Santiago Lorenzo Alonso, Principal Investigator; Geraldina Villalobos Quezada, Evaluation Specialist; Nicholas Prichard, Research Analyst; and Janet E. Kerley, Project Director.
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8. What should be highlighted to replicate this Mexican experience in other countries?

The team used a mixed-methods approach, focusing primarily on qualitative methods. These included a desk review of available activity documents, key informant interviews, and in-depth reviews of the EDII process to implement the new financial mechanism in three states. The data collection methods are described in Annex II: Evaluation Methodology and Annex III: Sources of Information.

The evaluation report presents findings and conclusions for each of the research questions. The report also discusses the five phases of the Activity and concludes with a discussion of how the bond banks are currently functioning. Finally, the authors offer overall conclusions on the performance of the activity, draw lessons learned, identify missed opportunities, and put forward recommendations for USAID's consideration. The audience for the evaluation is USAID/Mexico and its partner, EDII. The larger audience may be other USAID missions that are interested in engaging in this type of public-private partnership municipal financing activity. The results will be used by USAID to identify lessons learned for future activities in the municipal financing arena.

BACKGROUND

LOCAL GOVERNMENT FINANCIAL LANDSCAPE IN MEXICO

In the 1990s, the responsibility for health, education, security, and basic infrastructure was transferred from the federal government to the states and municipalities. At the end of the Institutional Revolutionary Party (*Partido Revolucionario Institucional*, or PRI) regime in 2000, after more than 70 years of centralized rule, state governments took a more prominent role in managing these issues, realizing as they did so, that having access to other financial sources could strengthen their political autonomy and sovereignty.

Prior to 2002, "Mexican states and municipalities relied solely on financing provided through the Mexican federal government and short-term commercial bank loans, as investor wariness and excessive transaction costs discouraged local governments from mobilizing funds through bond issuances...Mexican state and local governments receive approximately 95 percent of their total funding from the federal level."³ This dependency has been used as a form of administrative control by the Mexican Federation over state governments.

At the same time, in financial terms, most Mexican states were underleveraged—according to rating agencies—with significant available debt capacity, at around USD \$4-6 billion annually.⁴ This potential to increase financing, it was believed, could play a key role in delivering needed infrastructure services to the population. Currently approximately 40 percent of the population hovers at poverty levels.

EVOLUTION OF EVENSEN DODGE'S GOALS, OBJECTIVES, AND ACTIVITIES

Evensen Dodge International, Inc. began working in Mexico as a private company to support efforts to help local governments increase their access to financial markets. This work began following policy actions taken by the Zedillo administration after the country's peso crisis in the 1990s and the 2000 Mexican federal election. With the change in power, the company had seen a business opportunity for the financial advising sector in

³ Interview with Elizabeth Bauch, Ph.D., Senior Associate Advisor, Evensen Dodge International

⁴ Pees. Interview and EDII 10-year report. p. 9

which EDII had extensive experience and a large competitive advantage in the U.S.

Their first step was to create space for these services in this nascent niche of financial advising for local Mexican governments. EDII made the decision to engage with different actors on this topic, starting with the Federal Ministry of Finance.

In 2002, USAID signed a Cooperative Agreement with EDII entitled 'Model for Municipal Development through Infrastructure Financing in Mexico' (Table I). The partnership not only strengthened EDII's approach but opened the space for EDII to expand a market niche and support systemic change in Mexico. The partnership's goals were clear for EDII's business case and supported USAID's goals. Financial constraints frequently jeopardize development opportunities and improving local governments' access to financial markets undoubtedly could enhance the development opportunities in Mexico.

The context was clear. The power swing in the country definitively was going to favor local governments seizing more autonomy and the financial aspect was crucial for its success. Despite the potential obstacles, this financial niche market was headed towards growth. The long-term strategic orientation indicated this opportunity was an inevitable pathway for Mexico, and the alliance between USAID and EDII could accelerate this transition and produce positive outcomes for all. EDII was not trying to leverage U.S. government funds, but rather using the partnership with the U.S. government to leverage private sector resources.

Over the period of performance, USAID signed five consecutive agreements with EDII to continue the work (Table I).

TABLE I: LIST OF AGREEMENTS BETWEEN USAID AND EVENSEN DODGE, WITH TOTAL AWARD AMOUNTS

AGREEMENT INFORMATION	START/END DATES	TOTAL ESTIMATED USAID AWARD (USD)	USAID RESPONSIBLE OFFICE
Model for Municipal Development Through Infrastructure Financing AID-# 523-A-00-05-00039-00 Initial Cooperative Agreement*	2002-9/20/2005	\$501,795	Democracy and Governance Office USAID/Mexico
Expansion of the Model for Municipal Development through Infrastructure in Mexico AID-# 523-A-00-05-00039-00 Global Development Alliance	9/30/2005-9/30/2008	\$1,000,000	Democracy and Governance Office USAID/Mexico

AGREEMENT INFORMATION	START/END DATES	TOTAL ESTIMATED USAID AWARD (USD)	USAID RESPONSIBLE OFFICE
Expansion of the Model for Municipal Development through Infrastructure in Mexico AID-# 523-A-00-05-00039-00	9/30/2008-12/30/2015	\$11,000,000	Democracy and Governance Office
Mexico Bond Bank to Foster Development through Energy Efficient Infrastructure Financing in Mexico AID-523-A-15-00001‡ (EDII sent a Proposal in response to RFA #APS-OAA-14-00001)†	1/5/2015-1/4/2018	\$1,500,000	Economic Growth
Mexico Bond Bank to Foster Development through Energy Efficient Infrastructure Financing in Mexico and Foster Crime and Violence Prevention through Infrastructure Financing in Mexico Amended Agreement with modifications‡	1/5/2015-7/30/2018	\$2,500,000	Economic Growth and Justice and Citizen Security

*The Palladium team was unable to obtain a copy of extensions or modifications to the original USAID agreement for the next two years (2003-2005).

† ‡Signed agreement included the same proposal under #AID-523-A-15-00001. The title changed to include “foster crime and violence prevention through infrastructure financing in Mexico.” Language on crime and violence prevention added in the Jan 2015 modification, signed on July 24, 2018.

The overall objectives of the USAID-EDII Activity are captured in the statements below:

1. Mobilize domestic credit for basic infrastructure projects that benefit Mexican citizens and improve conditions for economic growth.
2. Lower costs of borrowing, including bond issuance, and encourage more states and municipalities to seek capital market financing.
3. Help states and municipalities engage directly with private investors through the market.
4. Provide incentives for local governments to improve financial management and reporting practices.

“The main objective of [the] USAID/Mexico—Evensen Dodge International GDA Program is to introduce new financial structures and practices to Mexico to enable local governments to access Mexico’s capital market and lower the cost of borrowing. This objective encapsulates four strands or specific objectives of EDII efforts.”¹

EDII ANNUAL REPORT, 2004

These objectives changed over the life of the activity, adapting as progress was made or changes arose in the external environment. They began with the goal to establish a federal legal environment that would enable the creation of bond banks, and then moved on to the objective of implementing the legal reforms necessary to

operate bond banks—as a mechanism rather than as a physical institution. Finally, EDII expanded the uses of the bond bank financing mechanism (as Master or Accredited Trusts) to the regional and municipal levels.

In the final three years of the activity, the GDA was renewed, with specific objectives added to develop projects in support of renewable energy, energy efficiency, and public safety and crime reduction, such as through energy-efficient public lighting (Table 1). The energy projects would support the significant actions Mexico had taken to become a global leader in combating climate change. [In 2012, Mexico became the second country in the world to pass a national climate change law, which pledged to reduce the country’s 2000 emission levels by 50 percent by 2050.]

USAID, recognizing global climate change as a policy priority for Mexico and the United States, was supporting national and subnational policy development to advance Mexican-led climate change initiatives. The longest standing of the five USAID/Mexico energy activities was the EDII work in the financial sector to leverage resources for sub regional infrastructure projects, including for energy projects.

However, as with any other transition with political dimensions, many uncertainties arose along the way and the USAID-EDII alliance had to be flexible to deal with the changing contexts. EDII had to contract different services to complement their own expertise to match the new windows of opportunity opening at each phase, such as engaging a firm in the later phase to assist in identifying clean energy projects. This activity also required EDII to work with dozens of Mexican private firms engaged in banking and finance, and also with firms seeking to implement energy-related projects. EDII promoted the competitive selection of service providers when preparing transactions—supporting government officials making decisions, but never making the decisions themselves (Annex IX. EDII Response to Draft Evaluation, p. 3).

The five key phases of the activity and related activities are described in the table below and will be referred to throughout the discussion of the findings for each research question (Table 2).

TABLE 2: PHASES OF THE EVENSEN DODGE ACTIVITY

	INITIAL PHASE	PHASE 1	PHASE 2	PHASE 3	PHASE 4	PHASE 5
Objective	Development of the legal framework For local government access to private financing	Federal revenue transfers interception in practice - simple model	Develop a bond bank in Mexico	Develop the legal framework for Public Private Partnerships	Backlash and capacity building	Using an SPV for Veracruz debt restructuring and to develop a pipeline of clean energy and crime prevention projects
Date	2000-2002	2002-2005	2005-2008	2008-2012	2012-2015	2015-2018
Entity with Whom they Work	Federal government (Presidency of the Mexican Republic, SHCP, SEGOB, Banobras, among others)	State Government of Michoacán, SHCP	State Government of Hidalgo, State Government of Quintana Roo, SHCP	State Government of Hidalgo, SHCP	Federal, state, and municipal)	Federal government, various states and municipalities
Description	EDII work, prior to partnering with USAID. Reforming the federal legal framework to give access to financial markets for local governments	First transaction: State of Michoacán for a total of \$300 million dollars, in two portions of \$150 million each. Used for matching municipal funds for infrastructure projects in health, education, roads. Introduced a Participatory Budget	First collective financing vehicle developed in Mexico (a bond bank): State of Hidalgo. First treasury fund: State of Quintana Roo (a Pooled Investment Fund) and a bond bank in Quintana Roo.	New PPP Law for the State of Hidalgo, required to provide the legal framework for private sector finance participation in BB projects and programs. The 12 models or variations of PPP were also used for establishing the federal law on the subject.	A new federal administration brought a different approach to local financing with its desire to return to centralized control. EDII worked to protect progress made in the field by educating politicians, training local governments' financial staff, and, in general, sustaining the achievements and defending progress in the domestic capital markets against a return to centralism.	Set up an SPV under an Accredited Trust structure, a financial model similar to a bond bank in the State of Veracruz - \$2 Billion. The third party receives and holds the federally transferred funds, not the subnational entity; the third party transfers the resources to the entities or invests on their behalf. The PPP law was created in several states to structure projects and access financing using the SPV-Accredited Trust. One objective of the final GDA, to facilitate clean energy and crime prevention projects, was only partially achieved.

	INITIAL PHASE	PHASE I	PHASE 2	PHASE 3	PHASE 4	PHASE 5
Contacts	Supported by President Fox	Lázaro Cárdenas, State Governor; Humberto Suarez, CPA, Secretary of State Finance; Javier Pérez López, General Director of INDETEC	Miguel Osorio Chong, Governor of the State of Hidalgo (Now Federal Secretary of the Interior); Nueva Mayorga, Secretary of Finance of the State of Hidalgo; Cesar Euan, Undersecretary of Finance and Administration of the State of Quintana Roo	Paulo Uribe, Attorney General of the State of Hidalgo; Pablo Uribe, Coordinator of Finances of the State of Hidalgo	Samuel Pelayo, Treasurer of the Municipality of Puerto Vallarta	Miguel Ángel Yunes Linares, Governor of the State of Veracruz; José Luis Romo, Secretary of Economic Development of the State of Hidalgo; President Superior Court Of Justice in Veracruz

II. USAID-EDII ACTIVITY PROGRESS

Accessing private capital under appropriate market conditions, which should include full financial and legal disclosures, offers an important means to build infrastructure of all types. EDII's parent company, Evensen Dodge, with extensive experience working with U.S. states and municipalities, believed that Mexico presented a possible business opportunity and an opportunity for establishing public-private partnerships. This decision was made by EDII following the implementation of NAFTA, the resolution of the country's 1994 financial crisis, and the rise to power of a new pro-free market president.

Mexico's public finance framework was and still is based on the income generated by tax collection. The Mexican Constitution defines the taxing capabilities for each level of government, with the federation and municipalities having regulated autonomy on certain tax issues and leaves more limited options to state governments. Some of the joint tax efforts, where multiple levels of government can collect revenues, must be harmoniously agreed to by all of the collecting entities, and some of these efforts could mean huge revenue potential in the form of rent and value added.

The federation collects the taxes and then shares back the revenue with states and municipalities. For this purpose, there is an intergovernmental transfer system using a formula based on socioeconomic parameters. Subnational governments receive multiple types of transfers from the federal government, including those categorized under "Ramo 28" of the federal budget⁵, which are the only federal transfers that may be applied to debt service, under specific conditions, and are now imposed by the national *Ley de Disciplina Financiera de las Entidades Federativas y Municipios*, issued in 2016⁶ (Annex IX. EDII Response to Draft Evaluation, p. 6).

In 2000, EDII performed an initial assessment of the Mexican capital market once the federal government explicitly severed the implied moral guarantee⁷ for states and municipalities in the late 1990s. Banking regulations tied banks' reserve requirements to the credit quality of their loan portfolios. Subnational governments had to obtain two credit ratings. Some states did issue bonds, but advisors and other service providers charged exorbitant fees—at times 10 percent of proceeds—effectively erasing any interest rate savings (Annex IX. EDII Response to Draft Evaluation, p. 4 & 18).

Private companies and the national government have been able to obtain domestic and international financing for decades. However, subnational government participation in Mexico's domestic capital market is a recent phenomenon. Early in its work, EDII identified unofficial but critical barriers to subnational government access to the capital market.

Mexico's fiscal policy reforms of the 1990s made it possible for states and municipalities to borrow based on their own credit quality. Mexican investors are concerned with issues such as debt repudiation and financial mismanagement, and as a consequence most will only consider participating in transactions if they maintain a good relationship with the government involved and the debt is rated AA.Mx or higher. Another barrier is the

⁵ The other main mechanism to transfer funds from the federal budget to states and municipalities is *Ramo 33*, designed to strengthen the subnational entities' response capacity and address local government needs in the fields of education, health, basic infrastructure, financial strengthening, public security, food programs, and social care.

⁶ To review the federal transfer mechanism during the 20th century, visit:

http://www.inafed.gob.mx/work/dso/la_distribucion_de_transferencias_federales_para_municipios.pdf

⁷ All government units pay a percent to the federal government which is allocated and distributed back to the units. There was an implied covenant that the federal government would 'take care of the sub unit.'

size of the transaction. Mexican investors undertake their own evaluations of credit quality and do not rely solely on published credit ratings. The level of effort this requires is significant, so most investors only undertake this if the borrowing amount is at least USD \$50 million (Annex IX. EDII Response to Draft Evaluation, p. 5).

EDII contributed to the introduction of legal mechanisms that address both credit quality and size barriers during its partnership with USAID. These mechanisms may be adopted or applied by any Mexican state or municipality. The GDA activity proposed structural features and mechanisms that, when adopted, successfully enhanced the credit quality of transactions to achieve AA.Mx or higher credit ratings. “The ratings are key to accessing the capital market because private investors compete for transactions that meet specific credit levels (AA.Mx or higher). They also represent third-party evaluations of transactions by credit rating agencies, and in the case of new structures, by their legal advisors. EDII’s transactions under the GDA activity are designed to be of the highest quality because this benefits both borrowers and lenders, and because high quality transactions are more likely to be studied and replicated by other market participants” (Annex IX. EDII Response to Draft Evaluation, p. 7).

The structural financial features and mechanisms introduced by EDII and the GDA activity included the Master Trust revenue intercept structure, state bond banks, and the Accredited Trust mechanism. In the case of state bond banks, which are a type of Special Purpose Vehicle (SPV), the in-depth review of EDII’s work in Michoacán, Hidalgo, and Quintana Roo demonstrated that the SPV could successfully pool debt transactions on behalf of smaller borrowers and meet both the transaction size and credit quality requirements of private investors. This activity promoted best financial practices and, in some cases—most recently in the State of Veracruz—credit rating agencies acknowledged improvements and raised the entity’s credit rating. The market openness also promoted the competitive selection of a financial advisor for debt transactions, demonstrating that costs could be contained to between 1.5 and 2 percent (Annex IX. EDII Response to Draft Evaluation, p. 5).

It is important to bear in mind that during the long period of collaboration between USAID and EDII, the world suffered probably the biggest financial crisis in 80 years. In 2008, all financial markets fell and Mexico was not immune to these events. On the other hand, domestically, the political shift in power brought new rules of the game and fiscal transfer between different levels of government became politically loaded, including high-profile cases of government corruption. However, the political will of some actors allowed EDII’s work to support both Hidalgo and Quintana Roo to complete financing transactions following the 2008 crisis. EDII’s work introduced mechanisms, including both the Master Trust and the Accredited Trust, that increase transparency for all parties and provide structural assurances that funds are properly applied. This transparency benefits both borrowers and lenders.

As independent financial advisors, EDII staff are hired to provide professional guidance to government officials based on their market experience. EDII provided diagnostics and analysis to help inform government decision-makers, and they also made recommendations for improving practices and/or laws and regulations in order to achieve long-term goals. EDII helped governments set sound foundations for their own borrowing, while recognizing the importance of maintaining flexibility for future borrowing. EDII also helped subnational government clients plan, structure, and execute debt transactions with the final objective to help their clients obtain financing under the best possible conditions available in the market (Annex IV. Technical Assistance).

EDII was careful to ensure that innovations, including the Master Trust, state bond banks, and the Accredited Trust met all legal and regulatory requirements at the national and state levels. In the case of the Accredited Trust, EDII sought and obtained a modification to the *Ley de Disciplina Financiera* that permitted the structure.

Subsequently, Mexico's *Comision Nacional Bancaria y de Valores* (CNBV) reviewed the structure and issued instructions for its application in some debt transactions. Other transactions required modifications of state laws and even state constitutions so that borrowers would be in compliance with national laws (Annex IX. EDII Response to Draft Evaluation, p. 7-8).

III. THE DEVELOPMENT OF THE MEXICAN BOND BANK

This section aims to clarify the concept of a bond bank and compare the system for obtaining loans through the financial markets in Mexico before and after the introduction of the Special Purpose Vehicle (SPV), i.e., a bond bank.

In the second phase of the collaboration between USAID and EDII (Table 2), the major goal of the GDA⁸ was to create a nationwide bond bank—an entity that engages in debt transactions on behalf of one or more participating borrowers (Annex IX. EDII Response to Draft Evaluation, p. 19)—and provide technical assistance to subnational authorities (and associated public and private entities) to further develop their institutional and financial capacities.

The concept of having a 'bond bank' is related to the ability and Capacity of state and local governments—historically weak in credit worthiness (perceived or real) —to improve their access to financial markets, though not necessarily by only issuing bonds. As in the U.S., smaller municipalities in Mexico lack experience in accessing competitive financing. A bond bank may issue bonds or engage in a competitive structured loan process on behalf of the borrowers participating in a specific transaction.

“A bond bank is not a building; it is a legal framework.”

**ELIZABETH BAUCH,
ADVISOR TO EDII**

State-level bond banks may be sued by the state or any underlying municipality, alone or in a transaction that pools multiple borrowers. Pooling allows smaller borrowers to save on the overall costs as costs are distributed proportionally. The bond bank transactions are evaluated and assigned credit ratings that are almost always higher than the ratings of the ratings of the smallest transaction participants (Annex IX. EDII Response to Draft Evaluation, p. 20).

'Bond bank' is a term encompassing a legal framework that enables debt consolidation—lowering risk for investors and improving borrowers' credit worthiness—for municipalities or states through federal tax revenue appropriations, in other words, legal instructions from the subnational borrower to the federal Finance Secretariat to direct a specific portion of the borrower's share of federally collected revenues directly to a trust account—which is held by a third party—for debt service payment, instead of directly into subnational accounts. These funds belong to the subnational entity but because they are not comingled with other state funds, investors see these monies as having a higher credit quality. A bond bank increases transparency. The

⁸ A GDA is a partnership between USAID and the private sector—and may also include a range of other partners—in which the parties work together to develop and implement activities that leverage and apply respective assets and expertise to advance core business interests, achieve USAID's development objectives, and increase the sustainable impact of USAID's development investments (2018). <https://www.usaid.gov/gda>

loan or bond proceeds flow to the bond banks, which immediately transfer them to the participating borrowers; the bond bank holds no funds (Annex IX. EDII Response to Draft Evaluation, p. 21 & 25).

The account that holds these federal transfer funds can be an Accredited Trust, a Master Trust structure or an institution, and in all cases, it needs to be transparent and accountable to the local legislative body. The Master Trust—a mechanism whose introduction can be attributed to EDII’s work on developing the necessary legal framework—is available to all subnational entities in Mexico. EDII estimated that USD \$40 billion in state and municipal debt is now secured through a Master Trust structure (Annex IX. EDII Response to Draft Evaluation, p. 25). By definition, the trust account needs to be created by a local law. A trust (Master or Accredited) at the federal level is its equivalent and requires the trust management to report on the transactions, which are also transparent, to the local authorities. These legal frameworks and financial mechanisms address credit concerns and increase the potential for attracting investors, thus creating greater competition. Bond bank transaction ratings to date have been higher than the stand-alone ratings assigned to the states in which they were established (Annex IX. EDII Response to Draft Evaluation, p. 21).

While the name of the financial tool is a ‘bond bank,’ improving development investment is not achieved only by issuing bonds. Getting the best lending opportunities implies expanding options instead of narrowing down to just one financing mechanism, in this case bonds. A bond bank is a type of SPV that can be used multiple times with different combinations of participants, but the use of this tool is optional and not required (Annex IX. EDII Response to Draft Evaluation, p. 20). The purpose of setting up a bond bank “is about enabling a legal framework that allows an SPV⁹, or any other potential financial vehicle, to operate and, thus, to access financial markets in a better way, under any other financial product.”¹⁰

A bond bank or SPV, because of its structure and accountability, provides critical information for institutional investors willing to participate in project investment. The financing component is just one element of developing, building, and managing a project successfully. A comprehensive approach is needed to assess the real opportunities for success.

EDII’s early work focused on supporting the necessary reforms within the federal legislation to allow states that were willing to do so, to create their own bond bank through some local and state legal changes, including to the local constitution. The work on implementing legal reforms continued through the life of the activity. For leveraging private finance, it was also important to create a local law on public-private partnerships (PPP). In the case of the State of Hidalgo, for example, the law—based on comprehensive work by EDII—contained 12 different types of potential partnerships allowing greater flexibility in the legal contract to enact the partnership. Prior to EDII’s work on supporting PPPs and their relevant laws, the enabling legislation was broad and general and essentially only applied to franchises. The greater flexibility in types of partnerships implies a broader range of projects can be pursued, including those related to clean energy and crime prevention (Annex IX. EDII Response to Draft Evaluation, p. 22). In the realm of public finance, detailing contracting modalities is important; there is a greater responsibility in managing how public money is used and in managing relationships with private sector partners, avoiding potential conflicts of interest or corruption.

The goal of the second and third agreements with USAID, from 2005-2015, (Table I) was to expand the model for municipal development by “helping Mexico’s nascent municipal bond market expand to a wider range of

⁹A subsidiary body with an asset/liability structure and legal status that makes its obligations secure even if the parent entity goes insolvent.

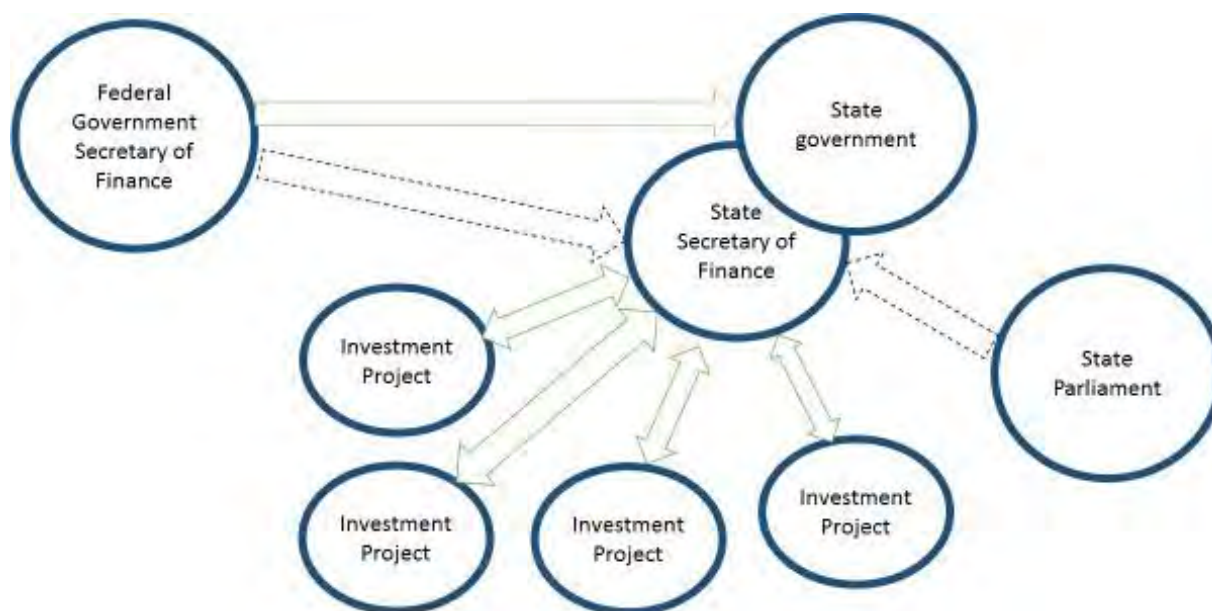
¹⁰ Interview with Elizabeth Bauch. Annex III. Sources of Information

issuing states and municipalities. This goal was pursued by providing technical assistance to selected sub sovereign entities to take actions to improve their credit quality and thereby make their debt more appealing to potential capital market investors.¹¹

Given that these reforms were taking place at the local level, the efforts also implied creating or enhancing local staff capacities. Hence, EDII engaged in a concentrated effort, through presentations, training courses, and other means of outreach, to educate local parliamentarians, state employees, bankers, and other stakeholders on what an SPV could mean to the state's finances. (See Annex V. Training and Capacity Building.)

A representation of the way infrastructure finance was organized prior to the EDII/USAID Activity is presented in Figure 1. The differences in the structure of financial mechanisms after EDII's work was completed is represented in Figure 2. In the first model (Figure 1), financial resources flowed from the federal government to the state, and the governor was the main political person responsible for its use; the local Secretary of Finance was the responsible administrative official. The local parliament periodically received a report on the use of the financial resources. All local infrastructure projects were financed with those federal resources (with around 5 percent coming from local taxes or short-term banking credits)

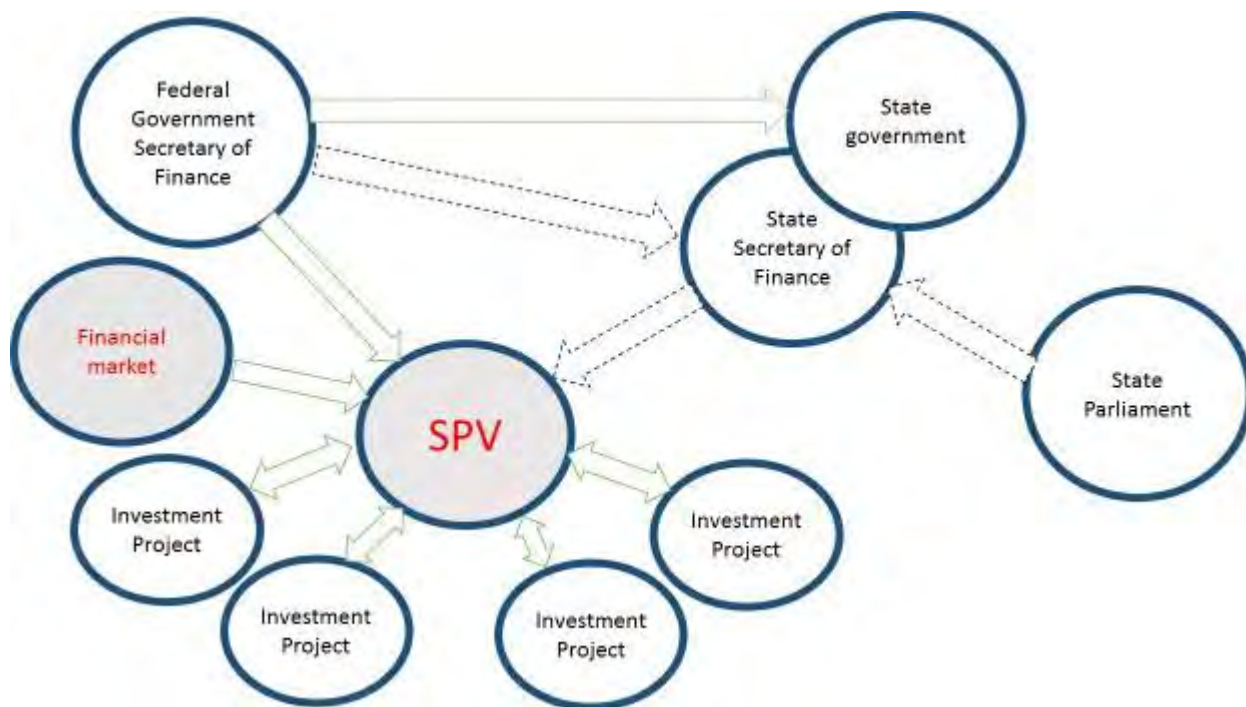
FIGURE 1: STATE-LEVEL SCHEME FOR FINANCING INVESTMENT PROJECTS WITHOUT SPECIAL PURPOSE VEHICLES (SPVS)



¹¹ EDII Cooperative Agreement 2005.

In the second model (Figure 2), the role of an SPV is shown as an independent legal entity or mechanism for financing infrastructure projects. The SPV can be established under different schemes but in this figure it is represented as an entity that, in a way, substitutes for the role of the local Secretary of Finance. As an independent entity, its administration is removed from any additional financial duty that the state government acquires. At the same time, due to the reform of local laws, it can directly access federal revenue participation to guarantee its debt.

FIGURE 2: STATE-LEVEL SCHEME FOR FINANCING INVESTMENT PROJECTS THROUGH AN SPV



IV. FINDINGS AND CONCLUSIONS

The evaluation study's research design (Annex II. Evaluation Matrix and Data Analysis) listed eight questions to be addressed. In the following section, the findings and conclusions are presented for each question. Overall conclusions and recommendations are presented in Section V and Section VII, respectively.

TO WHAT EXTENT WERE THE ACTIVITIES IMPLEMENTED AS PLANNED DURING THE FIVE MAIN PHASES?

The original objective of the GDA (and the successive modifications)—expand subnational government access to capital market financing (Annex IX. EDII Response to Draft Evaluation, p. 23) allowed EDII flexibility on choosing the activities to implement in order to achieve the goal of reaching the agreed-upon transaction targets. This was due, in part to the fact that when the USAID-EDII relationship started under a Cooperative Agreement, the Activity was considered “quite experimental.”¹² The transactions would help demonstrate how best practices combined with appropriate legal structures can facilitate access to private capital at market rates.

The USAID-EDII agreement implied supporting legal reforms, entailing working relationships with a diversity of parties (at federal and state levels) which made progress complex and sometimes difficult, as any technical work in this area is subject to political timing and trade-offs.

It took a long time to make the required legal changes to support SPV development, due to the technical and political complexities of the activity. The legal engineering required was highly innovative and many local governments were reluctant to change unless the situation was very favorable for it. An additional obstacle was Mexico's slow political processes. All state governors work both locally and nationally, so the agenda moves accordingly with different election rhythms.

Over the 16 years of cooperation with USAID/Mexico, EDII had an adaptive management approach allowing them to continue working under these diverse circumstances. Despite obstacles, EDII remained confident that opening this market was inevitable. Over time, the political landscape changed, raising some opportunities and narrowing or closing others.

These changes shaped how EDII was required to engage with partners and other stakeholders. Consequently, EDII adopted diverse approaches to achieve the overall objective (Table 2), depending on the political and economic context. In some phases, the political work was emphasized and, in others, the technical was accentuated, depending on the window of opportunity and the need for progress on each side. Such was the case, for example, in Phase Four (Table 2). When little progress was being made during the financial crisis and and the changes in the local political landscape, EDII shifted to focus activities on capacity building and education.

EDII encountered challenges during implementation, such as institutional inertia, vested interests, and the lack of understanding of financial markets by local government staff and parliamentarians, among others. Honesty, patience, and expertise on EDII's part helped to overcome those obstacles. These challenges also required flexible and versatile management of the activity. Being adaptive and learning along the way proved to be an

¹² Interview with Elizabeth Bauch. EDII

important strategy for EDII and USAID.

Circumstances affecting the Activity included:

- The 2008 financial crisis, causing a slowdown for these types of activities;
- Local governments' political agenda and timing of the election cycles (Michoacán);
- Change in the federal government's approach, with the appointment of a new Finance Secretary in 2012, who attempted to recentralize financing and created conflicts of interest. As a result, financial advisory firms were barred from working with state and municipal clients. EDII had to look to private firms seeking to develop PPP projects related to crime prevention;
- Lack of knowledge about financial markets by high-level government staff; and
- Financial reliance by national political parties on access to public resources through irregular schemes.¹³

SUMMARY OF THE FIVE PHASES (TABLE 1)

Initial Phase

The initial phase involved working with the federal government to reform the federal legal framework to give access to financial markets for local governments (Table 2). Mexico is a federation and, as such, around 80 percent¹⁴ of all tax revenue collection (compared with around 60 percent of other OECD federal countries) is concentrated at the national level. Since 2000, there had been some initiatives to strengthen states and municipalities, mostly focused on a better use of resources coming from federal tax revenue. These reforms made limited progress on improving transparency and accountability. EDII supported the federal government and worked alone as no agreement had yet been signed with USAID.

Phase One

The new possibilities opened by the reform on local financing was going to be tested. During this period, EDII supported the State of Michoacán (SoM) in obtaining two loans with good financial terms. The loans were used, with matching municipalities' funds, for infrastructure projects in health, education, roads, and for other highly demanded municipal needs.

The Public Debt Law of the (SoM) was reformed to align with the new federal legal framework. The State then obtained credit support—two loans of \$150 million each—for the financing of local government water sewage treatment, public lightning, school improvements and health infrastructure. They used an SPV pooled financial vehicle, called the Revenue Intercept Model. The loans were obtained at single-digit rates, while traditional financing was above 13 percent. A term of 10 years was also achieved, whereas the standard term length was six years. Over the next four years, the private initiative invested at least \$300 million of additional dollars for

¹³ <http://www.sinembargo.mx/28-01-2018/3378592> and https://elpais.com/internacional/2018/01/24/actualidad/1516833975_352478.html

¹⁴ <http://cidac.org/esp/uploads/1/disputa-recursos-textocompleto.pdf>

municipal development in *Nuevo Morelia*.

EDII also assisted SoM in issuing a bond. However, political timing caused the SoM to instead negotiate, with EDII's assistance, a structured syndicated loan with private financial institutions, which marked the first time such a loan extended beyond the term of a sitting governor (Annex IX. EDII Response to Draft Evaluation, p. 24-25). Using this revenue intercept structure, through the new Master Trust mechanism, allowed the state of Michoacán to have a portion of its federal transfers assigned to an irrevocable trust for debt service payment. [States receive multiple sets of transfers, all earmarked for specific purposes. Only those linked to Budget Branch 28 (*Ramo 28*) may be applied to debt service.] The transaction was approved and closed with excellent terms and conditions and long-term private financing was obtained. Subsequently, work was also completed on putting together a participatory budget.

Phase Two

This stage was a critical moment to test whether it was possible to achieve the purpose of the bond bank. In fact, the first bond bank was created in the State of Hidalgo (SoH) and a new Private-Public Partnership was adopted for the State of Hidalgo, a requirement to provide the legal framework for private sector engagement. These achievements created momentum for EDII's work, and the State of Quintana Roo followed quickly to create a bond bank. Both completed financial transactions proving that the model was functional (Table 2).

Phase Three

The SoH, as the pioneer, was the most engaged. In order to better use the bond bank, they required clear rules for engaging the private sector. EDII conducted a study of successful public-private partnerships internationally and presented this as a foundation for adopting legislation that could enable a government entity to apply any and all of these 12 models to projects, as appropriate (Annex IX. EDII Response to Draft Evaluation, p. 26). These were subsequently included in the PPP law.

Phase Four

During this phase, a new federal administration came into power and the incoming Federal Minister of Finance effectively halted any further progress on bond banks when he directed subnational entities to work exclusively with one financial advisory firm. After efforts by EDII to continue working as before failed, it was clear that other tasks should be undertaken. It was during this phase that EDII deepened their capacity building efforts. A comprehensive report of EDII's work in training and capacity building is found in Annex V.

Phase Five

In the final phase, from January 2015-2018, USAID introduced a focus on financing for “energy efficient infrastructure and crime and violence prevention projects” (Table 1). In mid-2016, with a change in political leadership, EDII began working with officials in the State of Veracruz (SoV). All the eyes of the nation turned towards this case and EDII engaged in a drive to complete a dramatic restructuring of a debt at approximately USD \$2 billion. As Veracruz was immersed in a critical financial crisis and delicate political situation, EDII shifted towards this capital market-enhancing opportunity but in the process did not meet some of the specific stated objectives from the final extension/agreement of the GDA which were to focus on facilitation of financing for USAID/Mexico's priorities – clean energy and crime and violence prevention

The SoV case was considered successful by EDII because the state received the funds needed to restructure its debt. The transaction(s) also accomplished the introduction of the Accredited Trust SPV, which represented a key achievement for the USAID-EDII GDA activity. It is effectively a national bond bank, the creation of which was an objective of the original GDA agreement (Annex IX. EDII Response to Draft Evaluation, p. 28). Its national visibility helped adverse political parties understand that an SoV bankruptcy would not benefit anyone.

The EDII staff offered three reasons to argue the relevance of focusing on SoV debt restructuring. First, the national attention and impact that such a large debt restructuring would have, were it successful, could highlight the relevance of using the Accredited Trust structure for better management of state debt. The second reason was that obtaining better credit conditions in a very difficult case would show others the benefits of this new scheme for any purpose. A third reason is that it was *potentially* consistent with crime prevention work dictated by the agreement with USAID.

USAID officials expressed the viewpoint they expected that EDII would also continue work on the clean energy component of the GDA. The evaluators judged that EDII's pursuit and achievement of a pipeline of clean energy and crime prevention projects weren't fully reached.

EDII officials argued that "Without the debt restructuring, the new state administration would have no resources for its crime prevention program." The SoV case did free up resources that authorities have indicated could be used in crime prevention and clean energy. The SoV is creating its own energy agency to embrace opportunities for clean energy and energy efficiency, which could be funded in part with these additional resources. Further, EDII participated in developing a small pipeline of projects related to energy and crime reduction, including the Iztapalapa public lighting project, the Hidalgo waste-to-energy project, and the proposed Coahuila solar park, among others. These projects remain in process or pending for reasons unrelated to EDII's work under the GDA Agreement.

There continues to be a difference of opinion on this issue between EDI and USAID as to whether seizing the SoV opportunity reduced the efforts to achieve the clean energy crime prevention target (Annex X: Statement of Differences).

Conclusions

1. The activities related to expanding the options for local government finance through the establishment of a bond bank were generally implemented in a logical way.
2. EDII pursued the development of a new mechanism that would expand capital market access for states and municipalities in Mexico. EDII contributed to successfully achieving the necessary federal legal reform in Phase One (Table 2). Once the reform was in place, this foundation provided the potential for EDII to go to any state and engage with local governments' administration and parliaments. This foundation allowed for the establishment of bond banks in two states.
3. After Phase Two, which ended in 2008, the enthusiasm to create more bond banks declined, largely because of the 2008 global financial crisis.
4. The work of the last three years, Phase Five of the agreement, resulted in a successful restructuring of the SOV debt, deviating from the new objectives included in the final GDA agreement between EDII and USAID to develop a pipeline of clean energy and crime prevention projects.

WHAT WERE THE MAIN ACHIEVEMENTS AND WHAT WERE THE MAIN CHALLENGES?

Prior to joining in a partnership with USAID/Mexico, EDII had already engaged in the task of generating change in the Mexican financial markets to enhance access for local governments. When USAID agreed to support EDII's work, EDII's role was substantially improved. Having the support from a major development actor in Mexico enhanced public trust in EDII's work. USAID was viewed as an influential partner and key U.S. officials, including Ambassadors participated in EDII's work-related meetings with Mexican authorities and other stakeholders in the early years of the Activity.

USAID was linked to the Mexican Association of Secretaries of Finance and also to the U.S. Treasury. USAID was able to make the link between these two groups, which was helpful. The Mexican Association of Secretaries of Finance has an annual meeting and they invited U.S. association members, which gave increased credibility to EDII's work.

The approach to creating financial reform could widen and deepen as a result of this partnership, as EDII was not a partner for specific financial institutions or local or regional governments, but a partner with a wider and systemic scope that clearly had a developmental mandate.

Federal Legal Reform

Initially, EDII assisted its partners at the federal level to achieve the legal modifications required for an SPV to intercept federal revenue streams to ensure local government debt service payment¹⁵ (Annex IX. EDII Response to Draft Evaluation, p. 25). This source for financial resources is the most secure and steady source, as the federation has the obligation to share revenue coming from federal taxes with the states of the union.

This most critical and binding reform came with the issuance of the "*Ley de Disciplina Financiera de las Entidades Federativas y los Municipios*" (Financial Discipline Law of Federal Entities and Municipalities) in April 2016. The law was created by combining different elements contained in previous fiscal legal instruments with new elements. The previous laws dealt with fiscal coordination (*Coordinación Fiscal*), public debt (*General de Deuda Pública*), and government accounting (*General de Contabilidad Gubernamental*). One of the main additions was the introduction of new practices and reporting obligations for local governments to the federal government.

State Legal Reform

EDII also worked to reform the Public Debt Law of the State of Michoacán to align with the new federal legal framework. This new law was created to replace the previous public debt law dating from the 1920s. With this new law, the state was empowered to access long-term financing and to pledge tax revenues and federal tax transfers to pay for debt obligations using an irrevocable trust mechanism (revenue intercept mechanism).¹⁶ The state congress approved a decree to authorize the state to access and carry out the financial transactions.¹⁷

¹⁵ 'Intercepted' means that the money that usually goes from the federal government to the state government is handled differently when a bond bank, or SPV, is in place. When this occurs, the money required to guarantee the bond bank or SPV operations is redirected to a trust account and the state government cannot use it for purposes other than debt service payment.

¹⁶ Decreto 258 – Enero 17 2003- Ley de Deuda Pública del Estado de Michoacán de Ocampo

¹⁷ Decreto 259 – 28 de Enero de 2003 – Autorización de Endeudamiento & Decreto 507 – 31 de diciembre de 2004 – Autorización de Endeudamiento

The new law authorized the features required for a mechanism that enables the operation of a bond bank. A bond bank can be created with its own limits and controls through local laws. It can have a very healthy management without any federal intervention, while intercepting federal revenue streams is guaranteed, based on the federal law reform.

The project with the Government of the State of Michoacán and EDII was key to the finances of the state, and in general for the country, since it successfully executed a transaction model whose interception of cash flows has been replicated by many states and municipalities in Mexico over the last 15 years. The Michoacán financial transaction was innovative since it used this model of an irrevocable private trust for the first time in Mexico.

EDII staff provided technical assistance to the state during the implementation stages including designing, structuring, and implementing the financial transactions using the new model of interception of cash flows; establishing a new payroll tax; and implementing a participatory budget by results. At the time, most of the states did not have a payroll tax because there was little incentive to expand their own tax collection efforts—the bulk of their revenues are delivered through the transfer of their share of federally collected revenues. This new payroll tax demonstrated to the private sector that the state was serious about maximizing revenues and being accountable, and this was recognized by the credit rating agencies (Annex IX. EDII Response to Draft Evaluation, p. 25-26).

The new financial model was proven a success, setting the stage for other states and municipalities in Mexico to access more favorable financing from private and public sources. At the time, the USAID/Mexico-EDII activity was focused on economic development, democracy, decentralization, and municipal autonomy. The results achieved were consistent with the activity objectives. The Michoacán case, and the financial mechanism used, became the public funding standard in Mexico. Today, 15 years later, it is still in force, allowing the state to mobilize more than MX 580 billion Mexican pesos for the development of productive public projects by subnational entities in Mexico.

Additionally, the law increases potential for states and municipalities to augment their own ability to collect local taxes as another revenue source. Some can collect a considerable amount of money and take part of the guarantee in the future.

With the aim to identify other potential sources for reliable and steady income for the state governments that could reinforce its credit worthiness, the team asked key informants: “Are there income generating opportunities in local taxes?” One answered: “Yes, there are opportunities; it can be an enhanced source. [For example], the car ownership tax (*tenencia*) should be a main one.” He also warned, “There are deep cultural problems for establishing more taxes (distrust in government’s accountability and transparency in the use of public money).” In any case, he added, “[since] setting up a tax is unpopular, and while revenue streams come from federal taxes in sufficient quantities, the blame for the increase in taxes remains at the federal level, while the use of them is local.”

Capacity Building Activities

During each set of activities, EDII undertook a number of capacity building activities as a way to educate local, regional, and national actors in the new approach and provide a sustained presence of the USAID-EDII Activity over time. EDII, jointly with a prestigious business university IPADE and the Fund for Capitalization and

Investment in the Rural Sector (FOCIR),¹⁸ created a public finance course (Senior Management Private Capital Program, ADECAP) addressing the needs of Mexican private sector executives and public sector officials participating in Mexican capital markets. The course was recorded on video and includes USAID-EDII case studies, as well as presentations and cases from other specialists in the Mexican public finance sector.¹⁹

EDII also developed a training module on financial models (including PPP options) addressing the needs of Mexican private sector executives and public sector officials participating in the Mexican capital markets. The publication is accessible on the web.

According to Humberto Suarez, former General Treasurer of the State of Michoacán de Ocampo and Secretary of Finance of the State of Michoacán de Ocampo, Evensen Dodge International provided the State of Michoacán with training and technical assistance that were important to carry out the project in that state.

“Evensen Dodge International [staff] accompanied me to meetings with the governor to explain the model and to obtain the necessary authorizations to make it happen. Afterwards, the Evensen Dodge Company was asked to train the State General Treasury personnel with whom they would have to work in order to implement this project, and a series of very professional workshops were carried out. Also, I requested that Evensen Dodge staff accompany me [on visits] with local deputies to explain the model and the financial transaction, so that they could approve the modifications for legal reform, the use of this financial model, and the financial transactions as well. Evensen Dodge staff were also requested to participate in meetings at the State General Treasury, and to conduct in-depth seminars and workshops to the personnel involved in different departments of the state government. It was hard work and Evensen Dodge International, in coordination with the subscriber and staff of the state treasury, attended it successfully.”

HUMBERTO SUAREZ

The principal government official involved in the negotiations and the implementation of the loans in Michoacán said, “In my opinion, one of the most important lessons is the confidence that the public official must have in his financial advisor [in this case, Evensen Dodge], and at the same time the need to establish relevant monitoring mechanisms [is also important].” He added, “Having an advisor who can indicate the important steps to reach the desired result, who worked and assisted us to coordinate service providers including lawyers and fiduciaries, etc., and who accompanied us to the state congress to explain the models, facilitated the process

¹⁸ IPADE, *Instituto Panamericano de Alta Dirección de Empresa*, de la Universidad Panamericana is the Pan-American University’s business school.

¹⁹The link to the FOCIR website is

<http://www.focir.gob.mx/ingles/template1.aspx?nombre=Programa%20de%20Alta%20Direcci%C3%B3n%20en%20Capital%20Privado>

of decision-making and approvals allowed us to reach the objectives in less time.”

A 2014 summary PowerPoint presentation by EDII on the results of the GDA agreement states that over 1,000 people were trained.²⁰ The team was not able to verify the number of people trained, however, as no training records were available for review. (See Annex VIII. Data Limitations.)

A comprehensive description of the training and capacity building activities undertaken by EDII staff is found in Annex V and a description of technical assistance provided is found in Annex IV.

Conclusions

1. The USAID agreement and alliance with EDII contributed to accelerating a process that is critical for enhancing finance for sustainable development in Mexico.
2. The work expanded and achieved more visibility having USAID as a partner, as it was then perceived as a driver for systemic change, and the work was no longer viewed as isolated efforts by a new player in the financial markets, as EDII was when it began in 2002.
3. As a result of EDII’s activities supporting the necessary legal reform at the federal level, the ability of subnational (municipal and state) governments to issue bonds or other financial tools as options for expanding their credit access at a federal level was secured.
4. EDII provided extensive technical assistance and training for officials in the early phases of the agreements, which strengthened investor confidence (Annex IX. EDII Response to Draft Evaluation, p. 35).

HOW IS THE EDII ACTIVITY ADDRESSING THE NEEDS OF TARGET BENEFICIARIES?

EDII and USAID identified two levels of beneficiaries for their activities, each with differing sets of needs:

- The first level of beneficiaries was the group of local government authorities requiring access to financial expertise.

The USAID-EDII Activity provided a tool for state and municipal governments to increase their financial ability to match the demands of their citizens. This Activity has definitively delivered to local governments the objective, i.e., to expand their alternatives to access private financial markets.

- The second level of beneficiaries was the local community residents, who require solutions to their legitimate demands.

Palladium’s evaluation did not have the means nor scope to survey a sample of citizens on how EDII’s activities influenced their lives. Therefore, there are no figures about the second level beneficiaries who are, from a USAID perspective, also main beneficiaries. However, there is no public participatory process in place, in any Mexican state, that guarantees all infrastructure projects be prioritized in consultation with citizens and their needs. At the same time, a representative democracy such as Mexico’s has other informal means to make

²⁰ Evensen Dodge PowerPoint Presentation: Mobilizing Private Financing – The Capital Market Story of Mexico, May 2014
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citizens' needs known to politicians. Upon reflection, the manner in which these governments deliver services to their population is a question of how a government really represents and cares for their population, and, though this USAID-EDII Activity is intended to help guarantee this final delivery, it is beyond the scope of the GDA.

The infrastructure projects in five states were reviewed and estimates on the number of beneficiaries reached (by estimating the number of municipalities and their populations) resulted in over 27,923,891 people being reached by the projects undertaken in those states (Table 3). The evaluation team was unable to conduct site visits or interview local beneficiaries, however.

TABLE 3: NUMBER OF BENEFICIARIES BY STATE

STATE	NUMBER OF BENEFICIARIES
Michoacán	4.5 million
Hidalgo	4 million
Quintana Roo	2,223,891
Vera Cruz	15.2 million
Guanajuato Puerto Interior	2 million
Total	27,923,891

The evaluation team devoted considerable effort to reviewing EDII records in an attempt to identify the completed transactions and calculate the total value of said actions (Annex VI: Evensen Dodge Loan Transactions). The estimated total for the completed transactions was USD \$1.5 billion, with an activity limit of USD \$2 billion. In the initial years, a large number of projects were discussed with subnational entities, and these were included in reports to USAID. Many of these projects did not come to fruition but this was not reflected in subsequent reports, creating initial confusion about the number of actual completed transactions. The transactions in Annex VII are a final compilation prepared by EDII in May 2018; the evaluation team was not been able to verify the completeness of the list (Annex VIII. Data Limitations).

Although facilitating financing for clean energy and crime prevention projects was a new objective of the 2015 GDA, these projects were slow to come on-line. The activity was criticized for not “closing more deals” in the energy efficiency and renewable energy arena.

A spokesperson for EDII noted that “the actual window for developing new clean energy projects dates to the 2016 modifications of the energy reform. This presents a very narrow window for subnational governments to evaluate their opportunities under the new legal framework, identify opportunities, and plan and design

projects, though some entities clearly recognized the opportunity and have made significant advances. Additionally, a self-imposed ban that Mexican states have on new borrowing in the final months of an administration further tighten[ed] the window for infrastructure project development.” (Annex IX. EDII Response to Draft Evaluation, p. 9-10).

In July 2018, EDII informed the evaluation team that two clean energy projects were close to completion—the Coahuila solar plant and the Iztapalapa public LED lighting project. However, neither had been completed at the time of this report (Annex VII: Financial Transactions in the Pipeline). As discussed previously, EDII was encouraged that the crime prevention fund in Veracruz would deliver results.

EDII’s expertise is in the field of providing financial advisory services and EDII worked mainly on the financial side to make project finance possible for any type of project. In this regard, EDII’s work in the financial sector has been praised as highly professional and effective. EDII had less expertise in the later priority sectors for USAID—clean energy and crime prevention. EDII maintained that increasing clean energy and energy efficiency demand and crime prevention were not areas in which it had a great deal of expertise. One approach that EDII adopted to address the interest in clean energy projects was to hire a firm of external clean energy experts. Just as important, EDII argued, they were respectful of state sovereignty and did not push for a specific agenda or type of transaction—such as clean energy—but supported what local governments proposed as projects to be financed.

Conclusions

1. The new tool (bond bank/SPV) that was created under the Activity provides subnational government officials with alternate options for financing for municipal and state projects and, if adequately used, it can contribute to satisfying local population demands for improved and sustainable municipal infrastructure services.
2. EDII was slow to meet the objectives of last three years of the GDA to generate transactions for clean energy and crime prevention projects.
3. A major inherent constraint in achieving the above goal is the overriding principle of state sovereignty in choosing the focus of the projects to be financed.

HOW EFFECTIVELY IS EDII BUILDING THE CAPACITY OF IMPLEMENTING PARTNERS AND ACTIVITY BENEFICIARIES?

Over the course of the activity, EDII was selected by several state governments, such as Quintana Roo, Hidalgo, and Michoacán, as the firm to provide financial advisory services. As the market matured, some state governments were looking for other local firms, showing that the market is open and there are existing developed capacities. It is still early to assess if the supply can respond to development challenges.

At the state government level, it seems that those states benefiting from EDII services have developed their own capacities. EDII noted that several of its clients, including the state governments of Quintana Roo, Hidalgo, and Michoacán have successfully accessed capital market financing without EDII assistance (Annex IX. EDII Response to Draft Evaluation, p. 13). However, the institutional permanence of this in-house capacity is difficult to ensure as technical expertise in key political/technical positions is hard to retain as high staff turnover is relatively common.

Conclusions

1. EDII provided technical assistance and capacity building training throughout the life of the activity. The training was well received and appears to have provided a solid foundation for those trained.
2. EDII faced a constraint outside of their control, which was the high turnover rate that accompanies political changes at elections.
3. One solution that would guarantee more stability for highly professional and skilled staff in this financial arena would be to create an institutionalized bond bank (an autonomous institution that is independent from the state government and the state parliament), with state of the art organizational and labor standards.

HOW DOES THE ACTIVITY SUPPORT THE OBJECTIVES OF MEXICO'S ENERGY REFORM?

The major goals of the Mexican energy reform were to:

- Open the energy sector to a variety of participants; and
- Reduce the cost of energy services.

Mexico's Energy Reform started in 2012 and further changes were issued under the 2016 adjustment reform. The reforms established a new and robust legal framework that directly sets the ability of states and municipalities to build energy-related infrastructure projects. Prior to the energy reform, the Federal Electricity Commission (*Comisión Federal de Electricidad*, —CFE—a public enterprise) was the sole national utility. As such, it held monopolistic powers on generation, transmission, and distribution (Annex IX. EDII Response to Draft Evaluation, p 8-9).

The 2012 energy reforms allowed private entities to generate power, but only for their own consumption. The 2016 modifications allowed private entities to generate and sell energy in Mexico's energy market, provided they registered as Qualified Generators with the Energy Regulatory Commission (*Comisión Reguladora de Energía* -CRE). The latter modifications also permitted private use of the nation's electrical grid system, provided they registered as Qualified Suppliers and paid a transmission fee to the CFE's National Energy Control Center (*Centro Nacional de Control de la Energía* (CENACE)). The reforms also allowed private and public entities to purchase electricity directly from third parties and not just through CFE (Annex IX. EDII Response to Draft Evaluation, p. 8-9).

Under the law, municipal power distribution grids must be updated with circuits that can handle medium voltage, and that can measure power. Most cities and towns in Mexico do not yet meter systems connected to the distribution grids. With the 2016 energy reform modifications, subnational governments are permitted to meter their electricity usage and to seek lower power prices in the new energy market, looking at offers from Qualified Generators and Qualified Suppliers. It creates opportunities for these entities to explore new technologies that promote greater energy efficiency, such as LED public lighting systems (Annex IX. EDII Response to Draft Evaluation, p. 9).

States and municipalities also may participate in energy generation projects if they are registered with CRE as

Qualified Generators or Suppliers. Some generation projects are in development, including the waste-to-energy project for Hidalgo and the Coahuila solar park, that are part of EDII's pending project pipeline as reported to USAID (Annex VII: Financial Transactions in the Pipeline).

The legal reforms and additional mechanisms providing financing to states and municipalities has opened the possibility for growth in clean energy projects. Some state governments proposed and developed energy projects, even prior to the final GDA agreement, specifying this as a priority goal.

Two examples of way in which the new financing vehicles was used for related projects are described below:

- In the State of Hidalgo in 2009-2011, while state financing was used to purchase land for a new oil refinery (to be built by the federal government), and provided new money for a state administrative complex, this transaction also included roughly 20 municipalities borrowing to make *green improvements to their public lighting systems*.
- In the case of Veracruz, the state government created a local energy agency and a crime prevention fund which could be the recipients of monies available from the debt restructuring.

Interviews with project developers in the area of waste-to-energy and clean energy, who were engaging with EDII to complete financing for projects, revealed that there was some loss of reputation for the approach as a result of their interactions. The developers expressed increased uncertainty about the prospect of completing the financial transaction for their project after their interactions with EDII. A few companies reported frustration that EDII's commitment on financing had not been delivered yet. An official of a fourth company expressed disappointment with the process and withdrew from the project.

Conclusions

1. The new opportunities based on debt restructuring become opportunities to enhance local energy investments. These have captured the attention of other states experiencing debt stress.
2. The potential for generating clean energy projects exists, through relatively few have been developed to date. EDII sees these approaches as opportunities to continue expanding their portfolio.
3. Engaging with those actors involved in local energy policies and projects at the outset would further advance this agenda.

WHAT CAN BE ACHIEVED BY THE END OF PHASE FIVE?

In July 2018, Mexico had a presidential election and all political movements were viewed within the context of this national event. In an election year, finance is always under higher scrutiny and a very conservative approach by state governors and by the Federal Ministry of Finance regarding expansion of the bond banks is likely, at least for the near future.

Conclusions

1. A new institution to manage the role of a bond bank is not likely to be established by the end of Phase 5 in July 2018.

2. Once EDII completed the highly visible case of restructuring the debt of the State of Veracruz, EDII turned back to the clean energy agenda. However, it was too late to close a transaction on clean energy before the end of the Activity in July 2018.
3. The success of the Veracruz debt restructuring activity could mean the consolidation of the bond bank/SPV tool in Mexico. In other words, as the success is publicized, other states may realize the benefits of this tool in their own region.

IS THE ACTIVITY DESIGNED AND IMPLEMENTED IN A WAY THAT ONCE USAID LEAVES THE ACHIEVEMENTS REMAIN AND ARE CONSOLIDATED?

Mexican financial markets are able to work for and/or with local governments, and financial institutions increasingly are aware of the potential positive development of this market niche and are directly engaging with states and municipalities. The changes in the legal framework to allow the new financing mechanism are solidly established at the national level and are beginning to emerge at the local level, as some states already have completed their own legal reforms. These positive examples should encourage other states to follow by undertaking their own reforms and setting up the bond bank/SPV over time.

Mexican financial markets are able to work for and/or with local governments, and financial institutions increasingly are aware of the potential positive development of this market niche and are directly engaging with states and municipalities.

“... this mechanism (the SPV/bond bank) changed the way to do finance in our country.”

A FORMER FINANCIAL COORDINATOR FOR THE STATE OF HIDALGO

While additional work can contribute to improve what has been already achieved and to expand the impact of the new financial tools available for local governments, even under the scenario of USAID withdrawing from this space, it is very likely that the GDA outcomes will remain in place. However, the use of these new financial tools for addressing developmental issues, such as climate change, needs further discussion to determine the usefulness of this vehicle to engage the public sector in this space.

One important question that emerged during the evaluation was “Why have no additional bond banks been established since the two existing banks were created in 2006, 12 years ago?” Two main factors appear to be constraining the development of additional banks: institutional inertia and the political support needed to create a bond bank.

One key informant expressed the concept of institutional inertia in this way: “Past paradigms, fear, and ignorance stop innovation in such a delicate issue as public finance. Politicians don’t want potential sources of political conflict and Secretary of Finance staff don’t move beyond their comfort zone.” Another individual noted, “to establish finance institutes at the state level is a process that would have required well over a year of legal work to do all the drafting...there was no incentive to save any money on borrowing, at least at that point in time.” (EDII staff member.)²¹

²¹ Interview with Elizabeth Bauch. EDII staff.

The second factor relates to the events at play in the Mexican political landscape. “Improving loan conditions would benefit public balance,” one key informant said, “but not a state governor with political campaign interests.”

As discussed under Research Question I (“To what extent were the activities implemented as planned during the five main phases?”), several key informants alluded to the idea that state finances are suspected of being a main financial resource for national parties’ campaigns. The transparency and accountability that a bond bank requires can become an obstacle for some political leaders who may want to misdirect the use of public money.

“Transparency isn’t always popular with [governors or secretaries of finance]. Sadly, I honestly think that was one of the reasons that nothing went forward, without making a pretext or excuse, as it was much easier for these entities to use traditional funding because they had access to them,” as one key informant said.

Conclusions

1. The Activity was designed and implemented in a way that makes it self-sustaining over time.
2. Local governments have the option for expanded access to financial markets.
3. Tasks remain to be done to consolidate the achievements, but the current outcomes will remain and improve.

WHAT SHOULD BE HIGHLIGHTED TO REPLICATE THE MEXICAN EXPERIENCE IN OTHER COUNTRIES?

Mexico, as an emerging economy and within the top 10-15 largest economies in the world, is a country with a wide, deep, and sophisticated financial market. Mexico’s size and political complexity present a singular case for enhancing local government access to financial markets.

Due to these distinctive characteristics, replicating this case in other countries will require a proper assessment of the local conditions and an adaptation of what was implemented in Mexico. “The solution needs to be tailored to the exact situation so [that] it works for investors and borrowers.”²²

No central administration (such as the federation in Mexico) wants the states/provinces to go bankrupt, as this can bring increasing economic problems to the nation. On the other hand, there are legitimate demands from states/provinces that need to be satisfied. It can be instrumental to find that balance between what the federation/central administration and the states/provinces can do and control from the financial point of view. Mexico is a special case, because the state sovereignty existing in Mexico does not occur in every country. Those financial institutions involved in the creation of bond banks/SPVs need to be aware of how these financial vehicles can develop in each country.

As a former USAID manager of the Activity in the initial years of the GDA, who is now currently working for EDII, noted, “...if there is a banking system, something can be done. If entities want to borrow money and there is a pension system, an insurance system, and a banking system, there is something that can be done. You have to work with the full range of market actors/stakeholders and regulators, and you have to find out if there

²² Interview with Elizabeth Bauch
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is a willingness and political support from the host country, and not every country presents those conditions.”²³

The basic starting steps are having high-level political will and completing the required legal reform. An additional key step is capacity building at all levels in most developing countries, especially at the local government level.

Conclusions

Government and financial institutions, project ownership, and adaptability to local conditions are the main factors required to replicate the outcomes of this activity in other countries. However, in the case of Mexico, it is of particular importance to understand how complex and developed the local financial market is and how such tools as a bond bank/SPV can play a decisive role in supporting the development of strong local government financing.

²³ Interview with Elizabeth Bauch

V. CONCLUSIONS

This section presents the major conclusions on the achievements of the GDA with EDII over the 16-year period and ranks them in terms of achieved, partially achieved, and not achieved.

LOCAL GOVERNMENT ACCESS TO FINANCIAL MARKETS: ACHIEVED

EDII was instrumental in creating the national legal framework for creating bond banks. In doing so, the EDII-USAID activity provided access to financial markets for local governments to expand their ability to meet growing infrastructure demands for their population. In the states of Michoacán, Hidalgo, Quintana Roo, and Veracruz, new financing vehicles were established that enabled the municipalities to obtain hundreds of millions of dollars in financing for roads, health care, education, airport facilities, and other local priority infrastructure projects. (See Annex VII. Evensen Dodge Financial Transactions.) This required capacity building and, in Hidalgo, the development of a new public-private partnership law. The terms of these loans were far superior to alternative financing vehicles such as commercial banks.

CREATION OF A NATIONAL BOND BANK: PARTIALLY ACHIEVED

One model, originally targeted by the GDA, was to create a single national bond bank. During the evolution of the activity, no national bond bank was created. However, using the changes achieved in the legal framework, two state bond banks were created, and the State of Veracruz transaction introduced a new special purpose financing vehicle, the Accredited Trust, which, for the purposes of Mexican states and municipalities, functions like a bond bank. These special purpose financing vehicles provided subnational governments with additional resources to meet the infrastructure needs of their citizens. EDII estimated that about 28 million people benefited from infrastructure services provided by these new resources. However, the evaluation team did not have access to information to verify this number nor information on how this translated to answering the needs of the citizens.

INVESTMENTS IN CLEAN ENERGY AND CRIME PREVENTION: NOT ACHIEVED

The creation of bond banks/SPVs has the capacity to contribute to enhancing the development possibilities opened by the energy reform. To date, there is little evidence of direct investment in energy efficiency and renewable energy projects using the bond bank/SPV vehicle. In the last phase of the activity, EDII placed secondary emphasis on the GDA objective of promoting clean energy and crime prevention while focused primarily on restructuring of Veracruz's debt. One outcome of the Veracruz debt restructuring was the creation of a crime prevention fund and, over time, more investments may be seen as a result. With greater oversight, USAID may have been able to better steer activities to meet USAID's and the GDA's objectives.

SATISFYING SECONDARY BENEFICIARIES: UNKNOWN

The services provided by EDII improved municipal services in response to the local government demands: nearly 28,000,000 residents in five Mexican states were reached through the projects. However, no data were available to describe how these reforms have contributed to satisfying local citizens' infrastructure demands or needs. This could be considered outside of EDII's scope, which was to provide new models of financing for subnational level governments. (See Annex IX. Data Limitations.)

BUILDING LOCAL CAPACITIES: PARTIALLY ACHIEVED

EDII's work in capacity building (especially evident during the period of administration change, Phase III, Table I) improved the ability of officials and staff in the states to understand and use the bond bank/SPV tool. However, the personnel rotation is high in local governments, leading to the loss of qualified staff and lack of sustainability of the training, due to no fault of EDII.

SUSTAINABILITY OF ACTIVITY RESULTS: ACHIEVED

Activity results will be sustained over time as the legal reforms have been created, put into practice, and are replicable in other subnational entities. In addition, financial transactions have been closed in four states. The case of Veracruz restructuring its debt may promote the bond bank/SPV tool among other Mexican states as the tool would demonstrate its success to other subnational entities. Further, other financial advisors – private Mexican financial institutions- have begun to work in this market.

ON THE GDA MANAGEMENT: NEED FOR MORE USAID OVERSIGHT

EDII acknowledged that through the partnership with USAID they increased their own capacity and outreach. EDII gained the trust of other stakeholders by working with USAID and the brand of USAID. Working with USAID expanded EDII's network. For USAID, EDII has been a solid partner in promoting and facilitating the opening of the legal framework and enabling local governments to access financial markets with superior terms. This goal was strategic for both parties in the GDA.

A private sector partner and the U.S. Government have many coincidental interests, however, and at some point, those can diverge. When the USAID-EDII agreement changed to emphasize work on clean energy and crime prevention, which meant more focused work by EDII in the generation of an adequate and bankable pipeline of projects, there was a divergence of strategic interests. While USAID wanted to take concrete steps in clean energy and crime mitigation areas, EDII was more focused on expanding its influence as a reliable and highly qualified financial advisor.

While it is possible that the Veracruz case can foster future opportunities for clean energy and crime prevention projects by releasing financial resources from debt payment obligations and by creating the Veracruz Energy Agency,²⁴ EDII's focus on Veracruz debt restructuring seemed to neglect the delivery of the GDA objective for 2015-18 on the activity pipeline.

Stronger USAID GDA oversight could have detected the diverging interests and ensured that activities remained focused on GDA objectives. This particular problem arose in the last stage of a long collaboration. USAID management would have benefited from having a deeper understanding of the complexity of the Mexican financial markets and political priorities, during the last phase that led local governments to prioritize financing for other infrastructure projects unrelated to crime prevention and clean energy.

Neither EDII nor USAID sets priorities for elected officials at any level of government. It may have been risky to agree on asking state governments to invest in energy and crime prevention without a better understanding of the local priorities for various Mexican subnational entities. USAID could have been better informed about these local priorities, and thus could have better understood the feasibility trying to focus financing on clean energy and crime prevention projects.

²⁴ <https://imagedeveracruz.mx/noticia/nace-la-agencia-estatal-de-energia-1220>

VI. LESSONS LEARNED

OWNERSHIP AND POLITICAL WILL

An activity like the USAID-EDII partnership totally depends on the local governments' and stakeholders' will to make it work. It takes time to build the proper environment for a successful activity—to start identifying stakeholders, evaluating the market, determining barriers, and exploring and offering potential solutions. Further, finance is always a very sensitive area at any level. Its management entails responsibility, respect for fiduciary duties, and managing risks even when the best intentions guide decision-making. Financial matters also have high political visibility. Consequently, governors and secretaries of finance move very cautiously and are risk-averse. Innovation in local public finance is not their priority; they prefer to move within traditional practices.

TIMING

Mexico's political context was favorable for the introduction of this activity. The federal and some state governments were looking to open access to financial markets for local governments when the agreement between EDII and USAID was signed. It was significant that there was a new party in power and the incoming president was formerly a state governor. This change, plus the new balance of power, explains the change in favor of a legal reform for more financial autonomy for state governments.

PATIENCE

Fiscal reforms—involving the executive and legislative powers—and the need to build capacity among local governments required time, focus, and clarity on the long-term goal. EDII was patient. They understood that the change in local government finance was an unstoppable process and backlashes were only the logical reaction against change that some actors always push for.

TRUST

The reform and the readiness for projects require huge efforts and wide expertise. Alliances and partnerships are necessary, and they can be achieved by building trust with all other stakeholders.

EXPERTISE

The technical expertise provided by EDII fulfilled a previous vacuum and was well appreciated. Counting with experienced and capable staff has shown to be the key for success.

RESISTANCE

Opening a new frontier for finance challenged the “business-as-usual” approach. There are sectors of local governments' staff and some banks that benefit from the status quo and vested interests in the federal government that were uncomfortable or negatively impacted by the change.

INSTITUTIONAL INERTIA

Both at the local and at the federal level, a legal reform faces challenges for institutional adjustment, management

styles, and culture. People are averse to innovation and risk.

HONESTY

Financial flows in general and particularly those from the federation-to-states-to-municipalities have been obscure and lack transparency. As such, keeping the activity clean of any suspicious transaction has been difficult, but is needed because of its importance in the context of a transition to a renovated democracy in Mexico.

BROAD SUPPORT FOR DEVELOPMENT

It is critical to have top-level (governors' and/or mayors') support for the financial reform and clarity to make progress. There were opportunities where the finance staff was convinced of the value, but all efforts were useless because there was a lack of prior. The best way to get this support is to clearly align the activity with the state or municipality political objectives.

VII. RECOMMENDATIONS

How can USAID build on the GDA's success and weaknesses to enhance the potential for impact in ongoing and future similar initiatives?

1. Prior to entering into a GDA, USAID should conduct due diligence as to whether the GDA objectives truly align with the priorities of the beneficiaries (in this case, the States) and the GDA partner.
2. Partners should ensure buy-in and ownership by all key government actors at all levels by engaging—at an early stage—with local organizations (business and civil society) on raising the profile of clean energy projects in the local political agenda.
3. Partners should recognize that the activity pipeline responds to legitimate sovereign interests. Therefore, creating partnerships with local stakeholders on clean energy and energy efficiency needs would have been a good step forward to identify more projects aligned with these objectives.
4. Improve accountability and transparency by applying the tools (regulations) in the bond bank design and setup.
5. Incorporate new climate risk tools to be used to conduct financial risk assessments in those projects to be financed by bond banks.
6. In an effort to ensure a process to improve USAID's oversight of activities, USAID should establish clear guidelines for reporting of progress and achievement of results from the different transactions and activities supported by USAID/Mexico. It is recommended that in future activities, partners, such as EDII, submit state or municipal level reports that include more evidence to support the actual outcomes achieved. These reports should present data on findings selectively and in an understandable manner; should organize data around objectives and major themes; and use charts and tables. Conclusions should be clearly connected to evidence on performance.
7. In future similar activities, it would be useful to identify themes (a learning agenda) on which summary reports could be prepared periodically to highlight key points from different types of transactions.

ANNEX I: EVALUATION MATRIX

The Evaluation Matrix provides the overarching scope of work for the evaluation. The matrix includes the list of approved evaluation questions, as well as the expected data sources and data collection methods. The discussion of the evaluation methodology (Annex II) and Data Limitations (Annex VIII) identifies how the evaluation was conducted and where the expectations of the SOW were and were not met.

I. Evaluation Criteria: Relevance - How does the EDII Activity relate to the main goals & objectives of the USAID Mexico Energy Activity?

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
I. Is the Activity relevant to USAID Mexico Energy Activity's goals & objectives?	How does the EDII Activity relate to the main goals and objectives of the USAID Mexico Energy Activity?	• USAID-EDII Activity documents including activities conducted and strategies or methods used to implement the EDII activity • Key government officials and other partners • USAID Mission Director and staff	• Review of activity documentation • Document analyses (Excel Database) • Interviews with relevant stakeholders, including Evensen Dodge project director and managers, pilot projects managers from different states and municipalities, representatives of the federal government, such as the Ministry of Energy in Mexico, and consultants
Sub-Questions	• To what extent is the Activity aligned with national strategy of Mexico's energy reform, including specific federal and regional strategies and legal frameworks?	• Activity documents • Key government officials and other partners	• Document analyses (Excel Database) • Interviews with relevant stakeholders and implementing partners

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
	• How does the Activity support the goals and objectives of the USAID Mexico Energy Activity? • How does the Activity support the objectives of Mexico's energy reform? • Does the Activity adequately take into account the national realities, both in terms of institutional frameworks and programming, in its design and implementation? • To what extent were national partners involved in the design of the EDII Activity?		
I.2 Is the EDII Activity addressing the needs of target beneficiaries?	How does the Activity support the needs of target beneficiaries, including direct and indirect activity beneficiaries? Direct activity beneficiaries are those government institutions or entities advised by EDII, such as the government officials with whom EDII has worked, and indirect activity beneficiaries include communities directly benefitting from local activities that evolve because of EDII's support, including assisting with legal reforms?	• Activity documents • Key government officials and other partners • Assessment of legal reforms that were achieved	• Document analyses (Excel Database) • Interviews with government officials and partners • Implementing Partners Survey and Activity Beneficiaries Survey • Focus Groups with Activity beneficiaries • Legal analysis

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
	• Is the implementation of the Activity being inclusive of all relevant stakeholders? • Are local beneficiaries and stakeholders adequately involved in activity design and implementation? • To what degree were stakeholders satisfied with activity implementation?		

2. Evaluation Criteria: Effectiveness: To what extent are the expected results/outcomes being achieved?

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
2.1 Is the EDII Activity addressing the needs of target beneficiaries?	• How does the Activity support the needs of target beneficiaries, including direct and indirect activity beneficiaries? Direct activity beneficiaries are those government institutions or entities advised by EDII, such as the government officials with whom EDII has worked, and indirect activity beneficiaries include communities directly benefitting from local activities that evolve because of EDII's support, including assisting with legal reforms?	• Activity documents • Key government officials and other partners • Assessment of legal reforms that were achieved	• Document analyses (Excel Database) • Interviews with government officials and partners • Implementing Partners Survey and Activity Beneficiaries Survey • Focus Groups with Activity beneficiaries • Legal analysis

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
	• Is the implementation of the Activity being inclusive of all relevant stakeholders? • Are local beneficiaries and stakeholders adequately involved in activity design and implementation? • To what degree were stakeholders satisfied with activity implementation?		
2.2 To what extent were the activities planned during different stages of the EDII Activity implemented as planned? (Pilot projects implemented as planned, capacity building activities, etc.)	• How are EDII activities implemented across different target beneficiaries (i.e., government institutions, organizations, communities)? • Are these differently implemented EDII Activity activities conducive to achieving the expected outcomes?	• Activity documents • Key government officials and other partners • Published official documents	• Document analyses (Excel Database) • Interviews with federal and regional government officials and partners • EDII Project Staff Survey, Implementing Partners Survey. • Focus Groups with Project beneficiaries
2.3 What barriers or challenges were faced during implementation?	• What are the main challenges that may facilitate or hinder implementation and impact of activity efforts? • Have any of these been addressed through project management? How?	• Activity documents and past audits or evaluations • Activity beneficiaries • EDII Activity staff and Implementing Partners.	• Document analysis (Excel Database) • Interviews with federal and regional government officials and partners • EDII Activity Staff Survey, Implementing Partners Survey

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
		• USAID Mission Director and staff	
2.4 How effective is the Activity in achieving its expected outcomes?	• Is the Activity effective in building capacity for Implementing Partners and activity beneficiaries through the achievement of its expected outcomes?	• Activity documents • Key stakeholders	• Document analysis (Excel Database) • Meetings with main Activity Implementing Partners including federal and regional government officials and other partners • EDII Activity Staff Survey, Implementing Partners Survey, and Activity Beneficiaries Survey • Focus Groups with activity beneficiaries
2.5 To what extent were the activities that were planned during different stages of the EDII Activity implemented as planned? (Pilot projects implemented as planned, capacity building activities, etc.)	• How are EDII activities implemented across different target beneficiaries (i.e., government institutions, organizations, communities)? • Are these differently implemented EDII Activity activities conducive to achieving the expected outcomes?	• Activity documents • Key government officials and other partners • Published official documents	• Document analyses (Excel Database) • Interviews with federal and regional government officials and partners • EDII Activity Staff Survey, Implementing Partners Survey. • Focus Groups with Activity beneficiaries

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
How efficient are partnership arrangements for the Activity?	• To what extent were partnerships between government institutions/ or organizations encouraged and supported? • How many partnerships between government institutions or organizations were established? • What were the efforts associated with creating each partnership? • What was each partnership supposed to do? • Which can be considered sustainable over time? • What was the level of cooperation and collaboration arrangements? • Which methods were successful or not, and why?	• Activity documents and evaluations • Activity partners • Beneficiaries	• Document analysis (Excel Database) • Interviews with federal and regional government officials and partners • EDII Activity Staff Survey, Implementing Partners Survey

3. Evaluation Criteria: Relevance – How does the EDII Activity relate to the main goals and objectives of the USAID Mexico Energy Activity?

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
3.1 How is the EDII Activity effective in achieving its long-term objectives, and effective in achieving the objectives of the USAID Mexico Clean Energy Activity?	• Will the Activity achieve its long-term goal that is to support Mexico's clean energy targets? • What are the impacts of the Activity on clean energy, energy efficiency, and other co-benefits as socio-economic impact issues?	• Activity documents including white paper on compendium of best practices, and past audits/evaluations • Key stakeholders • Beneficiaries	• Document analysis (Excel Database) • Meetings with main Activity Implementing Partners including federal and regional government officials and other partners • EDII Activity Staff Survey, Implementing Partners Survey, and Activity Beneficiaries Survey • Focus Groups with activity beneficiaries
3.2 Future directions for the Activity	• Are there any possible future activities or opportunities for USAID to consider for future programming? • How could the EDII Activity build on its successes and learn from its weaknesses in order to enhance the potential for impact of ongoing and future initiatives? • Is the capacity that is in place at the national and local levels adequate enough to ensure sustainability of the results achieved to date?	• Data collected throughout midterm assessment • Official legal publications • Activity documents and past audits or evaluations • EDII Activity staff and consultants • Implementing Partners • Activity beneficiaries	• Document analysis (Excel Database) • Interviews with federal and regional government officials and partners • EDII Activity Staff Survey, Implementing Partners Survey

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
3.3 What are the major lessons learned from the implementation of the EDII activities?	• What lessons have been learnt including changes that could benefit USAID-EDII Activity achievements? • How could the EDII Activity better target and address the priorities and development challenges of targeted beneficiaries? • What changes could have been made (if any) to the EDII Activity in order to improve its effectiveness, efficiency, and/or impact?	• USAID-EDII Activity documents including activities conducted and strategies or methods used to implement EDII Activity. • USAID Mission Director and staff • Key government officials and other implementing partners • EDII Activity staff and consultants • Implementing Partners • Activity Beneficiaries	• Document analysis (Excel Database) • Meetings with main Activity Implementing Partners including federal and regional government officials and other partners • EDII Activity Staff Survey, Implementing Partners Survey, and Activity Beneficiaries Survey • Focus Groups with ctivity beneficiaries
3.4 Sampling of loans	• How efficient has EDII been in supporting federal and regional government officials in the use of lending (bonds/loans)? • How selective has it been in the allocation of these bonds/loans and the choice of institutions and partners? • To what extent has EDII promoted the ownership and partnership of relevant national government institutions or private organizations,	• Activity documents and past audits or evaluations • Key stakeholders • Beneficiaries	• Document analysis (Excel Database) • Interviews with federal and regional government officials and partners • EDI Project Staff Survey, Implementing Partners Survey

Component to be Evaluated	Question/Sub Question	Data Sources	Data Collection Methods
	including those working on clean energy and crime prevention issues? • Has the actual distribution of project loans and technical assistance provided by EDII been selective with respect to state and municipality needs and regional locations? • How selectively have these bonds/loans been matched to needs?		
3.5 How is the EDII Activity effective in achieving its long-term objectives, and effective in achieving the objectives of the USAID Mexico Clean Energy Activity?	• Will the Activity achieve its long-term goal that is to support Mexico's clean energy targets? • What are the impacts of the Activity on clean energy, energy efficiency, and other co-benefits as socio-economic impact issues?	• Activity documents including white paper on compendium of best practices, and past audits/evaluations • Key stakeholders • Beneficiaries	• Document analysis (Excel Database) • Meetings with main Activity Implementing Partners including federal and regional government officials and other partners • EDII Activity Staff Survey, Implementing Partners Survey, and Activity Beneficiaries Survey • Focus Groups with activity beneficiaries

ANNEX II. EVALUATION METHODOLOGY

This annex describes the methodology and sources of data and information the Palladium team used to address the different research questions articulated for the evaluation.

DATA COLLECTION METHODS

The Evensen Dodge assessment team used a mixed-methods approach that focused heavily on qualitative methods, to collect the data about the Evensen Dodge activities implemented from 2000-2018. The team used three primary data collection methods to increase validity of findings and recommendations. These data collection methods are described in Table II. The total number of key informant interviews is found in Table III. The data collection instruments are found in Table IV.

TABLE II. DATA COLLECTION METHODS

GOALS	DESCRIPTION OF METHOD
Desk Review	Identified and reviewed relevant sources of information. Conducted a desk review of all available Evensen Dodge activity documentation, including GDA agreements, Quarterly and Annual reports, and ad hoc reports.
Interviews with Project Managers and Implementing Partners	Conducted interviews with Evensen Dodge project managers and state government officials (former Secretaries of Finance) from Hidalgo, Michoacán, and Quintana Roo to collect detailed information on the activities implemented for the Evensen Dodge Project, as well as results or achievements to date, including specific examples of impact/best practices from the different pilot programs implemented in different states.
Interviews with project managers and activity beneficiaries from selected pilot entities including Hidalgo, Michoacán, and Quintana Roo	Developed a case study protocol to collect information from state government officials and representatives of Hidalgo, Michoacán, and Quintana Roo who, in partnership with Evensen Dodge, have used these financial vehicles to access financing from the domestic capital markets with better terms and conditions. The interviews covered perceptions of the results achieved, challenges encountered and lessons learnt from this partnership. The protocol also included questions about their experiences and satisfaction with the training and technical assistance provided by Evensen Dodge project managers, staff, and consultants. The support was provided to subnational authorities (and associated public and private corporations) to further develop their institutional and financial capacities.

TABLE III. NUMBER OF KEY INFORMANT INTERVIEWS

INTERVIEWEE AFFILIATION	NUMBER
EDII staff	8
State government staff	3
IPs	4
GoM	2
USAID	3
Total	19

The team began by identifying the activity documents using the Evaluation Matrix template and evaluation questions to guide the search for details of the activities. The desk study reviewed the documentation relating to activity objectives; activity preparation; implementation stage documentation including annual reports and the progress reports on implemented activities; and, where available, other activity documents such as Evensen Dodge presentations to partners and training syllabi.

With this information, the team moved to selecting key informants for interviews (Table III) with Evensen Dodge project managers, implementing partners, and activity beneficiaries (see definitions of these categories at the end of the Annex) who described the objectives of the activity, its changes over the years, and the types of activities undertaken at various stages. The team also interviewed people who had transacted loans through the bond bank process; they provided valuable feedback on their experience from this activity.

In addition, the team prepared three case studies from selected pilot entities from the Evensen Dodge Activity—Hidalgo, Michoacán, and Quintana Roo. The purpose was to highlight what the states had accomplished and show how loan resources had been used to invest in public infrastructure, renewable energy, and crime prevention projects at the state level.

The activities in these regions provided details on how the process unfolded and offer promising best practices in how subregional entities were able to adapt the national framework to build the necessary enabling environment for subnational jurisdictions, public authorities, and public-private partnership (PPP) programs to access long-term financing from the Mexican capital market. The information from each case was interwoven into the body of the report.

The team identified a sampling frame that included government officials from these states and other activity beneficiaries to document the three case studies to obtain data on the main financial transactions conducted in

the States of Hidalgo, Michoacán, and Quintana Roo.

The data for the case studies was seriously limited, however, by the inability of the team to gain access to any beneficiaries of the projects and by the very limited access to government officials in each state who could speak about the process of using the bank bond to finance municipal or regional projects. In each state, EDII recommended one official and, given the time and financial limitations of the evaluation, the team was not able to travel to the states and locate additional officials for the interviews.

TABLE IV. INTERVIEW PROTOCOL—PROJECT DIRECTORS AND SENIOR ASSOCIATE ADVISORS

NUMBER	QUESTION
1	How does the EDII Activity support the goals and objectives of the USAID Mexico Energy Activity?
2	How have these pilot pooled financing transactions supported “clean energy projects and crime and violence prevention models”? (Use of the resources for clean energy projects).
3	What has worked/not worked well in running these financing transactions in the different states (i.e., Hidalgo, Michoacán, and Quintana Roo)? Why? For example: Why were there only three states in which bonds were set up, given that ED and high-level Mexican officials saw them as very useful? Why were no new bond banks set up after the first three?
4	What progress has been made in the pipeline (structuring financial transactions) during the last three years of the EDII Activity?
5	What have been some successful factors that have contributed to the effective implementation of the different activities planned for the EDII Activity? Please provide one or two examples.
6	What have been some challenges that have hindered/limited the effective implementation of the different activities planned for the EDII Activity?
7	How is the Activity effective in achieving its expected outcomes? How many partnerships between government institutions or organizations were established? Please provide some examples of supported partnerships or pilot projects. What type of projects were financed by supporting services from EDII activities? (e.g., water sewage, water treatment, public lighting, school improvements, health infrastructure, etc.) What type of pooled financing transactions (bonds/credits and loans), were structured with support of the EDII activities? (Number of states or municipalities that have received a bank bond/credit, or loan, and type of pooled financing transactions structured.)

NUMBER	QUESTION
8	What type of technical assistance or training has been provided to the different states or municipalities? Please provide one or two examples on how the Evensen Dodge Activity managers, staff, and consultants have contributed in building this capacity for the different Implementing Partners and activity beneficiaries? Please identify any changes in capacity in mobilizing resources (i.e., running/using resources) that you have seen after the implementation of EDII activities and technical assistance support and training. Is the capacity that is in place at the national and local levels adequate enough to ensure sustainability of the results achieved to date?
9	Are there any possible future activities or opportunities for USAID to consider for future programming? Please describe areas of opportunities or constraints of EDII activities or bank supported financing transactions.
10	Would it be possible for you to provide us with a list of states or municipalities who borrow money from you?
11	Who would you recommend that we speak with? (from the three different States: Hidalgo, Michoacán, and Quintana Roo), including: • Staff who are currently administering the bond funds; and • Individuals who represent the organizations that have actually borrowed money under the bonds.
12	What approaches or strategies have Evensen Dodge activity managers, staff, and consultants found to be most effective in structuring the different pilot pooled financing transactions?
13	Through its help supporting legal reforms, how does the Activity support the needs of target beneficiaries, including the government officials with whom EDII has worked, beneficiaries such as those who live near a completed infrastructure project (i.e., public lighting, solid waste management), or other beneficiaries?
14	To what extent were the activities were planned during the different stages of the EDII Activity implemented as planned (i.e., pilot projects implemented as planned, capacity building activities)?
15	What changes could have been made (if any) to the EDII Activity in order to improve its effectiveness, efficiency, and/or impact?

DEFINITIONS OF THE TYPES OF KEY INFORMANTS CATEGORIES

Project Management: formally assigned project managers, their staff, and consultants together with implementing partners who provided technical assistance to national government authorities in Mexico to modify their legal and institutional frameworks in order to provide the transparency and confidence investors require when participating in the emerging subnational financing market.

Implementing Partners: implementing partners who have knowledge of the USAID/Mexico-Evensen Dodge Activity or who are familiar with Evensen Dodge's role and activities past or present.

Project Beneficiaries: The Evensen Dodge project is multi-sectoral, with several different pilot project entities. The best means of obtaining more in-depth information and insights from different stakeholders involved in this Activity and impact information across these different government institutions (i.e., states and municipalities), would have been to ask activity beneficiaries directly about their perception of the activity's relevance, benefits, and other key elements or components of the various financial mechanisms implemented by Evensen Dodge activities, and whether they were involved in these activities, and then assess their responses based on an interview protocol developed by the Palladium team.

ANNEX III. SOURCES OF INFORMATION

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5. 2013 09 30 – EDII MEXICO Annual Progress Report
6. 2015 09 30 – (FINAL) EDII-USAID Mexico GDA Final Progress Report (Sept. 2005 – 2015)
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8. Decreto 259 – 28 de Enero de 2003 – Autorización de Endeudamiento & Decreto 507 – 31 de diciembre de 2004 – Autorización de Endeudamiento

KEY INFORMANT INTERVIEWS

The list of interviews conducted with EDII project managers and staff, implementing partners, and Mexican federal and state government officials is listed below in Table VI.

TABLE VI. KEY INFORMANT INTERVIEWS

NO.	DATE	NAME	INSTITUTION & POSITION
1	October 13, 2017	Mr. Fernando Gama	Evensen Dodge, Vice President
2	November 2, 2017	Mr. Fernando Gama Mr. Cesar Corona Mr. Enrique Pees Mr. Ricardo Anguiano	Evensen Dodge, Vice President EDII Project staff EDII Project Staff Implementing Partner (lawyer who worked on developing the reforms for Hidalgo and Veracruz)
3	December 19, 2017	Mr. Humberto Suarez	Former Secretary of Finance of the State of Michoacán (2000-2010)
4	January 12, 2018	Mr. Pablo Uribe	Former Finance Coordinator of the State of Hidalgo
5	January 19, 2018	Interview # 1 with Dr. Elizabeth Bauch	Elizabeth Bauch, Ph.D. Senior Associated Advisor Evensen Dodge International
6	January 24, 2018	Interview # 2 with Dr. Elizabeth Bauch	Elizabeth Bauch, Ph.D. Senior Associated Advisor Evensen Dodge International
7	February 1, 2018	Interview # 3 with Dr. Elizabeth Bauch	Elizabeth Bauch, Ph.D. Senior Associated Advisor Evensen Dodge International
8	February 8, 2018	Mr. Fernando Gama Mr. Cesar Euan	Evensen Dodge, Vice President Former Secretary of Finance, Quintana Roo
9	March 13, 2018	Emma Hodge and Dr. Donald McCubbin	USAID *Discussed sustainability aspects of the EDII Activity.

NO.	DATE	NAME	INSTITUTION & POSITION
10	March 23, 2018	Ing. Mauricio Merikanskas	MERIK
11	April 19, 2018	Ricardo A. Hamdan	Hitachi Zosen Inova, Sales Manager
12	April 25, 2018	Interview # 4 with Dr. Elizabeth Bauch	Elizabeth Bauch, Ph.D. Senior Associated Advisor Evensen Dodge International
13	May 2, 2018	Jorge Landa	Director General Renewable Energy

ANNEX IV. TECHNICAL ASSISTANCE

The information for this Annex on Technical Assistance activities was extracted from EDII Annual Progress Reports from several years; EDII presentations provided to the evaluation team by EDII; and from documents located on the internet. Nicholas Prichard and Geraldina Villalobos Quezada prepared the annex.

Through the National Assistance Module, Evensen Dodge formally worked with the Mexican Finance Ministry (SHCP), in developing proposals to reform the Federal Law for Financial Institutions and the Federal Law for Capital Markets to allow for the creation of subnational financing vehicles in Mexico.

Subsovereign Assistance and Transaction Completion Modules were developed by Evensen Dodge to encourage state and municipal borrowers to strive to earn the independent ratings they need for market access, through Special Purpose Vehicles (SPVs) such as bond banks, pooled financing, build, operate and transfers, public private partnerships, and revolving funds were developed to foster this model.

Evensen Dodge advised and assisted the subnational authorities from the states of Zacatecas, Quintana Roo, and Hidalgo to complete the preparatory work that was necessary to implement a financing vehicle, unique in Mexico, that would respond to each state's needs.

Additionally, EDII helped:

1. Update national and subnational legal and institutional frameworks to provide the transparency and confidence investors require when participating in the emerging subnational financing market;
2. Pilot-test model transactions with subnational authorities so they could access financing from the capital markets;
3. Pilot-test financing models that were designed to develop specific economic sectors such as in education, housing, water, agriculture, and health; and
4. Enable national and subnational authorities to perfect the subnational financing models that were being developed by including new elements from other successfully proven models used in other countries.

LEGAL REFORM

EDII assisted national, state, and municipal government authorities in modifying their legal and institutional frameworks to provide the transparency and confidence investors require when participating in the emerging subnational financing market. Highlights of the services rendered on this topic include:

- Technical assistance to regional and national authorities on what to update in their legal frameworks to encourage the development of a domestic capital market and how to facilitate municipal finance.
- Assessment of current tax, duty, or fee revenues that subnational jurisdictions control and recommendations on how to increase or securitize them.
- Analysis of current tax transfers from national or federal governments to subnational jurisdictions and recommendations on how to increase these revenue flows and how to securitize them.

- Technical assistance to update legal frameworks to encourage subnational jurisdictions to pursue higher credit ratings.
- Analysis of the obstacles preventing pension funds from participating as investors in subnational financing transactions and recommendations for modifying regulations to facilitate institutional investors investing in municipal finance.
- Research on current debt market instruments and technical assistance, as necessary, to develop new financial instruments that could be used as promissory notes or bonds in regional or domestic capital markets.

MARKET ANALYSIS

EDII advised and assisted selected local authorities to complete the preparatory work that is necessary to access the capital market. These transactional advisory services included: explaining financial viability criteria, linking municipal infrastructure programs with coherent financial structures, and delineating differences between municipal projects that may have inherent revenue sources with those that do not. EDII assisted the targeted jurisdictions to reduce costs and increase financial feasibility of inter municipal project development. EDII advised on how to increase project viability by promoting greater citizen participation in local development plans and made presentations to state and local leaders on financial concepts and educational tools available to facilitate long-term, high-credit quality financing structures that enhance a project's outcome. EDII assisted municipal authorities to understand the process and prepare for entity-credit rating audits and helped entities concession-out infrastructure projects to third party vendors, as necessary and feasible.

FINANCIAL PLANNING FOR PUBLIC ENTITIES

EDII advised and structured the deals to enable the pilot jurisdictions to access capital financing. EDII's assistance focused on developing the financial plan for the infrastructure project. EDII reviewed legal, financial, economic, and other pertaining documents and information necessary to advise the entity in consolidating the financial plan. The financial plan included the conduct of the planned-issue, an analysis of funding requirements, recommendations for alternative funding, an analysis of national tax implications on the issue, a plan for marketing the financial transaction, and recommendations on the most advantageous method of sale (competitive, negotiated, or private placement). Security features, such as call provisions, credit rating, credit enhancement, use of reserves and the funding of, and interim or other short-term issues were also part of the financial plan.

SELECTING FINANCIAL MODELS

Evensen Dodge has assisted in determining which financing mechanisms and approaches to use with the previously structured SPVs, i.e., general obligation bonds; revenue bonds; assessment bonds; moral obligation bonds; lease financing; certificates of participation; securitization; refunding; restructuring; variable rate; cash flow; commercial paper; derivatives; and/or, swaps, among others. EDII believes that the potential pool of state and municipal borrowers could become much broader as potential interest savings encourage these entities to strive to earn the independent ratings they need for market access. Some potential financial models include bond banks; pooled financing; build, operate and transfers; public private partnerships; and revolving funds.

IMPLEMENTING FINANCIAL TRANSACTIONS

EDII worked with the pilot entities to implement their Financial Plans (completed in Module Three) and complete the transaction. This included: (1) developing the presale analysis to define market conditions prior to issuing debt; (2) developing legal documentation such as indenture and trustee agreements; (3) requesting project-based credit ratings; (4) hiring other service providers necessary to complete the financing processes, such as bond counsel, underwriters, bank trustees, and financial intermediaries, and coordinating them; (5) advertising and undertaking the bidding processes in case of competitive sales, or developing sale agreements in case of negotiated sales; and (6) participating in the financing completion processes. EDII worked with rating agencies to get ratings for either a municipality or project and assisted municipalities in preparing the data to achieve a better credit rating. EDII also assisted municipalities to obtain credit enhancements and analyze the use of reserves that might be required in each particular region or country. When appropriate, EDII collaborated with the World Bank and the Inter-American Development Bank.

EDII assisted in averting potential obstacles by making strategic alliances with partners that facilitated the process. For example, as needed, EDII requested new project-based credit ratings to avert a credit risk of subnational governments with poor ratings. Another example was working with development banks or USAID's Development Credit Authority to enhance local credit through partial guarantees and risk sharing with investors when no local credit enhancement provider was available.

To help develop the country's economic sectors, EDII assisted national and subnational authorities to introduce best practices and new elements from successfully proven models used in other countries to foster the development of various industries by helping create financial structures (SPVs), organizations, and/or institutions that could enable or encourage secondary market participation, thus deepening the subsovereign bond market in Mexico.

ANNEX V. TRAINING AND CAPACITY BUILDING

The information for this Annex on Training and Capacity Building activities was extracted from EDII Annual Progress Reports from several years; EDII presentations provided to the evaluation team by EDII; and documents located on the internet. Nicholas Prichard and Geraldina Villalobos Quezada prepared the annex.

Evensen Dodge provided training and capacity building to a wide range of people and institutions at all levels of government, as they introduced the new financing model and provided advisory services to subregional governments looking to implement the models. In addition to the formal workshops and classroom trainings described in this annex, EDII developed capacity within the sector through the extensive technical assistance activities, are described in detail in Annex IV.

Some of the major types of training provided are described below.

TABLE V. STAGES/TRAINING MODULES

TYPE OF MODULE	DESCRIPTION OF MODULE
Module 1: Diagnosis	The Diagnosis Module is a comprehensive analysis of the current state of the legal and regulatory framework pertaining to subnational financing.
Module 2: National Level Assistance	The National Level Assistance Module focused on assisting national government authorities in modifying their legal and institutional frameworks to provide the transparency and confidence investors require to participate in the emerging subnational financing market. The goal of the activity was to encourage greater market participation by providing technical assistance to issuers or other key market actors engaged with states and municipalities. By providing technical assistance that is tailored to the needs of individual governmental entities, the activity would create examples for similar entities that might or might not be able to adopt best practices.
Module 3: Subsovereign Level Assistance	The Subsovereign Level Assistance Module was designed to provide technical assistance to targeted subnational jurisdictions to help them implement a financing vehicle to access financing from regional and/or domestic capital markets, under better terms and conditions. The technical assistance was provided in three phases: • EDII proposed to develop models capable of mobilizing USD \$1 billion for infrastructure development purposes in three years (through 2012). • EDII proposed to develop two or three different financial models (preferably one per year) focused on different priority sectors of the economy. • For each model, EDII would implement one to two pilot transactions with an estimated amount ranging from USD \$100 million to USD \$400 million each.

TYPE OF MODULE	DESCRIPTION OF MODULE
Module 4: Subsovereign Financial Plans & Transactions	Evensen Dodge proposed to work with the pilot entities to implement their Financial Plans, completed in Module 3, and conclude the transaction.
Module 5: The Sectors-of-the-Economy Financing	The Sectors-of-the-Economy Financing Module would assist regional (in this case Central American countries), national, and subnational authorities in expanding the subnational financing market by introducing new elements from other successfully proven models used in other countries.

DOCUMENTATIONS, CONFERENCES, SEMINARS, AND WORKSHOPS

The EDII GDA Activity has produced model-like documentation of the pilot transactions to replicate the financial models in other interested jurisdictions in selected regions and/or countries.

The EDII GDA Activity has produced conferences, seminars, and workshops to explain the success cases achieved by the USAID/Mexico GDA Activity in assisting Mexican subnational entities with access to financing with increasingly better terms and conditions. EDII staff have been invited to participate as speakers in numerous municipal finance conferences in Mexico, as well as several international conferences to explain this success. Some of their international speaking engagements include: World Water Forum in Japan, the World Urban Forum in Spain, the OECD Conference in France, seminars with USAID and other federal authorities in Washington, DC, a NAFTA conference in Tucson, Arizona, a MERCOSUR event in Paraguay, the Improving Capital Flows to Africa Conference in South Africa, and the South Pacific Financing Conference Workshop in the Philippines.

LOCAL CAPACITY BUILDING PROVIDED BY GDA ACTIVITY

EDII has provided comprehensive explanations to officers in the executive and legislative branches of the federal, state, and municipal governments in Mexico; governing bodies, directors, and analysts of public corporations; private sector participants including officers and analysts of financial institutions, law firms, rating agencies, trustees, notary publics, paying agencies, developers, and investors on the following topics:

- The current state of the legal and regulatory framework pertaining to subnational financing;
- Ascertaining the opportunities and limitations for subnational governments wanting to access capital markets to finance their infrastructure needs;
- Tax policies, types of taxes levied and collected at national, regional, and local levels, and the mechanisms used by the central government to distribute funds to subnational authorities;
- The assessment of regional capital markets in addition to the state of the domestic capital market;
- Debt instruments used, who are the investors, how do pension funds and insurance companies participate, who underwrites and what is their role, and what is the status of credit insurance agencies,

credit enhancement providers, and principal legal advisors;

- Assessing the capability and interest of financial institutions and investors in municipal finance and to understand their concerns; and
- The participation and impact of regional development banks and multilateral development banks on the ability of subnational governments to access a domestic capital market.

ANNEX VI. EVENSEN DODGE LOAN TRANSACTIONS

The information in Table VII describes the loans that were transacted (approved) during the Activity period 2002-2018. The sources for the data in the loan portfolio were Evensen Dodge Activity documents reviewed by the study team; background research on the internet conducted by team members, which located presentations made by Mr. Fernando Gama, Senior Vice President, EDII. Other loan information was located by reviewing the states' official websites (i.e., Hidalgo Quintana Roo). The information is public and available on Mexico government and state databases. The evaluation team was unable to obtain access to the databases (see Annex VIII. Data Limitations).

TABLE VII. USAID/MEXICO-EVENSEN DODGE LOAN PORTFOLIO

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
State of Michoacán †	Module 3 Subsovereign Level Assistance & Module 4 Implementin g Financial Plans	2002-05	Revenue Intercept to divert a portion of federal transfers to subnational governments to an irrevocable debt service trust	Type of projects financed infrastructure for <i>Nuevo Morelia</i> , a zone established for combined private business and residential development. The state purchased the land and developed basic infrastructure	Two new structured loan transactions in the amount of \$150 Million each for a total of \$300 Million MXN	The state reports an additional USD \$300 Million in private investment was leveraged as a result of the <i>Nuevo Morelia</i> project.	The first transaction of the Activity with USAID applied a revenue intercept structure that allowed the state to have a portion of its federal transfers assigned to an irrevocable	The Public Debt Law of the State of Michoacán, last revised in 1929, was modified to align it with the new federal legal framework. Single-digit rates were achieved, while traditional financing was above 13 percent. A term	Indirectly all 113 municipalities because the project that was <i>financed</i> (<i>Nuevo Morelia</i>) established a modern business park near the state capital and helped to trigger	4.5 Million

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
				for the lots: water sewage, water treatment, public lighting, school improvements.			trust for debt service payment. States receive multiple sets of transfers, all earmarked for specific purposes. Only those linked to Budget Branch 28 (<i>Ramo 28</i>) may be applied to debt service. The revenue intercept model introduced with this transaction became the market standard and has	of 10 years was also achieved, when the standard term length was six years, equivalent to the period of administration of a state. Subsequently, work was also done on putting together a participatory budget. At the time the USAID/ Mexico- Evensen Dodge activity was focused on economic development, democracy, decentralization, and municipal autonomy. The	additional private investment and private job creation that impacted the state as a whole and economic development for the whole state.	

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							subsequently been widely used by subnational borrowers in Mexico.	results achieved were consistent with the activity objectives.		
State of Hidalgo	Module 2 National Level Assistance & Module 3 Subsovereign Level Assistance	2007	Pooled Financing through State Bond Bank	Refinanced state debt for savings and to create space for new borrowing; the state addressed transportation, communications, health, and education needs.	Bond issued for the peso equivalent of USD \$227 Million		Hidalgo bond bank was the first to execute pooled financing in Mexico. The bond bank received an AAA.mx rating (the state's stand-alone	The refinancing saved the state millions of dollars and has given it needed room for future borrowing for infrastructure. The state had many infrastructure demands to be satisfied, but	Indirectly, 84 municipalities because the state reduced its debt burden and had more liquidity to invest in infrastructure	2.5 Million

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
	& Module 4 Implementin g Financial Plans						rating was A.mx). The bond bank issued USD \$227 million (peso equivalent) in refinancing bonds on behalf of the state government on May 10th, 2007, which were oversubscribed and sold at a record rate of Mexican prime plus 14 basis points for a term of just over 12 years.	mostly transportation, communications , health, and education needs were attended. At the time the USAID/Mexico-Evensen Dodge activity was focused on economic development, democracy, decentralization, and municipal autonomy. The results achieved were consistent with the activity objectives.	e and public services.	

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
State of Hidalgo	Module 3 Subsovereign Level Assistance & Module 4 Implementin g Financial Plans	May 2009- March 2010	Bond Bank Bridge Loan	Purchase of land to develop oil refinery and the airport/ logistic center. Public infrastructure. Additional transportation, communications, health, and education needs were addressed.	New financings in the amount of USD \$23 Million (May 09), USD \$115 Million (Feb 12), USD \$5 Million (Mar 12) & USD \$81 Million (Mar 12) were executed for a total of USD \$224 Million.	Additional Federal Pari Passau funds were mobilized in the amount of USD \$81 Million.	The bond bank executed a pooled transaction on behalf of multiple municipalities. The competitive transaction was completed at a fixed rate of 7.2% which set a record as the lowest interest rate for any transaction involving municipalities. Another transaction was executed on behalf of the state	The Congress of the State of Hidalgo approved a new Law for Public-Private Partnership Program (PPP) with technical assistance from Evensen Dodge International, Inc. The first comprehensive law of its kind at the subnational level in Mexico and internationally, it incorporated definitions of and appropriate regulations for 12 PPP models, and also requires that all	60	1.5 Million

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							government and additional municipalities. The bond bank borrowed money on behalf of the state Government and its municipalities. The transaction closed at Mexican prime plus 95 basis points for a term of 15 years. Each of the four transactions featured different terms and	public works developed under this law comply with the state's environmental sustainability criteria. Some of these transactions served small and poor municipalities, including some that had never received a loan before in history. At the time the USAID/Mexico-Evensen Dodge activity was focused on		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							conditions. All were within the range of other competitive market transactions completed in the same time period.	economic development, democracy, decentralization, and municipal autonomy. The results achieved were consistent with the activity objectives.		
State of Quintana Roo	Module 3 Subsovereign Level Assistance & Module 4 Implementing Financial Plans	2007-09	Bond Bank Loan	By refinancing some old debt, the state was able to reduce debt service payments. This created additional liquidity in its annual budget and state resources were applied to health, housing, economic	Three refinancing transactions: • Two for the state government: USD \$110 Million (Feb 07) and USD \$210 Million (Jun 10). • One refinancing for the Municipality		These transactions were implemented with the bond bank. The credit ratings, terms, and interest rates achieved for the State were:	Quintana Roo created the second bond bank in Mexico, which also served as a promoter of infrastructure projects for the state and underlying municipalities. The bond bank required passage of a set	8 municipalities Benito Juarez (Cancun) benefitted directly. Indirectly, all eight municipalities benefitted because the state reduced its debt burden	1 Million

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
				development, roads, and water and sanitation infrastructure projects.	of Benito Juarez (Cancun's legal name) for USD \$54 Million (Mar 08)		• Feb 07 AA.mx 12 yrs prime (TIIE) + 30bps - Feb 07 AA.mx 10 yrs. prime (TIIE) + 30bps - May 10 AA.mx 18 yrs. prime (TIIE) + 160bps - May 10 AA.mx 15.5 yrs. prime (TIIE) + 160bps - May10 AA.mx 15 yrs. prime (TIIE) + 165bps	- of new state laws by the state congress. These included: • A new Law to create a public corporation (SPV), • Reforms to the State Law of Public Debt • Reforms to the State Law of Fees and Tariffs • Reforms to the State Law of Revenue • Decree to reform the state budget,	and had more liquidity to invest in infrastructure and public services.	

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							Jun10 AA.mx 10 yrs. prime (TIIE) + 80bps Jun10 AA.mx 16 yrs. prime (TIIE) + 80bps The credit ratings achieved for refinancing for the City of Cancun o Mar08 were: A+.mx 11 yrs. prime (TIIE) +50bps A+.mx 11 yrs. prime (TIIE) +44bps The Governor of Quintana	Decree to authorize the financing transaction. At the time the GDA activity was part of the Mission's Democracy and Governance portfolio. The results achieved were consistent with the activity objectives.		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							Roo included the EDII-USAID GDA pilot activity as a highlight in his state to the state in April 2008.			
State of Quintana Roo	Module 3 Subsovereign Level Assistance & Module 4 Implementing Financial Plans	Dec. 2008- March 2009	Bond Bank Loan	With the savings and liquidity yield by the refinancing, the state attended health, housing, economic development, roads, and water and sanitation infrastructure projects.	Three new financings: • Two for the state government: USD \$142 Million (Dec 08), and USD \$223 Million (Jan 11) • One financing for the Municipality of Ithon P. Blanco	Additional Federal Pari Passau funds were mobilized in the amount of USD \$365 Million.	The credit ratings achieved for financing transactions for the state were: Dec08 AA.mx 15 yrs. prime (TIIE) + 305bps Jun09 AA.mx 15 yrs. prime	The transaction was structured and implemented using the Quintana Roo bond bank. Loan terms and conditions set favorable benchmarks in the market. Proceeds were used for health, housing, economic	8 municipalities	1 Million

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
					for USD \$11 Million (Feb 11)		(TIIE) + 210bps Jun09 AA.mx 20 yrs. prime (TIIE) + 285bps Jun09 AA.mx 15 yrs. prime (TIIE) + 220bps Dec10 AA.mx 20 yrs. prime (TIIE) + 85bps Dec10 AA.mx 20 yrs. prime (TIIE) + 150bps Jan11 AA.mx 20 yrs. prime (TIIE) + 165bps	development, roads, and water and sanitation infrastructure projects. At the time the GDA activity was part of the Mission's Democracy and Governance portfolio. The results achieved were consistent with the activity objectives. New drinking water infrastructure benefited 77,012 inhabitants. New sewer and sanitation		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							The credit ratings achieved for refinancing transactions for Municipality of Ithon P. Blanco was AA.mx The interest benchmark +165 bps. The state water and sewer utilities corporation (CAPA) accessed financing through a pooled financing	infrastructure benefited 146,879 inhabitants		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							transaction structured by Evensen Dodge International. One of the state's priorities was to provide maintenance and to expand its water and sewer infrastructure to satisfy the growing demands of the population. CAPA, a public-private corporation, pooled the financing requirements of several small			

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							municipalities to access domestic currency in an amount equivalent to USD \$30 million, which the federal government matched with USD \$30 million. Financing was in the form of a bank loan from Citibank. The credit rating achieved was of AA.mx from Fitch Ratings and Moody's. The interest rate benchmarked prime +19bps. For water and			

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							sewer infrastructure in Mexico the standard had been a spread of +500 to +800 bps, if any financing was available at all. Term was 15 years with grace of two in principal payment. Quintana Roo pooled this financing for water and sewer infrastructure, specifically to provide maintenance and to expand its water and			

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							sewer infrastructure to satisfy the growing demands of the population. New drinking water infrastructure benefited 77,012 inhabitants. New sewer and sanitation infrastructure benefited 146,879 inhabitants.			
State of Quintana Roo	Module 3. Subsovereign Level Assistance	2007	Pooled Financing Water and Sewer	Water & Sanitation Projects	New financing in the amount of \$24 Million (Sept 07)	Additional Federal Pari Passau funds were mobilized	The <i>Comision de Agua Potable y Acantarrillado</i> for the State of Quintana Roo (CAPA) is	This transaction was recognized at World Water Week on 2008 in Stockholm, Sweden, as one	8 municipalities	223,891

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
	& Module 4 Implementin g Financial Plans		Infrastructur e			in the amount of USD \$24 Million.	the state's water and sewer utility. CAPA accessed financing through a pooled financing transaction structured by Evensen Dodge International. One of the state's priorities was to provide maintenance and to expand its water and sewer infrastructure to satisfy the growing demands of the	of the best financial transactions in the water & sanitation sectors done around the world in 2007. Quintana Roo and the Director General of the bond bank and the Director General of the Water Utilities of the state, accompanied by USAID Officials and Evensen Dodge staff, attended the event where the Quintana Roo Finance Secretary gave a presentation		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							population. CAPA, a public-private corporation, pooled the financing requirements of several small municipalities to access the peso equivalent of USD \$24 million. This allowed the state to receive the same amount in federal matching funds, for a total of USD \$48 million for infrastructure.	about the transaction. CAPA required these funds for to meet the demands of the state's growing population, financing for water and sewer infrastructure. New drinking water infrastructure benefitted 77,012 inhabitants. New sewer and sanitation infrastructure benefitted 146,879 inhabitants.		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							Financing was in the form of a bank loan from Citibank. The credit rating achieved was of AA.mx from Fitch ratings and Moody's. The interest rate benchmarked prime +19bps. For water and sewer infrastructure in Mexico the standard had been a spread of +500 to +800bps, if any financing was available at all. Term was 15 years with grace of two	During this period, the GDA activity was part of USAID's Democracy and Governance portfolio. The results achieved were consistent with the activity objectives.		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							in principal payment.			
State of Veracruz	Module 4 Implementin g Financial Plans	2016-17	Short-term financing (transfer anticipation loan for emergency cash flow needs)	Payroll for police, doctors, and other governmental employees	Two new financial transactions, in the amount of USD \$240 Million (Dec 2016), and \$240 Million (Dec 2017), for a total of USD \$480 million.		When the new administration took office on December 1, 2016, they discovered the extent of the state's financial emergency. Records were destroyed, and the state did not have the resources needed to make payroll for that month. EDII helped the state negotiate emergency bridge financing in	Short-term financing to pay for current account expenditures. These loans are payback with national tax transfers that arrive in the state treasure every month.	All of the state's 212 municipalities because, if the state could not continue to operate and provide services, the entire population would have been adversely affected.	7.6 Million

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							anticipation of its refinancing. The rates of those short-term financings were around benchmarked +109bps.			
State of Veracruz	Module 2 National Level Assistance & Module 3 Subsovereign Level Assistance &	2017-18	"Mexico Bond Bank <i>fideicomiso acreditado</i> " structure	With the savings and liquidity yield by the refinancing, the state attended to health, housing, economic development, roads, and water and sanitation infrastructure projects.	The state refinanced most of its outstanding debt for a total of USD \$2.1 billion (peso equivalent)		The refinancing comprised separate loans from six financial institutions. The state used the proceeds to liquidate 20 prior financings, including five bond issues to payout 20	EDII created a mechanism, the <i>fideicomiso acreditado</i> , that incorporated many of the features of a bond bank in concert with the Government of Mexico. This mechanism goes beyond the irrevocable	Indirectly 212 municipalities because the State reduced its debt burden and had more liquidity to invest in infrastructure and public services.	7.6 Million

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
	Module 4 Implementin g Financial Plans						financings, including five debt issuances. The refinancing has reduced the state's annual debt service payments from USD \$356 to USD \$248 Million per year. This provides significant liquidity for the state. Additionally, the state realized one-time revenues of some USD \$325 Million when old debt reserve funds were released.	revenue intercept trust that was initially developed and which has been applied to the bond banks in Hidalgo and Quintana Roo. The Accredited Trust (<i>fideicomiso acreditado</i>) stands in front of the borrowing entity and borrows on its behalf (instead of passively receiving the intercepted transfers). The new trust required multiple adjustments to		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							These one-time funds are being applied in the 2018 budget for crime and violence prevention projects. The state will spend approximately USD \$55 Million (peso equivalent) on public safety cameras to be placed throughout the state, and the remainder would be applied to public works projects in order to generate	federal laws and regulations, which were completed with support from <i>Hacienda</i> . The Accredited Trust was introduced to all Mexican banks that lend to subnational governments at a meeting called by the Secretary of <i>Hacienda</i> . Mexico's Securities and Exchange Commission (CNBV) reviewed the structure and published rules and conditions for its application. The		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							additional employment. For each transaction, terms, and conditions please refer to table “Veracruz Refinancing Program”	structure was applied for all of the loans that comprised the Veracruz refinancing. Multiple law firms have reviewed the structure and presented formal opinions. By using this structure (<i>fideicomiso acreditado</i>), the Veracruz refinancing received credit ratings of AA.mx. The state’s stand-alone rating at that time was BB.mx below		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
								investment grade. This mechanism is now legally available to all states and municipalities in Mexico. It was pilot-tested with the Veracruz refinancing.		
Guanajuato Puerto Interior	Module 3 Subsovereign Assistance	2010	Domestic Credit Mobilization			USD \$150 Million	With the GDA Activity's assistance, the Internal Port of Guanajuato was developing a tailored financial vehicle to mobilize the needed capital	No financing transaction was completed. However, as a result of EDII's efforts, the State of Guanajuato decided to make a direct investment in the <i>Puerto Interior</i> and the	8 municipalities (indirectly)	2 Million

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							for port infrastructure and to trigger an initial public offer of the Port's stock in the Mexican securities market.	entity no longer required additional financing. The USD \$150 Million was used for infrastructure upgrades at the Port (e.g., railway, highway, and interior customs facilities). The Port estimates that an additional USD \$150 Million in private investments have been made in the state, generating additional employment.		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
Federal Congress	Module 2 National Level	2012	Reporting		N/A		Produced report on how to modernize the development banking system of Mexico based on experiences from other countries such as Turkey with the Istanbul Financial Center Program, Brazil, and Chile. Extensive traveling to these and other countries was required to fulfill this	Report produced by EDII		

PRIMARY PARTNER	MODULE/STAGE	YEARS	FINANCIAL MODEL	INFRASTRUCTURE/ PRODUCTIVE PROJECT TYPE	FINANCING AMOUNT USD*	CAPITAL MOBILIZED USD*	BRIEF DESCRIPTION	RESULTS	BENEFICIARY AMOUNT (MUN)	BENEFICIARY AMOUNT (RESIDENTS)
							commitment. Studied how Brazil modernized their State Oil Monopoly (PetroBras) to understand how the case study could be applied to Mexico's PEMEX.			

Sources - Evensen Dodge Activity Documents (Mexico DocReview 12.8, Excel Document), Pooled Financing Presentation-Evensen Dodge International, 2014.

†Indicates crime prevention projects

*EDII and IPs states that they have provided required matching funds —leveraged for the activity from September 2005 – September 2015— in an amount of \$11,716,567.00, as has been periodically reported to USAID/Mexico. The team was not able to confirm this total, due to incomplete activity records available from the IP.

*USAID/Mexico provided \$11,698,798.00 for this activity from September 2005 – September 2015. The team was not able to confirm this total, due to incomplete activity records available from the IP.

‡ Amount computed by adding the USD amounts together from entire table. If amount was originally provided in Mexican Pesos (MXN), an average exchange rate was taken from an average of exchange rates in all years during life of Activity to ensure that the USD figures was as precise as possible. USD and MXN figures in each row are NOT to be added together, but to be seen as an equal amount in respective currencies.

‡Additional Projects being planned were often described in reports, but evidence to confirm that the transactions were completed was not found. The planned-but-not-confirmed-as-completed-projects were not included in this table. Sources for the information were EDII Quarterly and Annual Reports submitted to USAID.

TABLE VIII: ACTIVITY LINKAGES WITH CLEAN ENERGY PROJECT GOALS

TYPE OF LINKAGE	NUMBER OF PROJECTS
Directly linked with clean energy	7
Indirectly linked with clean energy as a project goal	26

ANNEX VII. FINANCIAL TRANSACTIONS IN THE PIPELINE

After numerous requests by the Palladium evaluation team for a list of new or upcoming financial transactions in the pipeline (2017-present), the Evensen Dodge staff provided the following information in Table VIII.

TABLE VIII: LIST OF FINANCIAL TRANSACTIONS IN THE PIPELINE* (AS OF APRIL 24, 2018) FOR THE USAID/MEXICO-EDII GDA ACTIVITY

PRIMARY PARTNER	YEAR(S)	FINANCING AMOUNT USD	BRIEF DESCRIPTION	ESTIMATED CLOSING
Iztapalapa Delegation (Mexico City)	2018	USD \$100 Million	We expect the government will publish its request for quotations during the first half of May. This process will take between 60 and 90 days, and the financing transaction would then require an additional 60 to 90 days. EDII will assess the use of the <i>Fideicomiso Acreditado</i> (Accredited Trust) structure for this transaction.	November 2018
State of Coahuila Solar Park	2018	USD \$105 Million	The state expects to receive authorization from CRE in May. Once authorized, the transaction would require between 60 and 90 days to complete. EDII will assess the use of the <i>Fideicomiso Acreditado</i> (Accredited Trust) structure for this transaction.	August 2018
State of Hidalgo (waste-to-energy)	2018	USD \$150 Million	The transaction process has initiated and is expected to conclude between 30 and 90 days from now. We may seek a bridge loan to support the start of the project construction; this would be repaid from long-term debt proceeds.	July 2018

PRIMARY PARTNER	YEAR(S)	FINANCING AMOUNT USD	BRIEF DESCRIPTION	ESTIMATED CLOSING
			EDII will assess the use of the <i>Fideicomiso Acreditado</i> (Accredited Trust) structure for this transaction.	
State of Hidalgo Industrial Parks Project	2018-2019	USD \$75 Million	On April 2, 2018, the Hidalgo state congress approved its updated PPP law, the <i>Ley de Alianzas Productivas de Inversión para el Estado de Hidalgo</i>. This law allows this project to go forward. The state congress is reviewing the additional formal authorizations that the project requires. EDII will assess the use of the <i>Fideicomiso Acreditado</i> (Accredited Trust) structure for these transaction.	Transaction period: May 1, 2018-March 31, 2019 Multiple transactions are expected.
State of Hidalgo Public Lighting Program	2018-2019	USD \$50 Million	On April 2, 2018, the Hidalgo state congress approved its updated PPP law, the <i>Ley de Alianzas Productivas de Inversión para el Estado de Hidalgo</i>. This law allows this project to go forward. The state congress is reviewing the additional formal authorizations that the project requires. EDII will assess the use of the <i>Fideicomiso Acreditado</i> (Accredited Trust) structure for these transactions.	Transaction period: May 1, 2018-March 31, 2019 Multiple transactions are expected.
State of Coahuila Refinancing	2018	USD \$2 Billion, of which approximately USD \$300 Million will conform to the objectives of the GDA Activity (energy and crime prevention)	The refinancing will be completed in the second half of calendar year 2018 and, like Veracruz, will likely comprise multiple transactions. EDII has begun its preparatory work; however, the governor decided to postpone the transaction until after the elections in July. EDII will assess the use of the <i>Fideicomiso Acreditado</i> (Accredited Trust) structure for these transactions.	July-November 2018

PRIMARY PARTNER	YEAR(S)	FINANCING AMOUNT USD	BRIEF DESCRIPTION	ESTIMATED CLOSING
State of Durango Solar Park and Public Lighting	2018-2019	USD \$70 Million	Solar park with a generation capacity of 90 Mwh; 20 Mwh have already been built. The financing would be supporting the construction of the remaining 70 Mwh. EDII will assess the use of the <i>Fideicomiso Acreditado</i> (Accredited Trust) structure for these transactions.	Transaction period: May 1, 2018-March 31, 2019 Multiple transactions are expected.
Veracruz (<i>Iluminación municipios</i>)	2018-2019	USD \$100 Million	The state's energy agency has been established and has submitted a draft decree request to the state congress in order to authorize the public lighting program. EDII will assess the use of the <i>Fideicomiso Acreditado</i> (Accredited Trust) structure for these transactions.	Transaction period: May 1, 2018-March 31, 2019 Multiple transactions are expected.

* Completing the above transactions depends on political will and market conditions. Evensen Dodge International is working to bring them to successful closings in the shortest time possible.

ANNEX VIII. DATA LIMITATIONS

This section discusses several limitations to the data collected and reviewed for the evaluation.

LIMITED SOURCES OF INFORMATION

The evaluation team found that lack of access to data about the GDA was the key limitation and major constraint to this evaluation. Typically, an evaluation relies on multiple sources of information to provide as complete a picture as possible. Information sources identified for this evaluation fell into four main categories: policy makers; project staff; program participants, i.e., regional and municipal government officials who participated in training, technical assistance, and financial transactions on behalf of their state or municipality; and community members (Annex I. Evaluation Matrix). A fifth source was the project documentation.

This performance evaluation was carried out from September 2017 through September 2018 after the Evensen Dodge activities had, for the most part, ended. As a result, many of the individuals who were involved over the life of the activity were not easily identified or located, nor did the Scope of Work and funding accommodate a full-scale search. Consequently, interviews were limited to a convenience sample of those participants from a short list of individuals provided by EDII and USAID. The evaluation team was able to interview these individuals, and several others who voluntarily agreed to participate in interviews, but the team was unable to organize focus groups.

Many documents covering the full 16 years were no longer available. The team requested quarterly and annual reports from the beginning of the activity, as well as copies of the multiple award agreements between USAID and Evensen Dodge, and occasional white papers. Neither institution had a complete set of the agreements and reports, so despite good faith efforts on all parts, the team did not have the complete set of records.

The data for the case studies was seriously limited by the inability of the team to gain access to any beneficiaries of the projects and by the very limited access to government officials in each state who could speak about the process of using the bank bond to finance municipal or regional projects. In each state, EDII recommended one official and, given the time and financial limitations of the evaluation, the team was not able to travel to the states and locate additional officials for the interviews.

On numerous occasions the team requested that EDII provide more specific information regarding EDII trainings and workshops conducted with government officials and other public and private organizations. While EDII provided a description of the different Training Modules (Annex IV) that were going to be implemented, there is no record of trainings that were conducted, nor a list of training participants. Therefore, a limited number of interviews were conducted with program participants. The team was unable to organize focus groups with participants in the trainings and workshops as a result of lack of data.

Finally, the activity was funded through a Cooperative Agreements and GDAs which did not require detailed reporting of outcomes and results. Over the life of the Activity, USAID's M&E requirements became more stringent and the last agreement (2015-2018) included specific indicators on which the IP was to report. However, no data were reported on these indicators during this period. In recognition of this weakness, the evaluation team offered a recommendation that if USAID is going forward with similar projects that the overall reporting be enhanced, and the results achieved be more completely documented.

NO ACCESS TO STATE WEBSITES FOR DETAILED INFORMATION ON EDII LOAN

TRANSACTIONS

The evaluation team was not able to verify that the information on completed financial transactions reported by Evensen Dodge staff (Table VII) accurately reflected the loans that were transacted (approved) during the Activity period, as the financial records documenting the number and amount of transactions were not made available to the team, despite multiple requests.

The sources on the loan portfolio were limited to Evensen Dodge's project documents, a 2014 PowerPoint presentation by EDII staff, and revisions by Evensen Dodge to the table compiled by the team from project documents. Evensen Dodge staff referenced the states' official websites (Hidalgo and Quintana Roo) as loan information that was public and available on Mexican government and state databases. However, the evaluation team found this information was not readily accessible on the government websites. More complete information on the transactions would have improved the ability of the USAID evaluation team staff and stakeholders to report on project success.

Considering that the project was in its final stage, access to information and documents on loan transactions that were proposed or completed as supporting evidence or actual results of their project would have facilitated the evaluation team's work. At that stage, it was important for the Palladium team to highlight the results that this project achieved or initiated.

LIMITED ACCESS TO WORK PLANS OR MEMORANDA OF UNDERSTANDING (MOUS) FOR RELATIONSHIPS WITH GOVERNMENT OFFICIALS OR PRIVATE ORGANIZATIONS

Both Memoranda of Understanding (MOUs) and contracts are necessary to provide a framework for partner relationships, as the MOU establishes the conditions for cooperation between partners at the conceptual and strategic level. Under this evaluation study, the Palladium team was not able to review and/or was not provided with copies of such Work Plans or MOUs by Evensen Dodge staff, including more specific details on the proposed or completed financial transactions by EDII and collaborating organizations (e.g., MERIK, Hitachi Zosen, Universidad Panamericana).

The data sources used in the evaluation and the main limitations are summarized below (Table IX).

TABLE IX. DATA SOURCES AND EXISTING DATA SOURCE LIMITATION

DATA SOURCE	DATA SOURCE LIMITATION
Desk Review	• Evensen Dodge Activity documents and key informant interviews were the primary source of information. • The EDII Quarterly and Annual reports and state or municipal reports provided limited evidence to support the actual outcomes achieved versus indicators. • The Activity documents were the primary source for compiling the list of completed transactions, but they were incomplete. The reports did not

DATA SOURCE	DATA SOURCE LIMITATION
	clearly indicate which transactions were begun but not completed, and which of those resulted in a project. The team had no access to the financial records of the Activity to verify the value and location of the completed transactions.
Interviews with USAID Project Managers, EDII Project Managers and staff, and Implementing Partners	• Conducted interviews with Evensen Dodge project managers and state government officials (former Secretaries of Finance) from Hidalgo, Michoacán, and Quintana Roo to collect detailed information on the activities implemented for the Evensen Dodge Activity.
Interviews with project managers and project beneficiaries from selected pilot entities including Hidalgo, Michoacán, and Quintana Roo	• Conducted interviews with three key informants about the EDII work in Hidalgo, Michoacán, and Quintana Roo. • Prepared a survey to send to individuals who had participated in the projects in Hidalgo, Michoacán, and Quintana Roo. The survey was not deployed due to sensitivities around the timing, i.e. the presidential elections. The goal was to solicit feedback from a wider diversity of actors on what has been achieved or developed in this space over the last 15 years, based on the belief that increased access to financial markets for local governments had an impact on a wide set of economic and political actors. Survey participants were Mexican Ministry of Finance (SHCP) staff in charge of federal participation, other States' Secretaries of Finance, and financial services providers. • The restricted time and budget for the evaluation limited the principal investigators from conducting site visits in communities that have benefited from EDII activities.

ANNEX IX. STATEMENT OF DIFFERENCES: EVENSEN DODGE'S RESPONSE TO DRAFT EVALUATION



September 25, 2018

Palladium Group

**RE. Observations and comments to draft evaluation report
prepared by the Palladium Group on the Global Development Alliance (GDA) between
USAID/Mexico and Evensen Dodge International (EDII)**

Dear Sirs:

Evensen Dodge International Inc. (EDII) has reviewed the draft evaluation report prepared by the Palladium Group. We welcome the evaluation of the Global Development Alliance (GDA) between USAID/Mexico and EDII because we stand behind our work in Mexico and elsewhere. As noted in the draft, EDII supported the evaluation process by providing documents, including many that had been culled from USAID files, and our staff participated in multiple interviews with the evaluation team. Nevertheless, we have serious concerns about the adequacy and accuracy of the draft evaluation report, and we request that you address these concerns in the final evaluation report.

Our first concern is that the evaluation report does not adequately explain the nature of the relationship between USAID/Mexico and EDII in the GDA program. The GDA was a partnership between USAID/Mexico and EDII. It was not a contractual relationship in which USAID hired EDII to deliver specific outputs or outcomes. USAID was not EDII's client; our clients are the Mexican public entities to which we provide financial advisory services.

USAID/Mexico and EDII shared a common objective of increasing private investment in essential infrastructure by helping a range of public entities to improve their access to financing from Mexico's capital market. However, USAID and EDII also had distinct institutional interests while pursuing their common objective. USAID sought to increase financial transparency in local governments, support economic development of Mexican border states, reduce crime and violence, and reduce carbon emissions through energy efficient and/or clean energy infrastructure projects

EDII sought to establish a strong reputation as an ethical and effective financial advisor in a new market, and grow its business in Mexico into a self-sustaining, profitable, and competitive operation. The beauty of the GDA partnership was that the pursuit of these distinct interests actually served to advance the common objective we shared.

Our second concern is that the evaluation report seems to lose sight of the overarching objective

consistently pursued through the GDA partnership over its entire history. USAID and EDII collaborated over 16 years to introduce structural reforms to the Mexican capital market and demonstrate financial mechanisms that can be combined to enable subnational governments and other public entities to mobilize long-term capital for their infrastructure projects. USAID made use of the insights developed by EDII during transaction structuring to inform and advance its policy-level dialogue with the Mexican government. EDII made use of its relationship with USAID to guarantee that our firm's actions were transparent and accountable as well as to encourage Mexican public entities and investors to participate in innovative transactions that demonstrated the effectiveness of financing mechanisms developed by EDII for the Mexican market.

The evaluation report fails to recognize that the two principal constraints that hindered the financing of local development projects by the Mexican capital market were: 1) the lack of state and municipal government creditworthiness and 2) the smaller scale of most individual local infrastructure projects. The USAID-EDII partnership introduced legislative and regulatory reforms that enabled the use of innovative structures and mechanisms that addressed these barriers. All of these financing structures have been employed by multiple public entities, even without EDII advisory services, and therefore represent a robust and replicable response to the two principal constraints that previously hindered the financing of local development projects. In fact, despite the recent international financial crisis, Mexican subnational debt expanded from USD \$ 11.1 Billion outstanding in 2002, to USD \$ 27.2 Billion outstanding as of June 2018, of which an estimated \$24.5 Billion is secured using the Master Trust (revenue intercept of *participaciones*) mechanism introduced by EDII. We also note that the report does not cite any of the important third-party analyses of these mechanisms conducted by credit rating agencies and law firms specializing in financial transactions. This is discussed in more detailed in the document attached to this letter.

In addition to these two broad concerns with the evaluation report, EDII has a substantial number of specific problems with the report that are presented in our attached document entitled: *“EDII Response to the Draft Report: USAID/Mexico Municipal Development Through Infrastructure Financing Activity: A Performance Evaluation”*. These problems are organized in three categories:

1. Positive information about the accomplishments of the USAID-EDII GDA partnership that are inadequately presented and evaluated;
2. Important foundational information that was overlooked and never presented nor evaluated; and
3. Incorrect or misstated information that affected the evaluation.

The EDII response document points out each problem, explains why it needs to be corrected, and in some instances suggests an approach to correction.

We are especially concerned about the report's incorrect statement that *“EDII's uneven performance in this sector [waste-to-energy] has generated a reputational cost (a poor reputation) for them and for USAID within the Mexican waste treatment industry.”* The source of this misinformation appears to be one person who unsuccessfully attempted to extort money from EDII by threatening to give evaluators a bad report on our (terminated) work with him and his project. Additional evaluator interviews with more waste-to-energy project sponsors will correct this misconception and should be undertaken before report finalization.

EDII presents these concerns and problems in the spirit of helping the Palladium Group to prepare a final version of the evaluation report that better reflects the true performance of the USAID/Mexico

– EDII GDA. We expect to see these concerns and problems resolved in the final report, and we stand ready to answer any questions you may have about the content of this letter and our detailed response document attached herewith.

Sincerely,

Fernando Gama

Senior Vice President

cc.

Donald McCubbin, Ph.D., Director Office of Sustainable Development | Mission Disaster Relief Officer | USAID/Mexico

Simone Lawaetz, Bureau for Economic Growth, Education and Environment. | USAID



Janet E. Kerley
Technical Director, Measurement and Learning
The Palladium Group

Via e-mail

February 19, 2019

Dear Janet:

Thank you for this opportunity to review the revised draft of the evaluation report, dated November 15, 2018. You shared this final draft with us on January 18, 2019.

We note that this second draft incorporates language taken directly from our previous response, dated September 25, 2018, which is an attachment to the draft. Those September 2018 comments contain a reference to an individual; we have redacted our earlier comments to remove the name of that person. We attach the redacted version of the comments here and request that this version be included as an annex to the final report. (Attachment 1).

EDII Objects to the Conclusions of November 15 2018 Draft Evaluation Report Related to Our Firm and Our Work with USAID in Mexico

EDII cooperated with the evaluation team and provided significant input through interviews and documents. We provided detailed comments about an earlier draft report in a document dated September 25, 2018. We note that this second draft does not correct or address all the errors that were cited in that document.

EDII strongly objects to negative statements about our firm and our work that are presented in the draft evaluation report. These are based on fundamental misunderstandings of the objectives of USAID's GDA partnership with USAID.

EDII worked towards the objectives of the GDA Agreement throughout the agreement period. The evaluation report nonetheless alleges that we did not do this. These allegations are baseless for two reasons:

1) During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV). The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

2) EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

We attach a list of our objections to specific statements made in the draft evaluation report dated November 15, 2018. (Attachment 2).

Summary of EDII-USAID GDA Partnership Achievements:

EDII's work to promote broader subnational government engagement with the Mexican capital market supported several of USAID's strategic and development objectives, as reflected in the series of Agreements documented in the draft evaluation report. In Mexico, the decision to go forward with any financial transactions, for any purpose, is made by the government borrower.

Over the course of its collaboration with USAID, EDII introduced international best practices in financial and debt planning and promoted the competitive selection of service providers. EDII shared multiple models of financing for subnational governments that have been broadly used in the U.S. capital market. These are complemented by models for public private partnerships, ranging from 100% public to 100% private ownership. EDII provided targeted training for public officials and also coordinated with IPADE and INDETEC.

EDII adapted certain models and tools specifically to Mexico's capital market and to the laws and regulations that frame it. As in the U.S., laws and regulations may shift over time.

These tools were introduced in Mexico through concrete financial transactions that demonstrated how subnational borrowers could address investor concerns about credit quality and transparency. These included the Master Trust, a revenue-intercept mechanism that allows subnational entities to set aside the portion of federal transfers that will be applied to debt service in a transparent trust. The revenue intercept trust is irrevocable and remains in place for the live of the borrowing. According to the National Registry of Public Debt, this mechanism is used in the majority of subnational debt transactions: in mid-2018 they reported over 1,400 cases where this structure had been used. It is now a standard feature for subnational transactions in the Mexican capital market.

EDII helped introduce state-level bond bank SPVs in Hidalgo in 2006 and in Quintana Roo in 2007. These two states have utilized these SPVs for their own transactions, and for transactions involving underlying agencies and municipalities. Both completed transactions during the global financial crisis.

The third significant innovation is the Accredited Trust, an SPV functions like a bond bank for states and municipalities and which is available to all subnational entities nationwide. This SPV was introduced through the Veracruz debt restructuring that was initiated in November 2017 and completed in February 2018, within the period of the most recent GDA Agreement

with USAID.

Over the course of its partnership with USAID EDII assisted subnational government entities. Some sought to correct the poor debt practices of prior administrations, including the criminal manipulation of public debt. The technical assistance delivered under the GDA partnership helped subnational government clients obtain financing, and in some cases, resolve debt problems and restore sound financial management. None of the transactions that resulted from the work by EDII have had any type of negative outcomes.

Access to financing cuts across policy sectors at all levels of government. EDII assisted with financings related to multiple sectors in Mexico, including water and wastewater, urban development, public lighting, and industrial development. The transactions totaled over \$4 billion U.S. dollar equivalent. At the time the capital markets project was initiated, the subnational portion of the capital market comprised a total volume of just over \$11 billion. By introducing best practices and adapting successful financing models and mechanisms to Mexico, the USAID-EDII partnership helped the subnational portion of the market expand to over \$24 billion.

USAID/Mexico has been recognized as the Mission that has leveraged the largest levels private sector resources as a result of this partnership.

Conclusion

EDII values its partnership with USAID/Mexico. EDII is always willing to share information about our work with USAID to expand subnational government access to capital market financing.

Sincerely,

Fernando Gama

Senior Vice President

Evensen Dodge International, Inc.

cc:

Donald McCubbin, Ph.D., Director Office of Sustainable Development | Mission Disaster Relief Officer | USAID/Mexico

Simone Lawaetz, Bureau for Economic Growth, Education and Environment. | USAID

Attachments:

- 1) EDII September 25, 2018 Comments on Draft Evaluation Report, redacted
- 2) List of EDII objections to statements made in the Draft Evaluation Report dated November 15, 2018.

ATTACHMENT I: SEPTEMBER 25, 2018

EDII Response to the Draft Report: USAID/Mexico Municipal Development Through Infrastructure Financing Activity: A Performance Evaluation

General Comment on Methodology:

The draft report reflects the evaluator's lack of familiarity with capital markets in general, and with Mexico's domestic capital market specifically. The evaluators note that USAID management would have benefitted from having an officer familiar with finance issues—the evaluation would have benefitted from having one or more team members with this similar knowledge.

EDII is happy to provide additional information to the evaluation team; whether in the form of additional interviews or new documents. We could help the team obtain information that it is missing about specific transactions.

The case studies are dense and offer interesting information that needs to be carried into the main body of the report. But the studies need to be reviewed for English and for accuracy. For example, on p. 78 the authors attempt to present important information relative to the impact of the revenue intercept mechanism on the market, but mistakenly state that Michoacan has borrowed tens of trillions of dollars.

The report interviewed only two government officials, apparently from SENER. It would be helpful to the reader if these individuals were identified by title.

EDII believes the report would benefit from engagement with additional informants who are knowledgeable about Mexico's capital market. The team interviewed three former state officials who worked directly with EDII; we would recommend that the team interview government regulators and other market stakeholders, including legal experts and credit rating agencies. In addition, EDII believes that credit reports and legal opinions published for specific transactions would help to inform the evaluation overall.

We have an issue with one individual who was interviewed; we believe that he is the source of negative comments about our work. This individual demanded payment from EDII in order to provide a positive evaluation. We refused. Accordingly, we believe that the evaluation team should not rely on any information that he provided.

Section I. Statements that are essentially correct but need to be highlighted or which need additional explanation:

1) The evaluation report should more clearly set out and explain the key achievements of the GDA Program.

At various points in the draft report the evaluation team refers to innovations introduced to Mexico by EDII in order to address barriers to subnational governments accessing the capital market. These include the Master Trust (revenue intercept) mechanism, and the introduction of state bond banks.

For example, the draft report cites the revenue intercept/trust structure (*fideicomiso maestro*) that EDII introduced with Michoacan's 2002 transaction most completely on p. 78 of the 83- page document.

The report presents the most recent innovation, the Accredited Trust structure, incorrectly (it is not a trust fund) on p. 22 and elsewhere. The Accredited Trust is an advanced iteration of the Master Trust that has now been reviewed and tested by regulators, investors, ratings agencies, and bond counsel, and which may now be used by all Mexican states and municipalities seeking capital market transactions, regardless of the presence or absence of a state level bond bank.

All three types of innovations introduced by the GDA Program represent structures/mechanisms that enhance the credit quality of debt transactions to the level required by private investors. EDII has noted specific sections of the draft report where the authors misstate or misrepresent the characteristics of these innovations.

In addition, EDII has consistently promoted the establishment of a legal foundation for multiple types of public-private partnerships (PPPs). Initial national and state laws were vague or only addressed one or two forms of PPPs; EDII conducted an international study to determine how many types of PPPs were being used successfully, and for which types of projects. Accordingly, EDII has encouraged its subnational clients to adopt or modify comprehensive PPP laws that enable governments to enter into appropriate contractual arrangements with private firms, and to ensure that the governments have a basis and means for unwinding contracts that do not meet mutually agreed upon performance requirements. This work is especially important in light of the effort to develop new energy projects under the terms of the most recent GDA Agreement.

2) On p. 12 the authors write in reference to the initial 2002 Cooperative Agreement:

"The partnership's goals were clear for EDII's business case and supported USAID's goals, as improving local governments' access to financial markets undoubtedly could enhance the development opportunities in Mexico, as financial constraints frequently jeopardize development opportunities."

EDII presented an unsolicited proposal to USAID to address gaps in Mexico capital market in order to expand access for subnational governments. This was seen by USAID as fitting with the Democracy Strategic Objective (S.O.) and its underlying intermediate result "good governance."

Access to finance clearly enhances government capacity to build infrastructure, but access to finance also rewards improved financial planning and management by governments, and transparency and accountability overall. USAID agreed that accessing the capital market could offer an incentive to states and municipalities to strengthen financial transparency and accountability to citizens.

We suggest that you contact Jene Thomas, current USAID Mission Director in Haiti, who headed USAID/Mexico's democracy office at that time.

3) On p. 14 "However, as with any other transition with political dimensions, many uncertainties would arise along the way and the USAID/EDII alliance had to be flexible to deal with the

changing contexts. EDII had to contract different services to complement their own expertise, to match the new windows of opportunity opening at each stage. “

This is correct. This project required EDII to work with dozens of Mexican private firms. EDII has worked with multiple Mexican firms engaged in banking and finance, and also with firms seeking to implement energy-related projects. EDII promoted the competitive selection of service providers when preparing transactions—we supported government officials making decisions, but never made the decisions ourselves. For this reason firms have come to recognize that our interests are to work on behalf of a client, never in favor or against any other market stakeholders. We saw some individuals move from government to the private sector and back to government over the course of our partnership with USAID. We believe that any entity working on capital market issues maintain high ethical and professional standards. This is a feature that should be taken into account when discussing if the activity could be replicable in other countries.

4) On p. 20 the report quotes a USAID official that this program was “quite experimental.” EDII agrees and believes that this should be highlighted in the evaluation. The EDII-USAID partnership to expand capital market access for subnational governments was unprecedented.

5) On p. 26 the authors write, “In this regard, EDII’s work in the financial sector has been praised as highly professional and effective.”

EDII would like to see this observation expanded a bit and highlighted earlier in the report.

6) On p. 32 the authors write:

USAID is not the U.S. Treasury. USAID is not a partner with any country’s finance ministry. Therefore, there is a limited niche for what USAID can offer. The Mexican experience can show where the niche is.

This is an important statement and should be highlighted in the final evaluation. EDII believes that precisely because USAID does not partner with national finance ministries, it is uniquely positioned to offer important technical assistance to potential borrowers to help them meet the conditions required for accessing capital market finance with or without applying a guarantee mechanism that uses sovereign resources of the United States (DCA) or other countries.

Section II. Sections or General Information Missing from the Evaluation Report

1) International Best Practices in Borrowing: Transparency and Accountability to Lenders, Regulators, and Citizens

The report should discuss the international best practices that EDII has introduced in its work throughout its partnership with USAID.

This GDA program successfully mobilized over \$5 Billion in 16 years. In 2014 USAID/Mexico received a USAID/Washington award as the Mission that leveraged the most money worldwide.

No government anywhere has sufficient current revenues to build all desired and important basic infrastructure. Accessing private capital under appropriate market conditions, which should include full financial and legal disclosures, offers an important means to build infrastructure of all types. EDII's parent company, Evensen Dodge, an independent financial advisory firm with decades of experience working with U.S. states and municipalities, believed that Mexico presented a possible business opportunity following the implementation of NAFTA and the resolution of its 1994 banking crisis. But first the market needed to develop to a point that would increase the frequency and volume of activity so that a broader group of financial service providers could have sustainable businesses.

EDII performed an initial diagnosis of the Mexican capital market once the federal government explicitly severed the implied moral guarantee for states and municipalities in the late 1990s. Banking regulations tied the credit quality of subnational loans to reserve requirements. Subnational governments had to obtain two credit ratings. Some states did issue bonds, but advisors and other service providers charged exorbitant fees, at time 10% of proceeds, effectively erasing any interest rate savings.

EDII recognizes the importance of government oversight and regulation but also believes that investors play an important role in recognizing and sometimes rewarding entities that consistently display best practices in financial management and debt planning.

The Program promoted these best practices, and in some cases, most recently the State of Veracruz, credit rating agencies acknowledged improvements and raised the entity's credit rating. We can provide reports published in July and August that reflects the state's stand-alone credit upgrades.

EDII also promoted the competitive selection of financial service providers for debt transactions, demonstrating over and over that costs could be contained to between 1.5% and 2%, in line with the 1% that is typical in the much older and larger U.S. municipal market. EDII also promoted competition among potential investors to ensure the lowest cost debt service for subnational government clients.

2) Barriers to Greater Subnational Government Participation in Mexico's Capital Market

Mexico's stock market was established in 1933. Private companies and the national government have been able to obtain domestic and international financing for decades. However, subnational government participation in Mexico's domestic capital market is a fairly recent phenomenon. Early in its work EDII identified unofficial but critical barriers to subnational government access to the capital market.

Although Mexico's fiscal policy reforms of the 1990s made it possible for states and municipalities to borrow based on their own credit quality, borrowers can only be successful if they find lenders. Mexican investors are wary of issues such as debt repudiation and financial mismanagement, and as a consequence most will only consider participating in transactions that are rated AA.Mx or higher.

Another barrier is the size of the transaction. As in the U.S., Mexican investors undertake their own evaluations of credit quality and do not simply rely on published credit ratings. The level of effort

this requires is significant, so most investors only undertake this if the borrowing size is at least \$50 million.

EDII has introduced legal mechanisms that address both credit quality and size barriers during its partnership with USAID. These mechanisms belong to Mexico and may be adopted or applied by any Mexican state or municipality. The GDA Program introduced structural features and mechanisms that successfully enhanced the credit quality of transactions to achieve AA.Mx or higher credit ratings. These included the Master Trust revenue intercept structure, state bond banks, and the accredited trust mechanism. In the case of state bond banks, which are a type of special purpose vehicle (SPV), EDII demonstrated that the SPV could successfully pool debt transactions on behalf of smaller borrowers and meet both the transaction size and credit quality requirements of private investors.

3) Mexico's Public Finance System

The report should clearly outline Mexico's public finance framework, especially what taxes may be legally collected by municipalities and states (they are different), and how the intergovernmental transfer system works. The report should make clear that subnational governments receive multiple types of transfers from the federal government, including those categorized under Ramo 28 of the Federal Budget, which are the only federal transfers which may be applied to debt service, under specific conditions imposed by the national *Ley de Disciplina Financiera de las Entidades Federativas y Municipios*, promulgated in 2016. The draft reports contains references to this law that are incorrect, and does not provide sufficient explanation for readers unfamiliar with Mexico's public finances.

4) The Domestic Capital Market and Subnational Debt in Mexico

The report should incorporate an overview of subnational borrowing through Mexico's capital market. This should explain the objectives of banks and institutional investors, and how government regulation and oversight has evolved over the course of the EDII-USAID partnership.

An overview section should outline the major changes to the legal and regulatory framework for subnational government borrowing. This outline should highlight major events that had an impact on the Mexican capital market and subnational government borrowing, starting with the Zedillo administration's actions to strengthen the federal government's credit quality by formally disavowing any implied federal guarantee for subnational debt and changes to banking regulations that put in place requirements for two separate credit ratings for subnational debt transactions.

This section should incorporate a summary description of the role of key capital market stakeholders, including investors, borrowers, market regulators, and financial service providers including trustees, escrow and paying agents, specialized legal counsel, and independent credit rating agencies.

The section should identify the volume of the subnational market at the start of the Program and what the volume is today.

The Mexican capital market has been affected by international events, such as the global financial crisis that started in 2008, and by domestic events, including high profile cases of subnational government corruption. EDII's work enabled both Hidalgo and Quintana Roo to complete financing transactions following the 2008 crisis, at a time with AAA-rated U.S. states could not obtain new financing. EDII's work introduced mechanisms, including both the Master Trust and the Accredited Trust, that increase transparency for all parties and which provide structural assurances that funds are properly applied.

The report should include reference to the credit ratings achieved by EDII-structured transactions. The ratings are key to accessing the capital market because private investors compete for transactions that meet specific credit levels (AA.Mx or higher). They also represent third-party evaluations of transactions by credit rating agencies, and in the case of new structures, by their legal advisors. EDII's transactions under the GDA Program are designed to be of the highest quality because this benefits both borrowers and lenders, and because high quality transactions are more likely to be studied and replicated by other market participants.

The report should also point out the dangers and pitfalls presented by unscrupulous borrowers, such as the cases of the states of Coahuila and Veracruz.

5) EDII as an Independent Financial Advisor

The report incorrectly refers to EDII as "providing financial services" in various sections. The report instead should describe the EDII's role as an independent financial advisor. EDII and similar independent firms do not invest money, nor do they have a stake in the outcome of any financial transaction except that it is the best possible outcome for government clients. In the U.S. some financial advisors are affiliated with banks; this presents a possible conflict of interest that U.S. market regulators have addressed.

Independent financial advisors are hired to provide professional guidance to government officials based on market experience. EDII provides diagnostics and analysis to help inform government decision-makers, and the firm also makes recommendations for improving practices and/or laws and regulations in order to achieve long-term goals. EDII helps governments set sound foundations for their own borrowing, while recognizing the importance of maintaining flexibility for future borrowing.

EDII also helps subnational government clients plan, structure, and execute debt transactions. Our objective is always to help clients obtain financing under the best possible conditions available in the market.

EDII is careful to ensure that innovations, including the Master Trust, state bond banks, and the Accredited Trust meet all legal and regulatory requirements at the national and state levels. In the case of the Accredited Trust, EDII sought and obtained a modification to the Ley de Disciplina Financiera that permitted the structure. Subsequently Mexico's Comision Nacional Bancaria y de Valores (CNBV) reviewed the structure and issued instructions for its application in debt transactions. Other transactions required modifications of state laws and even state constitutions so that borrowers would be in compliance with national laws.

6) General Timeline for Infrastructure Project Planning, Design, and Development

The report implies that EDII is at fault for energy projects not going forward during the final phase of its partnership with USAID. The evaluation should explain to the readers how subnational infrastructure projects are planned, designed and developed. A financial advisor is only one of many private firms that play key roles in this process. EDII's role is to help states and municipalities address financial issues. Other firms are responsible for the quality of the products they contribute, including technical design features, and for obtaining the necessary permits. Preparation for a financing transaction can only be accelerated once a project is ready to show the market.

No infrastructure project financing has been delayed because EDII failed to meet its obligations to subnational government clients.

7) More Rigorous Presentation of the Legal/Regulatory Framework Established by Mexico's Energy Reform of 2012 and its modification in 2016

In order to more precisely respond to the research question concerning the GDA Program's support for Mexico's Energy Reform, the evaluation report should provide more explanation to readers. Greater context is also needed to appropriately evaluate EDII's efforts to promote financing for clean energy projects under the terms of the GDA Agreement.

Mexico's Energy Reform was established in two phases, starting with the changes implemented under the initial reform in 2012 and then incorporating the deeper changes that were promulgated under the 2016 modifications to the reform. The reforms established a new and robust legal/regulatory framework that directly affects the ability of states and municipalities to build energy-related infrastructure projects.

Prior to the Energy Reform (2012 and modified in 2016) the Federal Electricity Commission, CFE, was the sole national utility. As such it held a monopoly on power generation, transmission, and distribution. All retail consumers purchased their electricity from the CFE. The Energy Reform drafted in 2012 allowed entities to generate power, but only for their own consumption. However, in 2016 modifications of the reform allowed private entities to generate and sell energy in the Mexican energy market as long as they registered as Qualified Generators with the Government of Mexico's Energy Regulatory Commission (CRE). The 2016 reform amendments also permitted private entities to use the nation's electrical grid system, provided they registered as Qualified Suppliers with CRE, and paid a transmission fee to the CFE's *Centro Nacional de Control de la Energía* (CENACE). The 2016 modifications also allowed private and public entities to purchase electricity directly from third parties, and not just through the CFE.

Under the law municipal power distribution grids must be updated with circuits that can handle medium voltage, and that can measure power. Municipalities that fulfill this condition may register as Qualified Consumers with CRE. This establishes a foundation for more precise control and metering, which in turn creates opportunities for savings of both money and energy.

State and municipal governments purchase power for city-lighting, public buildings and water pumping from CFE. CFE estimates their consumption using a statistical methodology rather than by actually measuring actual usage. Most cities and towns in Mexico do not yet meter systems

connected to the distribution grids. With the new energy law, municipal governments may register as Qualified Consumers if they re-engineer the city/towns power distribution grids into circuits measured in medium voltage. This way CFE or any Qualified Supplier can now charge for the actual, versus estimated usage. A metering system is a necessary foundation for establishing the viability of any proposed project to increase energy efficiency.

Mexico's energy reform modifications of 2016 now permit subnational governments to meter their electricity usage and to seek lower power prices in the new energy market, looking at offers from Qualified Generators and Qualified Suppliers. It also created an opportunity for these entities to explore new technologies that promoted greater energy efficiency, such as LED public lighting systems.

States and municipalities may participate in energy generation projects, so long as they are registered with CRE as Qualified Generators/Suppliers. Several generation projects are in development, including the waste-to-energy project for Hidalgo and the Coahuila solar park that are part of EDII's pending project pipeline as reported to USAID.

8) Cite the Narrow Window for Energy Project Development

The report correctly notes that EDII was not successful in obtaining financing for clean energy projects. However, the report is incorrect in asserting that this is because EDII pursued different projects. EDII pursued the goals of its GDA partnership with USAID throughout the period of the last agreement.

A more complete review of the national legal and regulatory framework for energy provides important context for the lack of energy project financings. The actual window for developing new projects dates to the 2016 modifications of the energy reform. This presents a very narrow window for subnational governments to evaluate their opportunities under the new legal framework, identify opportunities, and plan and design projects. Some entities clearly recognized the opportunity and have made significant advances. However, EDII is not aware that any state or municipality financed a clean energy project during the period of the GDA Agreement, 2015-2018.

EDII notes that only PEMEX and the CFE (*Comision Federal de Energia*, the Federal Energy Commission) have completed some new infrastructure projects under the new energy laws. A handful of private energy projects were grandfathered under the terms of the Energy Reform and subsequent modifications (*proyectos legados*).

9) The Impact of the Election Cycle on Infrastructure Financing

Although the report notes that elections lead to turnover among public employees, and therefore impact the effectiveness of EDII's training and capacity-building efforts, the report omits reference to the fact that many states have a prohibition on new borrowing in the final months of an administration. This self-imposed ban on borrowing tightens the window for infrastructure project development.

The report should also explain that states and underlying municipal election cycles are usually coordinated; state governors are elected to 6-year terms, mayors to 3-year terms (Coahuila alone has adopted 4-year municipal terms.). Legislators at the state and local levels may serve more than one term, but cannot run for consecutive terms. State legislatures are typically comprised of

elected representatives from multiple parties. Long-term borrowing by states and municipalities requires action by both executive and legislative bodies.

10) Corruption as a Core Challenge to the GDA Program

The evaluation should be direct in referencing corruption as a real challenge to the GDA Program. While it is true that some actors resist innovations and change for valid reasons, a number of actors have confronted EDII over the course of its partnership with USAID because the firm's market-based recommendations threatened a deeply entrenched system of obtaining bribes. EDII has been asked for bribes many times, and we have always refused. We have cited our partnership with USAID as a reason for maintaining transparency. We have been fired for failing to pay bribes, and we have shared these cases with USAID and other U.S. Embassy sections. EDII staff has provided specific examples to the evaluation team. Corrupt PRI officials used opaque financing methods to obtain funds for political and personal purposes.

Ongoing corruption is a key reason why more entities have not consistently applied the best practices that EDII has introduced. Ongoing corruption is a reason why the State of Veracruz was faced with the gravest financial crisis in recent Mexican history.

We note that the evaluation team interviewed (REDACTED), an individual who has an ongoing dispute with EDII. This person demanded payment from EDII in exchange for a positive evaluation. We refused. This individual's statements should not be incorporated in the evaluation.

Unlike the U.S., Mexican states and municipalities cannot declare bankruptcy. Indeed, Veracruz would continue to receive significant federal transfers from one year to the next. However, the state had entered into debt contracts that contained unusual balloon payments that would trigger a default that would in turn accelerate debt service repayment for all obligations. The national government responded to the crisis generated by Veracruz (and other states) by further restricting borrowing conditions for subnational governments in the *Ley de Disciplina Financiera*, promulgated in 2016.

Section III. EDII comments on Report Errors and Omissions

1) Executive Summary pp. 8-10

The summary reflects the errors contained in the body of the draft report.

p. 8

EDII notes errors and omissions related to the nine USAID Research Questions:

Question 1. To what extent were the activities implemented as planned during the five main phases?

The report omits reference to EDII's effort to support the Merida Initiative, which became effective in 2008. At the request of the USAID Mission and Ambassador Carlos Pascual, EDII shifted its outreach efforts to focus on the northern Border States to promote greater public infrastructure development. It is assumed that infrastructure attracts increased private investment overall, and

thus contributes to job creation. Job creation has been promoted as a means of preventing crime and violence by multiple Mexican administrations. EDII's work sought to complement the limited development financing available through the North American Development Bank (NADBank). EDII met repeatedly with federal officials engaged in President Calderon's *Todos Somos Juarez* initiative, including individuals in Presidencia and SEDESOL. Unfortunately we did not develop new transactions in this region at that time. EDII has always been willing to adjust our outreach and engagement with potential subnational government clients to reflect USG priorities during our partnership with USAID.

Question 2. How has the nascent local governments' access to financial markets expanded as a result of the EDII activities?

We assume that "nascent" refers to the capital market.

In order to address this question the evaluation report should identify the barriers to subnational governments accessing financing through Mexico's capital markets, discussed in Section II, above.

Political risk was one barrier. Prior to the reform of the national financial structure in the 1990s, subnational governments could access credit based on their political ties to the party in power, and only for the term of the sitting governor/mayor. Debt repudiation was a real probability. Elected executives and legislators serve single terms under the "no re-election" section of the Mexican Constitution of 1917; new authorities often failed to recognize the contractual obligations entered into by their immediate predecessors. Local officials tied to the PRI party structure were favored by some banks that sought to tightened relationship with the party that controlled the national government.

While increased lending to subnational governments is important, it is equally important that lending be executed under appropriate conditions to ensure the soundness of the capital market. Mexico's financial system has been challenged by the banking crisis of 1994 and the global financial crisis of 2008. Hidden transactions among corrupt actors, such as those completed by past administrations in the states of Veracruz and Coahuila have triggered reforms at the national level. EDII client transactions have always fully met or exceeded legal requirements for transparency, and the mechanisms that EDII has introduced through these transactions have been recognized as strong by investors and credit rating agencies.

One of the features affecting this expansion of the market was the introduction of the Master Trust mechanism, created as part of EDII's work with Michoacan under its initial cooperative agreement with USAID.

According to SHCP records, at the time EDII started working in Mexico the volume of subnational debt in the capital market was USD \$11.1 billion; volume as of June 2018 is \$27.2 billion. SHCP reports that the current market comprises 1,478 transactions that include short-term debt (due within 12 months) and leases, as well as long-term obligations such as bonds (*emisiones bursatiles*) and loans with Banobras and commercial banks. A small percentage of long-term obligations are secured by own-source revenues, but the majority are secured by a pledge of a portion of federal transfers (*participaciones*). Of the total debt outstanding as of June 2018, \$24.5 billion is secured by

transfers applying the Master Trust mechanism first introduced by EDII through the Michoacan structured loan transaction of 2002.

Question 3. How is the EDII activity addressing the needs of target beneficiaries?

How does USAID define “needs of target beneficiaries” for the purposes of this evaluation? Capital market participation is a means through which governments can obtain financing for infrastructure projects in order to address such needs, but EDII itself did not have a role in establishing priorities. During the course of the final phase of the GDA Agreement EDII sought to work with entities that had established energy and/or crime prevention projects as priorities.

Question 4. How effectively is EDII building the capacity of implementing partners and activity beneficiaries?

EDII notes that several of its clients, including Quintana Roo, Hidalgo, and Michoacan, have successfully accessed capital market financing without EDII assistance, but this is not adequately explained in the draft report.

Question 5. How does the activity support the objectives of Mexico’s energy reform?

The report does not adequately outline the objectives of the energy reform and how states and municipalities seek to take advantage of the opportunities the reform presents. This is discussed more fully in Section II, above.

Question 6. What can be achieved by the end of Phase Five?

EDII achieved the implementation of the equivalent of a “Mexican Bond Bank” by introducing an innovative special purpose vehicle, the *fideicomiso acreditado*. Both SPVs stand in front of the borrowing entity or entities and facilitate the interception of federal transfers into an irrevocable trust for debt service. Both have been proven to achieve higher credit ratings for transactions than the stand-alone ratings of borrowers.

Because EDII was unable to find a government or private entity willing to host a national bond bank, our firm, in consultation with USAID, elected to design a mechanism that can be utilized by states and municipalities regardless of whether or not the states create bond banks. EDII notes that both SPVs provide structural credit enhancement. More developed capital markets, such as the U.S. municipal market; embrace the use of multiple types of credit enhancement features.

EDII pursued the Veracruz debt restructuring as an opportunity to introduce the new *fideicomiso acreditado* SPV in consultation with USAID. The entire process, which began when the new state administration took office on December 1, 2016 and ended when the final old debt obligation was retired in February 2018, took approximately 15 months.

The *Fideicomiso Acreditado*, a new legal mechanism that is similar in impact to a “bond bank”, was tested and legally implemented, with full attention of banks and other private sector investors, through multiple transactions executed by the State of Veracruz in November 2017. The structure received two AA.Mx ratings; when the transactions occurred, the State of Veracruz was rated below investment grade and could not access the capital market. EDII outlined this achievement in its

quarterly progress reports presented to USAID during the course of this evaluation. EDII provided the evaluation team with documentation related to the *fideicomiso acreditado*. The mechanism is now legally available to all Mexican states and municipalities. EDII is continuing to work with Veracruz and other entities with projects in the GDA program pipeline at the time the Agreement expired have expressed a strong interest in using a *fideicomiso acreditado* for future transactions. It was the major achievement of the GDA Program period 2015-2018.

Question 7. Did USAID involvement enhance Mexico’s developmental opportunities, and particularly in local governments’ access to financial markets?

The World Bank notes that there is never enough public money to address a country’s infrastructure needs. Accessing domestic capital markets is one means of increasing investment in infrastructure. However, in most countries subnational governments face significant barriers to borrowing through the local capital market. USAID’s contribution to Mexico, supporting the careful expansion of the domestic capital market to bring more investment to subnational entities is unique and the results obtained have attracted interest from other sovereign governments and multilateral development banks.

USAID’s GDA partnership with EDII without question enhanced the ability of states and municipalities to access Mexico’s capital market though the draft report does not adequately reflect that fact. Furthermore, these “new” borrowers have met or exceeded all market requirements. At the time the EDII/USAID partnership began the public finance capital market was \$11.1 billion, it is now \$27.2 billion. That figure includes short-term obligations, leases, and long-term debt secured by own-revenue sources. However, \$24.5 billion of that debt is secured by the irrevocable pledge of federal transfers utilize a form of the Master Trust mechanism introduced by EDII under its first cooperative agreement with USAID. Additionally, some of the debt was issued through the Hidalgo and Quintana Roo state bond banks that incorporate that master trust mechanism, some reflects the new debt obligations of the State of Veracruz that apply the *fideicomiso acreditado* structure. The U.S. public finance market, the oldest and deepest in the world, has a volume of roughly \$6 Trillion.

Question 8. Is the activity designed and implemented in a way that once USAID leaves the achievements remain and are consolidated?

The achievements of the GDA Program are reflected in law and practice, notably the broad application of the Master Trust structure introduced under the EDII-USAID partnership. The report should make it clear that USAID’s presence or absence will not impact the continued application of the innovative structures introduced by the GDA in the domestic capital market.

Question 9. What should be highlighted to replicate this Mexican experience in other countries?

Because the evaluation team lacked fundamental knowledge and understanding of capital markets and public finance, its recommendations are deficient in relation to this question in particular.

EDII has sought at all times to develop transactions that promoted best practices and the use of innovative mechanisms that significantly improved credit quality in order to attract potential investors/bidders. By attracting more investors the offers become more competitive, ensuring that

clients obtain financing under the best possible conditions. All of the mechanisms and best practices are grounded in Mexican law, and are therefore replicable by Mexican entities. In countries that undertake similar legal and regulatory reforms, these mechanisms can also be adapted to those countries' legal frameworks to produce similar results.

p. 9 “PARTIAL ACHIEVEMENTS A key goal was the creation of a single national bond bank; in fact over the period of the activity no national bond bank was created but several state bond banks were created. These provided subnational and regional governments with additional resources to meet the needs of their citizens. EDII’s estimate of the number of citizens reached was 27,923,891. However, the evaluation team did not have access to information on how this translated to answering the needs of the citizens. In terms of capacity building, EDII’s work greatly improved the ability of officials in regards to the use of the BB/SPV tool. A constraint to sustaining the capacity was the high turnover rate of government employees at each change in government. This occurrence stalled the ability to create a sustained qualified staff.

As previously noted, EDII created the *Fideicomiso Acreditado* that serves essentially the same purpose as a national bond bank: it is a special purpose vehicle that stands in front of the borrowing entity which can directly receive a portion of the borrower’s federal transfers.

There are no regional governments in Mexico. Subnational governments comprise states and municipalities.

Borrowing through the domestic capital market is a means of financing public works. Elected officials determine which projects are prioritized and eventually built. How each project “meets the needs of citizens” is highly subjective: the evaluation team had access to public statements from each borrowing government concerning their justifications for each new project. EDII suggested using the state’s population as a stand-in for “beneficiaries” when the transactions are completed using an SPV like a bond bank or the *fideicomiso acreditado* to restructure outstanding debt or to build state infrastructure projects.

Turnover is a constant feature of all three levels of government because there is no re-election and as of this writing, no formal civil service at either the state or national levels.

The election cycle also has an impact on project developments and financing transactions, because many entities have adopted a ban on new borrowing in the final months of an administration.

p. 9

“MISSED OPPORTUNITIES Stronger USAID activity oversight could have detected the diverging interests and ensured that activities remained focused on GDA objectives. This particular problem arose in the last stage of the 16-year long collaboration. Further, USAID management would have benefited from having a deeper understanding of the complexity of the Mexican financial markets and political priorities that led local governments to prioritizing financing for other infrastructure projects unrelated to crime prevention and clean energy.

EDII remained focused on GDA objectives throughout its partnership with USAID. The authors apparently believe that EDII did not pursue projects related to energy and crime prevention. This is not true. The authors seem to assume that there are a number of “bankable” projects ready and waiting for investors. This is a gross error.

There’s a significant gap between developing a project proposal and having something that is ready to bring to investors. Everything must be tailored to local requirements and objectives, and proposed costs and contingencies must be reviewed. EDII’s work as a financial advisor necessarily focuses on the financial aspect of project preparation

Thanks to EDII, during the final GDA Program phase Banobras, the national development bank, developed a program of lending to support specific project development.

Saying that USAID management did not understand Mexico’s political priorities is astonishing. USAID has an ongoing relationship with the Government of Mexico (GOM) and with participants in the energy sector. Also, USAID through this GDA with EDI has permanent participation with national, subnational, regulatory, and private entities in the sector. USAID and EDI have positively influenced both the national and local governments in establishing priorities, mechanisms and tools to foster crime prevention and clean energy projects.

EDII informed the USAID AOR and outlined in quarterly reports roadblocks as these emerged. This includes the contradictions between national energy legislation designed to promote the development of crime prevention and clean energy projects, and the legislation advanced by the Secretariat of Finance that deliberately restricted and even prohibited the use of specific revenue streams that would have readily been used to finance such projects. Both USAID and EDII highlighted these contractions in discussion with Government of Mexico officials. These officials recognize that this feedback as tangible value added provided to the Government of Mexico by this GDA Program. This level of constructive feedback could only be delivered because both GDA partners, USAID and EDII, deeply understand the political priorities and objectives of the different participants in the sector.

pp. 9-10 Recommendations- EDII OBSERVATIONS

EDII believes that most of the recommendations summarized here are aspirational rather than practical. What kind of activities and timeline would be required to “raise the local political profile” of clean energy projects? How many conditions can USAID impose on financial mechanisms and transactions based on providing technical assistance? Why would any entity subject itself to USAID’s conditions?

It is up to each country to establish the legal framework for capital market transactions and to impose legal restrictions on the use of proceeds, etc. Domestic investors also affect the conditions and structure of transactions by subnational governments. When and if a DCA guarantee is applied USAID is in a position to impose certain conditionality; but not for technical assistance alone.

What are the “compulsory mechanisms” for bond banks cited in Recommendation #5? The bond banks established through the GDA program are designed to be optional; both USAID and EDII sought to enhance government financial flexibility rather than constrain it.

2) pp. 12-14 Evolution of Evensen Dodge Goals, Objective and Activities

The authors write on p. 12:

“With the change in power, the company had seen a business opportunity for new financial services in which EDII had long experience in the U.S. and a large competitive advantage.”

The only financial services that EDII provides are those of a financial advisor. The report does not contain any information about this role, which is key to understanding EDII’s work in Mexico. We do not understand what the authors mean by a “large competitive advantage.” It seems to imply that EDII sought to establish some kind of “advantage” through its work with USAID on this GDA Program. EDII competed successfully in the U.S. and welcomes legitimate (vs. corrupt) competition in Mexico. A larger capital market creates more work for EDII, other financial advisors, and all other service providers.

The opportunity to establish greater access to financing/private capital (versus financial services) for subnational governments arose, not from a “change in power”, but from key policy actions taken by the Zedillo administration following Mexico’s peso crisis in the 1990s. In order to protect the country’s sovereign credit rating, the national government expressly renounced any responsibility for making debt payments on behalf of subnational governments—thus eliminating a moral hazard for the federation.

In addition, the government implemented new standards for bank regulation, notably requiring banks to increase their reserves to reflect the credit quality of their loan portfolios. Local government loans had to have two independent credit ratings or be considered to be below investment grade. This action increased the business opportunity for the three major international credit rating agencies at that time, Fitch Ratings, Moody’s Investors Service, and Standard & Poor’s, all of which have established operations in Mexico and all of which rate subnational government credits.

Evensen Dodge, an independent financial advisory firm based in Minnesota, recognized that these changes were significant and that they presented a business opportunity. Once they completed an evaluation of the Mexican capital market, the firm recognized that Mexico presented a unique opportunity to develop the domestic capital market. Evensen Dodge was fully aware that this would entail working carefully with all market stakeholders, including not just potential borrowers, but investors, banks, financial system regulators, and other financial services providers (such as ratings agencies). To facilitate working with USAID, Evensen Dodge established Evensen Dodge International Inc. (EDII), to distinguish the work done outside the U.S. from work performed in the U.S., and to simplify financial reporting to reflect USAID’s requirements.

See our discussion of the role of an independent financial advisor in Section II, above.

The authors write on p. 14:

“The longest standing of the five USAID/Mexico’s energy activities is the Mexico Bond Bank Activity, established to introduce financial models that could leverage resources for sub-regional entities for climate change mitigation.

Energy-related projects by states and municipalities primarily fall into three categories: 1) energy-efficient public lighting systems; 2) waste-to-energy facilities that incinerate solid waste to generate electricity; and 3) participation in renewable energy generation projects, such as wind farms or solar projects. Subnational governments do not have a mandate for climate change mitigation per se, but the carbon savings from each energy-related project certainly could be measured using standard methodology. As a financial advisor, EDII focuses on the financial viability of projects and whether or not they could be financed using subnational government revenues, project revenues, or a combination.

3) pp. 15-19 The Development of the Mexican Bond Bank

On p. 16 the authors write:

“This section discusses the characteristics of a bond bank and compares the system for obtaining loans through the financial markets in Mexico before and after the introduction of the Special Purpose Vehicle (SPV), i.e. a bond bank.

The major goal of the GDA4 was that EDII would create a nationwide bond bank—an entity that issues bonds for sale—and provide technical assistance to sub-national authorities (and associated public and private entities) to further develop their institutional and financial capacities.

The concept of having a “Bond Bank” is related to the ability and capacity of local governments— historically weak in credit worthiness—to improve their access to financial markets. A Bond Bank is a “...state-level entity that provides that state's smaller public entities with debt financing at a lower cost than what the small entity could obtain on its own. Bond banks serve cities, municipalities, schools, hospitals, water and sewer districts, and more. They are able to provide lower-cost financing as long as they have higher credit ratings than the entities that seek to borrow.”⁵

The bond bank is the legal framework that makes it possible to create a loan guarantee for municipalities through federal tax revenue intervention. It can be a trust fund or an institution and in both cases it needs to be transparent and accountable to the local legislative body. By definition, it needs to be created by a local law. A trust fund at the federal level is its equivalent and requires the fund management to report on the transactions that are also transparent, to the local authorities. However, the versatility of a bond bank is greater. One can create a legal entity that can guarantee that the debt acquired is backed up by the federal institutions for accessing markets.”

This entire section is convoluted and confusing. That the authors resort to a reference from “Investopedia” (footnote 5) is troubling.

A bond bank does not “issue bonds for sale;” a bond bank engages in debt transactions on behalf of one or more participating borrowers. The bond bank does provide transaction-related services to participants.

A bond bank may issue bonds or engage in a competitive structured loan process on behalf of the borrowers participating in a specific transaction. State- level bond banks may be used by the state or any underlying municipality alone or in a transaction that pools multiple borrowers. It is a special purpose vehicle (SPV) that can be used multiple times with different combinations of participants—but there is no requirement that states use the SPV once it is in place. It is designed to be optional.

Pooling allows smaller borrowers to save on the costs overall—costs are distributed proportionally. The bond bank transactions are evaluated and assigned credit ratings that are almost always higher than the ratings of the smallest transaction participants.

44 U.S. states have bond banks. These SPVs function as debt consolidators: in the U.S. as in Mexico smaller municipalities lack experience in accessing competitive financing. Bond banks are typically part of the state treasurer’s staff; this staff works with the entities seeking financing to ensure that they provide the standard information required by the SEC for the preparation of offering documents, and they work in concert with the legal counsel hired to oversee the transaction. Bond banks work with external financial advisors.

The perceived or real lack of creditworthiness is a barrier to accessing private finance. As noted earlier, the Mexican government linked banks reserve requirements to the credit risk of their loan portfolios. Institutional investors, such as pension funds and insurance companies, are also concerned about credit risk.

There is no “loan guarantee” and there is no “federal tax revenue intervention.” A guarantee in capital markets is a third party legal contract. Theoretically a guarantee could be provided by the federal government, an international development agency such as USAID through its Development Credit Authority, or a private entity, such as a bank or an insurance company. In transactions that involve a guarantee, investors evaluate the credit quality of the guarantor and the specific guarantee conditions (i.e. is it full or partial), and the timing for payment to creditors. It appears that the authors mean to refer to the higher credit quality of bond banks because of the structural features incorporated at the recommendation of EDII.

Bond banks are created under state laws, and are designed to comply with federal laws. These vehicles may be public or private.

The authors refer to a “trust fund at the federal level.” This is incorrect. Mexican law permits multiple types of trusts. A trust fund is distinct from an irrevocable trust account. A trust account in Mexico has the same as an account in the U.S.: the funds therein are managed by a third party and are designated for specific purposes. Such a trust is transparent to all parties. The authors use the term “trust fund” incorrectly throughout the draft report.

There is no legal guarantee in these transactions; the transparent flow of funds through the SPV is sufficient. Mexican investors are satisfied with the Master Trust mechanism that was introduced by EDII through its work with Michoacan in the first phase of its engagement with USAID. This is not a

“federal tax revenue intervention” but a legal instruction to Hacienda (the Finance Secretariat) to direct a specific portion of the borrower’s share of federally-collected revenues to a trust account for debt service payment. These monies belong to the subnational entity but because they are not comingled with other state monies, investors see the funds as having a higher credit quality. (As stated above, the Master Trust, now a market standard, is a major contribution of the GDA Program that increases access to finance for subnational entities. The evaluation report should reflect this).

Bond banks as established in Mexico increase transparency. The loan or bond proceeds flow to the bond banks, which immediately transfer them to the participating borrowers; the bond bank holds no funds. The bond banks also incorporate the master trust structure through which entities instruct Hacienda to assign a small portion of their federal transfer monies to a dedicated trust account for debt service repayment. (the master trust was introduced by EDII through its work with Michoacan in the first phase of this GDA Program and is currently the market standard in Mexico). These legal mechanisms address credit concerns and increase the potential for attracting investors, thus creating greater competition. Bond bank transaction ratings to date have been higher than the stand alone ratings assigned to the states in which they were established. EDII has provided the evaluation team with the credit reports; the evaluation report should indicate this achievement.

On p. 17 the authors write:

“EDII’s early work focused on supporting the necessary reforms within the Federal legislation to allow states that were willing to do so, to create their own bond bank through some local and state legal changes, including to the local constitution. For leveraging private finance, it was also important to create a local law on public-private partnerships (PPP). In the case of the State of Hidalgo, for example, the law contained twelve different types of potential partnerships allowing greater flexibility in the legal contract to enact the partnership. Detailing contracting modalities is important when talking about using public finance, as this entails greater responsibility in how to operate with private sector partners and avoid potential conflicts of interest or corruption.”

Work on public-private partnership enabling legislation and concomitant training of public officials and employees proceeded parallel to EDII’s work promoting the introduction of bond banks and other features that enhanced creditworthiness of subnational borrowers.

The three case studies presented as part of the draft report clearly demonstrate that EDII’s work with subnational entities requires systematic review and modification of each state’s legal framework for borrowing. This extensive engagement is what establishes the replicability of completed transactions: once the framework is in place subsequent transactions may be completed more easily. This careful, comprehensive legal work is a cornerstone of EDII’s work in Mexico. It is what ultimately helps to build the financial architecture for future infrastructure borrowing.

The Quintana Roo bond bank (Instituto para el Desarrollo y Financiamiento del Estado de Quintana Roo, IDEFIN) differs from the Hidalgo bond bank (Instituto para el Financiamiento del Estado de Hidalgo, INFEH). The evaluation report should indicate that EDII tailors SPVs to meet the needs and objectives of government clients, although these represent the same type of SPV. (We note that there are key differences among the U.S. state bond banks as well).

This work was not limited to some “early phase” of the GDA Program; the work EDII completed with the State of Veracruz from 2016-2017 that culminated in the establishment of the *fideicomiso acreditado* SPV involved multiple changes in state law and included important adjustments to national laws and regulations.

Public-Private Partnerships (PPPs) are related to but distinct from access to finance through capital markets. Part of EDII’s work with Hidalgo and other states has been to help states craft appropriate legislation to enable multiple types of PPPs, with varying degrees of private participation. Specific PPP models are appropriate for different types of projects. Prior to EDII’s interventions, the enabling legislation was broad and general and essentially only applied to franchises. The draft report reflects a superficial understanding of PPPs; this necessarily undermines the team’s evaluation of EDII’s work to promote financing for clean energy and energy efficiency projects during the period 2015-2018. There are several erroneous statements in the draft report related to EDII’s work to establish a legal foundation for multiple types of PPPs in Mexico. EDII considers its work to introduce comprehensive PPP legislation as a significant achievement of this GDA Program.

On pp. 17-19:

The authors do not present a coherent explanation of why bond banks are a means of improving access to capital market financing. The report is missing information about the key barriers to borrowing banks and institutional investors: subnational borrowers are not perceived to have the credit quality that these investors demand.

The report does not address how bond banks play a key role in presenting pooled financing transactions to the market. In the United States the threshold for accessing the capital market is roughly \$1 million. If an entity wants to borrow \$1 million they could elect to issue a bond or seek a competitive bank loan. In Mexico the threshold is higher, \$50 million, which reflects the much smaller market volume and the fact that market-based lending to subnational governments has been in place for a relatively short period of time. Smaller entities would rarely be able to meet this threshold on their own; pooled financings through bond banks thus present an important innovation. This was demonstrated by the Hidalgo bond bank transaction for multiple underlying municipalities, outlined in the Hidalgo case study.

4) pp. 20-32 FINDINGS:

RESEARCH QUESTION 1: TO WHAT EXTENT WERE THE ACTIVITIES IMPLEMENTED AS PLANNED DURING THE FIVE MAIN PHASES? Pp. 20-23

On p. 20 the authors write:

“The original objective (and the successive modifications) of the GDA allowed EDII flexibility on choosing the activities to implement in order to achieve the goal of reaching the agreed-upon transaction targets, in part, because when the USAID/EDII relationship started under a Cooperative Agreement, the activity was considered “quite experimental.”⁹

EDII agrees that the initial relation was “quite experimental.” This should be highlighted in the final evaluation.

The statement concerning the objective of the GDA is incorrect. The objective of EDII’s GDA partnership with USAID has been to expand subnational government access to capital market financing. EDII pursued transactions in order to demonstrate how best practices combined with appropriate legal structures can facilitate access to private capital at market rates.

The transactions are, of course, important. They ground the project in reality and offer immediately measurable result outcomes. Government officials do not have time to work with partners who do not help them advance their policy goals, so the transactions by necessity reflect local priorities. The completed transactions demonstrate that credit quality can be improved through structural and legal means that may be replicated by other entities. The transactions thus provide proof of concept.

a. P. 20-22 Synopsis of Phases – summary

On p. 21—authors correctly note that the initial phase of EDII involvement with Mexico’s financial “architecture” was undertaken without USAID involvement.

On p. 21 the authors write:

“The evidence from the review of documents and interviews with EDII Personnel revealed that from the many initiatives launched by EDII in different States, not all were fruitful, especially in terms of completing financial transactions. EDII would introduce new transaction development efforts in Quarterly and Annual Reports, but not discuss them in subsequent reports, making it difficult to determine what if the transactions had been completed and projects in fact were underway. The final list of transactions in Annex VI required many iterations and the authors continue to question the reliability and completeness of the information. “

EDII did in fact work with multiple governments on proposed transactions that were never completed. This is true of the period from 2015-2018 and also for previous years of this program.

In one case outlined in an interview with the authors, EDII staff noted that initial work with the State of Quintana Roo was abruptly terminated when the governor at the time solicited a bribe that EDII refused to pay. The state treasurer and EDII were fired; the state contracted with new “advisors” who completed the transaction within 60 days using the work product prepared by EDII. The new “advisors” also charged the state an exorbitant fee (as high as 10% of proceeds) and we assume that most of that reached the accounts of the corrupt official involved. That governor subsequently became a fugitive whose U.S. visa was revoked. This is just one example of how corruption interfered with the efforts, and it is one additional reason why this is a development project.

All completed transactions were fully reported to USAID and are a matter of public record, as required by Mexican law. We do not understand why the authors “question the reliability and completeness of the information” regarding completed transactions when they could have pursued records from other sources.

b. Phase Two- Michoacan

On p. 21 the authors write:

“EDII also assisted SoM in issuing a bond. Unfortunately political timing caused the SoM to rush into a more standardized commercial loan. Nevertheless, thanks to the possibility to guarantee the loan with federal tax revenue transfers, the terms were favorable. ”

This is incorrect. With EDII’s assistance, the state negotiated a structured syndicated loan (definitely not a “standardized commercial loan) with private financial institutions that marked the first time such a loan extended beyond the term of a sitting governor. It also marked the first time a state obtained a structured loan at an interest rate of under 10%. This transaction demonstrated, for the first time in Mexico, that states could direct a portion of their Ramo 28 federal transfers to a third-party trust account for the payment of debt service (using the new *fideicomiso maestro* mechanism, the master trust).

The authors fail to note the three major innovations introduced because of EDII’s work with Michoacan in conjunction with a cooperative agreement with USAID: a) introduction of the Master Trust; b) first time a private lender agreed to a 10 year term—previously loans were limited to the period of the sitting governor’s administration; and c) Michoacan took action to implement a state payroll tax because the Treasurer recognized the importance of maximizing the state’s own-source revenues to improve and maintain good credit quality for private investors.

Obtaining credit beyond the administration’s term in office was a very important first step.

The structured loan also introduced the Master Trust structure—a major innovation that is now the market standard for public finance transactions. Again, I think that this section reflects the authors’ lack of understanding of finance. The authors write “Nevertheless, thanks to the possibility to guarantee the loan with federal tax revenue transfers, the terms were favorable.”—no, thanks to the introduction of the Master Trust (*Fideicomiso Maestro*), the terms were favorable. There is no federal guarantee of the loan.

This section should describe the Master Trust and the intercept feature in greater detail—it is a major achievement for the GDA Program.

Footnote (12) on p. 23 to the Legal Reform section states:

“‘Intercepted’ means that the money that usually goes from the Federal Government to the State Government is handled differently when an SPV / BB is in place. When this occurs, the money required to guarantee the SPV / BB operations is redirected to it and the State Government cannot use it for other purposes.”

Because the transfers (*participaciones*) legally belong to the subnational government that receives them, even before the transfer is completed, the interception of these federally-collected monies can only be taken when the State (or other subnational borrower) **instructs** the Federation to transfer the portion of resources that is legally available to debt service directly to the Trust account, which is held by a third party—instead of directly into State accounts. The work to develop the legal framework for this feature is a major achievement for the GDA Program as a whole: some

\$40 billion in state/municipal debt is secured through identical master trust structure. The Master Trust is a mechanism that is available to all subnational entities in Mexico; it is perhaps the most outstanding contribution of the GDA Program during this early phase.

Another, indirect result of the GDA Program work in Michoacan was the state's decision to implement a payroll tax for the first time. (this was the case for several states—because the bulk of their revenues are delivered through the transfer of their share of federally collected revenues, there was little incentive to expand their own tax collection efforts. The payroll tax, implemented by a PRD administration, demonstrates to the private sector that the state was serious about maximizing revenues and being accountable. This was recognized by the credit rating agencies.

On p. 21 regarding Phase Two Bond Banks in Hidalgo and Quintana Roo:

Hidalgo and Quintana Roo both adopted and implemented bond banks, but these SPVs were tailored to the specific objectives and requirements of each state. Both states utilized their bond banks for multiple transactions. At some point in the evaluation report the authors should cite the financial impact of these transactions, including their respective credit ratings. Hidalgo's initial bond bank transaction was significantly oversubscribed and set a long-standing interest rate benchmark, demonstrating very positive response from domestic investors.

Phase Three:

On p. 22 the authors write:

"Phase Three: The SoH, as the pioneer, was most engaged. In order to better use the bond bank, they required clear rules for engaging the private sector. Thus, EDII developed 12 models for public private partnerships. These were subsequently included in the PPP law."

The State of Hidalgo became the first state to adopt a bond bank as a special purpose vehicle. This has been used for multiple transactions by the state.

The state was also interested in generating more public private partnerships (PPPs).

We noted in earlier notes that EDII did not "develop" 12 models for PPPs—our firm completed a study of successful PPPs internationally and presented our analysis as a foundation for adopting legislation that could enable a government entity to apply any and all of these models to projects, as appropriate.

The authors do not mention that USAID asked EDII to direct effort to the border region as part of the government-wide effort to support the Merida Initiative, starting in 2008. EDII did a lot of outreach to state and federal entities during this period, which is not reflected in this summary section.

c. Phase Four

On p. 22 the authors write:

During this phase, a new administration came into power and the incoming Federal Minister of Finance adopted new rules that stopped any further progress on bond banks. All local financial reforms and transactions would be dealt with by the firm where the new Minister used to work – a major conflict of interest (confirmed by all the interviewees).

After some efforts to continue working as before failed, it was clear that other tasks should be undertaken. It was during this phase that EDII deepened their capacity building efforts. Unfortunately few detailed records were kept describing the specific capacity building activities carried out by EDII.”

The authors do not adequately convey the impact of the corrupt actions by the previous Secretary of Finance on the GDA Program. The Finance Secretary did not adopt “new rules” — rules are formally drafted, adopted, and published. In this case the Secretary gave verbal instructions to subnational entities that required them to work with a specific firm to which he has financial ties. This is corruption, not “new rules.” One of many instances of public corruption, this action was the most significant that EDII faced over the course of its work in Mexico because it interfered with our ability to work on behalf of subnational government clients.

This verbal instruction directing states work only with a single advisory firm shut out all other firms seeking to provide advisory services to subnational entities—not just EDII. This is why EDII had to focus its efforts under the GDA Agreement to private entities, not subnational governments. Once Secretary Meade took his position he told states and municipalities they could work with the advisors they chose—and EDII was invited to work with Mexico City and Hidalgo on potential energy projects, and with Veracruz, where we saw an important opportunity to introduce a new special purpose vehicle that would have many of the features of a “bond bank” and that could be available to all subnational governments in the country.

Corruption should be highlighted as a significant obstacle to private innovation, as noted in Section II, above.

d. Phase Five

On p. 22 the authors write:

“... EDII began working with officials in the State of Vera Cruz (SoV). From this point on, EDII focused the majority of its time and resources to solving the debt crisis in (SoV). The work in the State of Veracruz was a significant deviation from the last set of revised objectives, which were to focus market access to further finance USAID/Mexico’s priorities. Further, the work did little to accomplish the specific objectives of the final agreement to finance projects focused on clean energy and crime prevention

EDII claimed some credit for money devoted to a crime prevention fund established by the State of Veracruz that was available as a result of the debt restructuring. This fits within the topic of crime prevention, which was part of EDII’s agreement with USAID.

While EDII acknowledged that this work was a major distraction from the specific objectives listed in the final extension, EDII personnel noted that the SoV was immersed in a critical financial crisis and in a very delicate political situation. All the eyes of the nation turned towards this case and EDII engaged in a drive to complete a dramatic restructuring of a debt of around USD 2 bn...”

The restructuring of the Veracruz debt presented a very important opportunity to introduce a new, nationally applicable SPV, the *fideicomiso acreditado*, which is effectively the Mexico Bond Bank

that was an objective of this GDA Agreement. The *fideicomiso acreditado* is a legal mechanism that stands in front of the ultimate borrower and provides transparency to investors and government regulators. The establishment of a new nationally-available mechanism was possibly only because USAID agreed that work with Veracruz had the potential to impact the entire market. Because Veracruz was in crisis, the SHCP and the CNBV offered their full attention to this proposed instrument. It was implemented because key federal officials agreed that it could work without disrupting the banking system or the capital market, and they provided timely opinions and instructions. From the GDA Program perspective, if this SPV was shown to work for the Veracruz restructuring transactions, it will definitely work for non-stress transactions by other states and municipalities.

This draft report demonstrates a significant misunderstanding of the complexity and the impact of the introduction of the *fideicomiso acreditado*. As EDII noted in reports to USAID, outreach to key market stakeholders in the first months under this 2015 GDA Agreement led us to conclude that a national “bond bank”—while appealing to potential investors—did not have the political support required to establish this mechanism at the national level. No one wanted to host this administratively—and making a “private” bond bank would have required collaboration among multiple private sponsors.

EDII pursued and implemented an alternative SPV. This required modifications to national regulations, review and response from the CNBV (Mexico’s SEC). This needed to be done with a real, vs. hypothetical transaction.

EDII has summarized this outcome in its verbal and written reports to the USAID AOR.

On p. 23 the authors state:

“The SoV case was considered successful by EDII because its national visibility helped adverse political parties understand that the SoV bankruptcy would not benefit anyone and thus, the necessary reforms were made faster and the call to all national banks was led by the Ministry of Finance (SHCP).

What are “adverse” political parties?

SHCP modified the *Ley de Disciplina Financiera de las Entidades Federativas y Municipios* through a Presidential signature. The call to all banks for a meeting where the state introduced the figure of the *fideicomiso acreditado* was made by SHCP because of the severity of the state’s financial crisis and the potential impact on the national banking system. The Comision Nacional Bancaria y de Valores (CNBV) review of the *fideicomiso acreditado* and its subsequent publications of rules for its application took place on an accelerated basis because the pending transaction was for Veracruz. None of the federal entities would have acted with such alacrity had the new SPV mechanism been introduced by a creditworthy subnational entity, despite its positive features. This would probably have languished into the election season but for the urgency of addressing the Veracruz fiscal situation.

The Veracruz financial crisis was extremely problematic on a number of levels, and the federal government wanted to avoid a bail-out situation that likely could cascade to other states and thus

adversely affect the sovereign's credit rating. No other state in Mexican history had faced a default on this scale. Veracruz was not "bankrupt"—unlike the U.S. Mexican law does not recognize governments as "bankrupt."

Based on the success of the Veracruz transactions, EDII suggests that an additional conclusion could be that USAID recognize the opportunities presented by entities in crises. Certain subnational entities always have access to financing, typically the largest, capital city. This program shows that it is possible to introduce replicable market-based solutions that may be used by all government entities, when no one else is willing to work with a government in financial difficulties.

e. P. 23 Conclusions

The authors state:

"After phase two, which ended in 2008, the enthusiasm to create more bond banks declined. "

EDII notes that thanks to their bond banks the ONLY entities that were able to access private credit in 2008 once the global financial crisis was underway were Hidalgo and Quintana Roo. AAA-rated states in the U.S. were unable to access credit during the early phase of this crisis, which started in the fall of 2008.

EDII cannot explain why more states did not seek to adopt bond banks, except to note that each state administration has its own priorities.

The authors also state:

"4) The work of the last three years of the agreement was a deviation from the objectives in the final GDA agreement between EDII and USAID and it would be difficult to assess the impact of the intervention on reducing crime."

This sentence is incorrect. EDII pursued the development of a new mechanism that would expand capital market access for states and municipalities in Mexico, and EDII pursued the implementation of projects related to the energy and crime prevention objectives cited in the agreement. EDII coordinated with USAID's AOR throughout the term of the agreement. The pipeline of projects that EDII developed all relate to energy and crime prevention, and were reported consisted to USAID.

EDII did achieve the establishment of a new mechanism that effectively enhances the credit quality of subnational borrowers. This effect was demonstrated in the set of debt restructuring transactions for the State of Veracruz: two different rating agencies assigned AA.Mx ratings to the transactions using the fideicomiso acreditado at a time when the state's stand-alone rating was B.Mx, below investment grade.

Thanks to the refinancing the State of Veracruz is purchasing and installing a system of security cameras. Because this action is underway there are no data on whether or not the cameras themselves led to a reduction in crime. The state of Veracruz is also applying some of the funds liberated from debt reserve accounts for new state infrastructure projects, which are part of the state's effort to generate new jobs as a means of reducing crime. This obviously an indirect means

of addressing crime and violence prevention, but job creation has been cited repeatedly in Mexican government efforts to reduce crime.

EDII is aware of multiple studies reporting that better public lighting contributes to crime reduction. New LED lighting systems not only reduce energy consumption, they require fewer “poles” to illuminate a broader area. In some cases, municipalities have elected to include security cameras on the same poles. Of course it will take years to determine the specific crime reduction impact of the new systems in each location—is street crime reduced or does it simply move to new areas outside the lighted area. However, it is possible to calculate the future financial impact.

EDII would ask how any program that focuses on increasing access to private capital for infrastructure financing could be evaluated as “reducing crime” given that our work focused on developing financial architecture, legal frameworks, and introducing features that improve creditworthiness in order to appeal to private investors—not on designing and building the infrastructure. Public lighting improvements and the installation of security cameras can deter criminal activities in specific geographic areas, but do the criminals stop committing crimes or do they move elsewhere? Also, several state governors have identified public infrastructure development as a means of expanding local employment. This assumes that one of the “causes” of criminal activity is a lack of economic alternatives. This GDA Program did not direct government clients to specific actions, it was designed to help governments obtain the financing needed for the actions that they wanted to take as part of their crime prevention policies.

The authors state on p. 23:

“In Phase 5, it appears that Evensen Dodge paid more attention to activities that would create future business opportunities within the private sector than to fulfilling its obligations to USAID as agreed to in the GDA.

What is the basis for this untrue statement? All of EDII’s efforts under the GDA agreement were focused on fulfilling GDA objectives. We have fully documented the implementation of the *fideicomiso acreditado*, the new mechanism that stands as the figurative Mexican Bond Bank because it may be legally used by any and all subnational governments in the country. To accomplish these, we structured a compound set of financial transactions on behalf of the State of Veracruz. The *fideicomiso acreditado* mechanism was applied in each separate transaction and in each case the specific transactions were reviewed by two competing credit rating agencies and were assigned credit ratings that were 14 notches above the state’s stand-alone rating. EDII participated in developing a pipeline of projects related to energy and crime reduction, including the Iztapalapa public lighting project, the Hidalgo waste-to-energy project, and the proposed Coahuila solar park, amongst others. The status of these projects was reported to USAID in our quarterly reports. These projects remain in process or pending for reasons unrelated to EDII’s work under the GDA Agreement. See our discussion of Mexico’s Energy Reform and its 2016 Amendments, in Section II above.

The authors of the report completely ignore the fact that is cited on their on p. 22 of the draft report, where they mistakenly refer to new financial “rules” As we noted in our written reports and in interviews with the evaluation team. EDII and other financial advisory firms were barred from

working with state and municipal clients because of the corruption of the Finance Secretary cited in the reference to Phase Four on p. 22.

This corrupt action on behalf of a firm in which he had financial interest meant that EDII had to look to private firms seeking to develop PPP projects related to energy and crime prevention. This was done specifically to further the objectives of the GDA, not *instead* of fulfilling our obligations under the agreement with USAID. Further, when Jose Antonio Meade became Secretary he told states to work with whomever they chose—and Mexico City, Hidalgo, and Veracruz chose to work with EDII, as reflected in the project pipeline that was developed for the GDA.

RESEARCH QUESTION 2: HOW HAS THE NASCENT LOCAL GOVERNMENTS' ACCESS TO FINANCIAL MARKETS EXPANDED AS A RESULT OF THE EDII ACTIVITIES? Pp. 23-24

a. Legal Reform Activities

The report does not reflect a solid understanding of the interconnected relationship among state and federal laws that apply to subnational finance. The section titled “Legal Reform Activities” on pp 23-24 incorrectly summarizes EDII’s extensive work on legal reforms at the state level and also misstates EDII’s efforts to have the federal government modify existing laws and regulations in order to make the *fideicomiso acreditado* fully operational. The authors do not appear to grasp the importance of making sure state laws address federal laws appropriately. Without this work no transaction could go forward. The section conflates the actions needed to complete the Veracruz restructuring in late 2017 with EDII’s work to ensure that state laws meet federal requirements so that new transactions can go forward.

The discussion of the *Ley de Disciplina Financiera* of 2016 is confusing— the law was established in response to high profile cases of state government corruption (Notably Coahuila and Veracruz). It does, in fact, restrict the borrowing capacity for states and municipalities. All states had to modify their debt laws to reflect the new federal law.

The authors state on p. 24:

“Additionally, there is increased potential for states and municipalities to augment their own ability to collect local taxes as another revenue source. Some can collect a considerable amount of money and take part of the guarantee in the future.

With the aim to identify other potential sources for reliable and steady income for the State governments that could reinforce its credit worthiness, the team asked key informants: “Are there income generating opportunities in local taxes? One answered: “Yes, there are opportunities; it can be an enhanced source.” “[For example], the car ownership tax (Tenencia) should be a main one.” He also warned, “There are deep cultural problems for establishing more taxes (distrust in government’s accountability and transparency in the use of public money).” In any case, he added, “[since] setting up a tax is unpopular, and while revenue streams come from federal taxes in sufficient quantities, the blame for the increase in taxes remains at the federal level, while the use of them is local.”

Mexico's fiscal system is based on the so-called "Pacto Fiscal" among the three levels of government. It is deliberately designed so that states and municipalities share, on a formula basis, in specific federally- collected taxes and other revenues through seven different federally-managed funds. These represent the subnational entities' legal share of specific federal revenues. All transfers are made under the authority of the federal budget, based on contracts or compacts in force with all underlying state and municipal governments (Ramo 28). The sources of the shared revenues are federally collected taxes and fees, including income tax and value-added tax.

Each subnational entity owns these transfers, subject to specific earmarking established under national law. This is reflected in the fact that Mexicans refer to the transfers as *participaciones*. There are several categories of *participaciones*, most of which are earmarked for specific sets of expenditures, including education and public safety.

Own-source revenues at the subnational level are a much smaller share of overall revenues. Under the fiscal pact the largest own-source revenue for municipalities is the property tax. States are permitted to collect car registration fees (*tenencia*) and payroll taxes (*impuesto a la nomina*). States have very restricted own-revenue collection capacity, and in most cases states receive roughly 90% of their operating revenues through the federal transfers. Almost all of the by federal law, only a fraction of the federal transfers to subnational entities may be applied to debt service

Because of the federal earmarks, states have little flexibility with regard to expenditures.

EDII has noted that credit quality is a key barrier to accessing the capital market. Increasing own-revenue collections is important, but these revenues would not enhance the credit quality of the state or municipality. If the municipality or state does not have a stand-alone rating of AA.Mx or higher, pledging own-sources revenues to debt service does not permit capital market access. All of the innovations introduced by EDII through the GDA Program, including the Master Trust, state bond banks, and the Accredited Trust, are structural means of enhancing credit quality for subnational governments. These structures have achieved AA.Mx or higher ratings because the monies transferred from the AAA.Mx federation go into trust accounts, and are not managed by the subnational governments themselves. This is what has permitted expanded capital market access.

We note that Michoacan's action to implement the state payroll tax was a significant new own-source revenue that the authors did not cite earlier in this draft. EDII is aware of a few financings that use either *tenencia* or *impuesto a la nomina* as a primary source of debt service payment, but in all cases also pledge a portion of Ramo 28 transfer. Pledging different revenue streams for the same financing results in excessive costs for the borrowing entity; revenues subject to state control are not considered to be as reliable a source of debt service repayment as federal transfers. Consequently, obligations that are secured by own-revenue sources typically have a lower rating than federal transfers.

Two, the federal government transfers legally belong to the states and municipalities. The formula for transfers is well established and the amount of transfers is guaranteed from one year to the next. The predictability of the federal transfers is part of their appeal to private investors. The fact that subnational borrowers instruct Hacienda to divert part of their transfers to either the Master Trust or the Fideicomiso Acreditado underscores that these monies belong to the subnational

governments under Mexican law. EDII has pointed out to the evaluation team that the creation of the trust structures that stand in front of the borrowers, as opposed to transferring money to state accounts and then to debt service escrows, permits the credit quality of the funds to be higher than the ratings assigned to the states themselves.

The flow of payments into and out of the trust accounts do not in any way prevent the states/municipalities using the structures from pledging own-source revenues in addition to Ramo 28 transfers. But the *nomina* and *tenencia* resources on their own would be insufficient to address the infrastructure borrowing requirements for essentially all states.

b. Capacity Building Achievements

On p. 24 the authors write:

“A 2014 summary power point presentation by EDII on the results of the GDA agreement states that over 1,000 people were trained. The team was not able to verify the number of people trained, however, as no training records were available for review.”

EDII provided training to all state finance staff throughout our work on with subnational governments, in particular both before and after specific transactions closed. There are no training records because USAID did not request them under the GDA agreements.

In addition to our work training state officials and staff, EDII has collaborated with multiple entities on training efforts throughout the period of our work with USAID.

The report does not reflect EDII’s collaborative work with INDETEC (the Instituto Para el Desarrollo Tecnico de las Haciendas Publicas). INDETEC, based in Guadalajara, is an entity jointly funded by Mexico’s Hacienda and by all states, to provide technical services to state finance officials.

The report does not reflect EDII’s diplomado program with IPADE, Mexico’s most prestigious business school. (not UPN).

The authors state on p. 25:

Conclusions:

1) As a result of EDII’s activities, the ability of sub-national (municipal and state) governments to issue bonds or other guaranteed financial products as an option for expanding their credit access at a federal level was secured through supporting the necessary legal reform at the federal level.

2) EDII provided technical assistance and training for officials in the early phases of the agreements, which provided confidence to the investors.

Sentence (1) does not make sense as written. What are “guaranteed financial products?” Do the authors mean financing instruments, such as bonds or structured loans? By introducing replicable structural and legal means to strengthen the credit quality of the proposed transactions, EDII has demonstrated that more entities can meet the credit risk conditions that the market currently requires.

Sentence (2) is incorrect and vastly oversimplifies EDII's work as a financial advisor. EDII provides technical assistance to government clients. Part of this T.A. does include training for officials, but that is not what "provided confidence to the investors." The transactions are evaluated for their credit quality by the investors and by independent credit rating agencies. Banks' reserve requirements are linked to their portfolio of loans, including loans to subnational governments. These transactions must have two independent credit ratings or otherwise are considered to be below investment grade, which means that banks must increase their reserve levels. EDII works to ensure that entities access financing for their projects under the best possible conditions, which include achieving the highest possible credit ratings. That is what makes investors "confident," not the training delivered as a regular part of the EDII's advisory work.

On p. 25 the authors write:

"A 2014 summary power point presentation by EDII on the results of the GDA agreement states that over 1,000 people were trained. The team was not able to verify the number of people trained, however, as no training records were available for review."

USAID did not request that EDII present "training records" as part of any of its GDA Agreements.

RESEARCH QUESTION 3: HOW IS THE EDII ACTIVITY ADDRESSING THE NEEDS OF TARGET BENEFICIARIES? Pp 24-27.

On p. 26 the report refers to: "number of beneficiaries by region"

The report erroneously refers to states as "regions" here and elsewhere.

On p. 26 the authors write:

"Although facilitating financing for clean energy and crime prevention projects was a new objective of the GDA, these projects were slow to come on line. The activity was criticized for not "closing more deals" in energy efficiency and renewable energy arena. Public safety and water management, it was learned from key informants, appeared to be higher priorities at this time. In the last six months of the activity, EDII was working to close two clean energy projects.

EDII is not aware that any "energy efficiency and renewable energy" projects supported by municipal or state debt transactions were completed during the term of the GDA agreement. EDII questions the veracity of the unidentified "key informants" that water management was a "higher priority" at any stage of the final GDA Agreement. EDII doesn't know what "public safety" projects are being included here—could it be the State of Veracruz's decision to use funds liberated from debt service reserve funds following the debt restructuring transaction to purchase a security camera system? If so, this is consistent with the "crime prevention" component of the GDA Agreement.

EDII consistently promoted advancement the projects identified in the pipeline reported to USAID, including the Iztapalapa public lighting project, the Hidalgo waste-to-energy project, and the Coahuila solar park. These did not reach the final transaction stage during the term of the GDA Agreement. The Iztapalapa project is on hold because of Hacienda's determination that lighting

projects are not “productive projects” for the purposes of the *Ley de Disciplina Financiera para las Entidades Federativas y Municipios*.

On p. 26 the authors write:

“EDII’s expertise is in the field of financial services and EDII worked mainly on the financial side to make project finance possible for any type of project. In this regard, EDII’s work in the financial sector has been praised as highly professional and effective. EDII’s had less expertise in the later priority sectors for USAID, clean energy and crime prevention. EDII maintained that increasing clean energy and energy efficiency demand were not areas in which EDII’s had a great deal of expertise, but as important, EDII argued, they were respectful of state sovereignty, meaning that EDII did not push for a specific agenda or type of transaction – such as clean energy – but supported what local governments proposed as projects to be financed.

One approach that EDII adopted to address the interest in clean energy projects was to hire external experts on clean energy as a way to address this objective.

We appreciate the statement that EDII’s work in the financial sector has been praised as highly professional and effective but would like this to be highlighted (See Section I, above).

EDII does not “provide financial services.” EDII is an independent financial advisor. In Mexico as elsewhere, we apply our expertise on financial matters. Governments also hire other firms with expertise in other fields, such as infrastructure design and engineering. These firms have to complete their tasks before final financing options can be evaluated and decisions made.

EDII has been involved in transactions for a wide range of infrastructure projects. Working with sector experts, especially firms that offer design and construction services, is part of our standard practice. EDII’s role is to identify possible financing options, revenue sources, and possible structures and to make recommendations to government clients.

RESEARCH QUESTION 4: HOW EFFECTIVELY IS EDII BUILDING THE CAPACITY OF IMPLEMENTING PARTNERS AND ACTIVITY BENEFICIARIES?

On p. 27 the authors write:

“Conclusions :

- 1) The new tool (bond bank/SPV) that was created under the activity allows State government officials an alternate source of financing for municipal and regional projects, and, if adequately used, it can contribute to satisfying local population’s demands for improved and sustainable municipal infrastructure services.**
- 2) EDII was slow to meet the objectives of the GDA to generate transactions for clean energy and crime prevention projects, especially to meet the objectives of the last three years of the GDA.**
- 3) A major constraint in achieving the above goal is the overriding principle of state sovereignty in choosing the focus of the projects to be financed.**

1). This statement is incorrect. A bond bank is not an alternate source of financing, it is a legal structure, a special purpose vehicle (SPV). The capital market is a source of financing—a bond bank is a means of accessing the capital market at the highest possible credit rating. States execute state projects, either on their own or as public-private partnerships. States do not execute “municipal or regional” projects.

2) This statement is incorrect. EDII as a financial advisor can only proceed with transactions that are ready to go to the market. Financings do not go forward until all of the planning and design work is completed. EDII has assisted multiple entities to obtain “bridge financing” to assist with project development, which is reflected in the supporting documentation that we provided. During the final GDA Agreement EDII convinced the national development bank, Banobras, to establish project preparation loans, which could be ultimately be repaid from bond or loan proceeds.

3) The GDA Program was a) a capital markets project and b) secondarily related to specific types of infrastructure projects. In Mexico as in the U.S., states and municipalities ALWAYS choose the projects that they want to implement based on their policies and their priorities. EDII’s role as financial advisor is to provide comprehensive suggestions that enable subnational entities to structure their debt in a manner that maximizing their flexibility and the ability of future administrations to borrow.

EDII correctly pursued the opportunity to introduce an innovative mechanism that could address barriers to market access, following consultations with USAID. The Veracruz transaction demonstrated the viability of the new fideicomiso acreditado structure and established the legal basis for its use by all subnational governments in Mexico. USAID is aware that EDII worked to advance specific energy projects such as the Iztapalapa public lighting project. This is not go forward during the term of the GDA Agreement because Hacienda issued a decision in early 2018 that lighting projects were not “productive” and therefore could not be debt financed. This decision has been appealed, but essentially all state and municipal public lighting projects have been halted.

States and municipalities are sovereign under Mexican law. Their respective authorities pursue policy goals and identify infrastructure projects essentially the same way their counterparts do in the United States. The Mexican federal government at this time offers no incentive to subnational governments to pursue either energy or crime prevention infrastructure projects.

RESEARCH QUESTION 5: HOW DOES THE ACTIVITY SUPPORT THE OBJECTIVES OF MEXICO’S ENERGY REFORM?

On p. 28 the authors state:

“The major goals of the Mexican energy reform were to:

- 1. Open the energy sector to a variety of participants**
- 2. Reduce the cost of energy services “**

This section is missing significant information, as outlined in Section II, above.

EDII did assist the State of Veracruz with the creation of its state energy agency, which is charged with exploring alternative energy and energy efficiency opportunities.

RESEARCH QUESTION 6: WHAT CAN BE ACHIEVED BY THE END OF PHASE 5?

The report misstates EDII's determination that establishing a national bond bank during the course of the GDA Agreement was not feasible. Although stakeholders agreed that such an SPV could be beneficial, no entity or institution stepped up to host this administratively. Consequently, EDII considered other options to achieve similar results, and the firm developed the concept of the *fideicomiso acreditado*. This legal structure was successfully introduced in the State of Veracruz debt restructuring transactions, completed with the support of USAID, and is now legally available to all states and municipalities in Mexico as a means of accessing the capital market, whether or not their respective states have established bond banks. The two legal structures are complementary.

RESEARCH QUESTION 7: DID USAID INVOLVEMENT ENHANCE MEXICO'S DEVELOPMENTAL OPPORTUNITIES, AND PARTICULARLY IN LOCAL GOVERNMENTS' ACCESS TO FINANCIAL MARKETS?

EDII values its partnership with USAID. Multiple Mission Directors and Ambassadors and other Embassy officials have supported the GDA Program over the years. We appreciate their direct involvement, helping our subnational government partners to demonstrate to constituents that they are engaged in a respected international program. We have always respected USAID's organizational objectives and we have responded to opportunities to meet with USAID and Embassy contacts and partners.

The GDA partnership presents a guarantee of transparency. This coincides with our firm's ethics. We provided the evaluation team with examples of how corrupt individuals attempted to extort or threaten the firm, and cited the relationship with USAID as a key factor in thwarting these efforts. In one specific case, after providing detailed work product to a state finance secretary, another part of the state administration fired that secretary and EDII, claiming that our firm failed to deliver materials promised. EDII was able to state categorically that the materials had, in fact, been delivered to the state because duplicate materials were delivered to USAID simultaneously.

On p. 29 the authors write:

"...USAID was linked to the informal Mexican Association of Secretaries of Finance, and also to the much more formal body in the U.S. linked to the U.S. Treasury. USAID was able to make the link between these two groups, which was helpful. The Mexican Association of Secretaries of Finance in Mexico has an annual meeting and they invited US association members, which gave increased credibility to EDII's work."

As Elizabeth Bauch explained to the evaluation team, the relationship between U.S. state treasurers and Mexican state finance secretaries was developed as a complement the EDII activity and a means to highlight best financial management practices. Initially the finance official engagement was an activity under the good governance contract with Casals, and later through a cooperative agreement with the Sacramento-based Council of State Governments. This activity with the National Association of State Treasurers (NAST) was one of several efforts to link Mexican state officials to their U.S. counterparts, including state attorneys general (with the Conference of Western Attorneys General, CWAG), building on the successful experience of the Border Legislative

Conference that brings together legislators from the U.S. and Mexican border states. The Mexican Association of State Secretaries of Finance is not an “informal” organization; it links all state financial officials to Hacienda.

USAID arranged a series of breakfast events at the Club de Banqueros in Mexico City, featuring a U.S. and a Mexican state finance official as speakers. EDII was able to introduce some of their clients to U.S. officials who had deep experience in the U.S. public finance markets, including with bond banks. EDII arranged for several individuals to travel to NAST conferences in the U.S. and to various states to meet with government finance teams. NAST members were invited to Mexican Association of Secretaries of Finance Events and participated as speakers. INDETEC supported and participated in the state treasurers’ program. EDII took advantage of the opportunity presented by the state finance officer activity to introduce Mexican government clients to U.S. state officials whose states used bond banks to help underlying municipalities

On p. 29 the authors state:

“One significant example was a project with the Government of the State of Michoacán and EDII in which the results of the project were key to the finances of the State and in general for the country, since it successfully executed a transaction model whose interception of cash flows has been replicated by many States and municipalities in Mexico over the last 15 years. The transaction saved the state millions of dollars and empowered the municipalities with a record low cost financing for municipal infrastructure. “

This is a cornerstone achievement of the GDA Program and should be highlighted. The introduction of the revenue intercept mechanism, now known as the Master Trust, has helped to transform Mexico’s capital market and significantly increased access to private capital by states and municipalities. The Master Trust opened access to states and municipalities by providing a means to intercept revenues from the national government and direct them into a restricted trust account for debt service payment. This structure has consistently received AA.Mx or higher credit ratings.

This legal structure has had a measurable impact. According to the National Registry of Public Debt, as of June 2018 some \$24.5 billion of the total \$27.2 total outstanding debt of states and municipalities—all the debt secured through federal transfers-- featured one or more of the legal mechanisms introduced by EDII under its partnership with USAID.

The initial transaction using the Master Trust was a \$150 million structured loan. This represented the first time a state obtained bank financing at an interest rate below 10%. Interest cost was not the only element of this transaction that resonated in the Mexican capital market. The structured loan that the state obtained marked the first time in Mexican history that a state was able to obtain a loan agreement that extended for 10 years. Prior to Michoacan, banks –mainly government banks- lent money to states only through the term of the sitting governor, if at all, because they considered the political risk of debt repudiation as a serious possibility.

EDII worked with the state to put in place the legislation needed for the state to access private capital under the best possible terms at the time. This included updating the state’s debt law, which had been in place, unchanged, since 1929—long before the modernization of Mexico’s banking and

capital market oversight regime. EDII developed the Master Trust (*fideicomiso maestro*), a mechanism through which Michoacan was able to deviate a small portion of its federal transfer revenues (legally available under Ramo 28) to a trust account held by a third party –a private financial institution properly registered by the CNBV, the federal agency that regulates banks and the capital market.-, which was used for debt service repayment. This was the first time in Mexican history that a state was able to formally request that its federal transfers be “intercepted” by an independent trust account, and this helped to transform the market. The Master Trust structure has been used by multiple subnational entities with and without EDII technical advisory assistance; to date it has been used for approximately \$40 billion of transactions.

On p. 29 the authors write:

“ The work expanded and achieved more visibility with USAID as a partner, as it was then perceived as a driver for a systemic change and not only isolated efforts by a new player in the financial markets, as EDII was when it began in 2002.”

This is a key characteristic of the EDII-USAID partnership: it is a development program, not a business opportunity for a single private company. This should be highlighted in the final evaluation report.

RESEARCH QUESTION 8: IS THE ACTIVITY DESIGNED AND IMPLEMENTED IN A WAY THAT ONCE USAID LEAVES THE ACHIEVEMENTS REMAIN AND ARE CONSOLIDATED?

On p. 31 the authors write:

“Interviews with project developers in the area of waste-to-energy and clean energy, who were engaging with EDII to complete financing for projects, revealed that there was some loss of reputation on their part for EDII as a result of their interactions. The developers expressed a loss of trust and increased uncertainty about the prospect of completing the financial transaction for their project after their interactions with EDII. One company reported frustration that EDII’s commitment on financing has not been delivered yet. An official of a fourth company expressed disappointment with the process and withdrew from the project.

The local private sector appears to be turning to alternate sources of financing and away from collaboration with EDI. Mexican firms are gaining market share and appear to be taking the place of EDII. This in turn may undermine the spirit of the GDA that is endeavoring to create partnerships and encourage private sector engagement in the development agenda.

The statement that “One Company reported frustration that EDII’s commitment on financing has not been delivered yet. An official of a fourth company expressed disappointment with the process and withdrew from the project.” Is not valid for two reasons: (1) EDII suspects that the reference to “loss of reputation” is directly tied to the individual cited in our cover letter, who attempted to extort payment from our firm in exchange for a positive evaluation. (2) Under Mexico’s laws

government public investments by states and municipalities, the clock starts running on a project finance timeline only after the state legislature formally approves the projects and its financing, and authorizes officials to initiate the RFP process to achieve the financing. At this time the government entity officially publishes its financing timeline and milestones. Prior to this state, private developers and government authorities must invest in developing the project design and engineering files and in applying for the necessary permits that are a foundation for state legislative action. Projects that do not meet all legal and technical requirements are not submitted to the state congress for authorization. In some cases, government authorities determine not to proceed with a project for their own policy or political reasons. EDII has no control over the completion of project design and engineering files, and is not a party to any permitting process. EDII is also not responsible for project advancement or cancellation decisions made by government clients.

The process for developing projects that are ready for financing relies on many factors, most of which are under the control of the developers themselves or other private entities. For energy projects specifically, obtaining the necessary permits from government authorities can take many months or even more than a year. No project can obtain financing without reaching the final permits stage. Therefore, EDII cannot “deliver financing” for projects that are not ready for presentation to the capital market.

EDII strives to maintain the highest ethical standards, with or without a partnership with USAID, and the firm does not take shortcuts. During the course of the GDA Program EDII always sought to comply with Mexican laws and regulations, and to push for modifications in these where appropriate to ensure the best possible conditions for borrowers and investors. This included incorporating modifications to public-private partnership laws. The authors do seem to take the opinions of the private sector companies reported here at face value instead of asking additional, appropriate questions.

As stated in Section II, EDII is not aware of any state or municipal energy projects that obtained financing during the period from 2015-2018.

On p. 31 the authors write:

Conclusions:

- 1) Yes, the activity was designed and implemented in a way that makes it self-sustaining overtime.**
- 2) Local governments have the option for expanded access to financial markets.**
- 3) There are still tasks to be done to consolidate the achievements, but the current outcomes will remain and improve.**

EDII agrees with these observations.

RESEARCH QUESTION 9: WHAT SHOULD BE HIGHLIGHTED TO REPLICATE THIS MEXICAN EXPERIENCE IN OTHER COUNTRIES?

On p. 32 the authors write:

USAID is not the U.S. Treasury. USAID is not a partner with any country's finance ministry. Therefore, there is a limited niche for what USAID can offer. The Mexican experience can show where the niche is.

This is an important statement and should be highlighted in the final evaluation. EDII believes that USAID is in a unique position to support technical assistance to advance transparent, responsible subnational government borrowing through domestic capital markets without the application of a guarantee mechanism using sovereign resources. EDII through the GDA Program did not attempt to change national monetary and fiscal policy objectives, but it sought to create opportunities for increased subnational government participation in the market.

This kind of program works from the bottom up — making sure that states and municipalities have their legal foundations in place, consulting with investors and other market stakeholders to understand their concerns and objectives, and ultimately delivering transactions that are appropriately structure and which may be replicated by other entities.

On pp. 32-33 the authors write:

INVESTMENTS IN CLEAN ENERGY AND CRIME PREVENTION: NOT ACHIEVED

The creation of bond banks/SPVs has the capacity to contribute in enhancing the development possibilities opened by the energy reform. To date, there is little evidence of direct investment in energy efficiency and renewable energy projects using the bond bank/SPV vehicle. In the last phase of the activity, EDII placed secondary emphasis on the GDA objective of promoting clean energy and crime prevention and instead focused on restructuring of Veracruz's debt, although an outcome of the Veracruz debt restructuring was the creation of a crime prevention fund and over time, more investments may be seen as a result. With greater oversight, USAID may have been able to better steer program activities to better meet USAID and the GDA's objectives. EDII.

EDII has overlooked the waste-to-energy pipeline, with unclear support for projects. EDII's uneven performance in this sector has generated a reputational cost (a poor reputation) for them and for USAID within the Mexican waste treatment industry."

Please see our discussion of the impact of Mexico's Energy Reform and the opportunities these reforms created for states and municipalities in Section II. Mexico established a new and complex legal and regulatory framework to open the country's energy markets. While federal entities such as Pemex and CFE have completed transactions for new energy-related projects, states and municipalities lag. EDII is not aware of any state or municipal energy projects that completed financing transactions.

In order for any project to obtain financing through capital markets, a number of conditions must be in place. In response to the cases of extreme corruption presented by certain states, most notably Veracruz, the Mexican government focused on preventing similar abuses instead of on promoting the development of new energy projects. The Law of Fiscal Discipline specifically only allows states

and municipalities to borrow for “productive” projects, subject to approval by the Secretariat of Finance. While several projects were advancing in the GDA program pipeline, once the Finance Secretariat declared that a public lighting project for the municipality of Zapopan, Jalisco (not a GDA program client) could not be financed with debt, most of these projects have halted.

EDII has worked on a number of projects that did not finalize financing transactions throughout the course of its history as a firm. Many U.S. projects that were pursued by as public private partnerships were not completed. There are a number of reasons why projects do not move forward, but EDII always collaborates so long as stakeholders work together in good faith, for shared objectives.

On P 33 the authors write:

SATISFYING BENEFICIARIES: PARTIALLY ACHIEVED.

The services provided by EDII satisfied the local government demands; nearly 28,000, 000 residents in five Mexican states, were reached through the projects. However no data were available to describe how these reforms have contributed to satisfying local citizens’ demands/needs.

What is the methodology used to determine how reforms contributed to the satisfaction of citizen demands/needs? EDII suggests that assisting states and municipalities to obtain financing for priority infrastructure projects is a means of promoting good, transparent governance.

On p. 33 the authors write:

SUSTAINABILITY OF ACTIVITY RESULTS: ACHIEVED.

Activity results will be sustained over time as the legal reforms have been made and are unlikely to be undone, and subsequently financial transactions have been closed in four states. There are still tasks to be done to consolidate the achievements, but the current outcome will remain. The case of Veracruz restructuring debt probably will promote the bond bank / SPV tool among other Mexican States.

However, there are other financial service providers working in this market, private Mexican Financial Institutions that offer support for waste-to-energy projects.

EDII agrees that the Program results to date are sustainable, but the evaluators need to explain this more clearly. The results are sustainable because the mechanisms introduced and applied are replicable. EDII clients have used the bond bank mechanisms without EDII oversight, and we have already noted that the Master Trust intercept structure has been embraced as the market standard for subnational borrowers. EDII believes that the Program achievements are sustainable because market regulators and investors can be expected to continue to demand high credit quality, to maintain the integrity of Mexico’s financial markets.

The Program has demonstrated that laws, regulations, and even state constitutions can be amended; there is no guarantee that future administration won’t seek changes.

As for “private Mexican financial institutions” supporting waste-to-energy projects, EDII notes that any project can be financed if cost is no option, and if maintaining the financial flexibility and credit quality of the subnational partner is forsaken in the pursuit of one-time profits or gains. Like the U.S., there are unscrupulous actors working in Mexico to promote projects for their own self-interest, which may or may not coincide with the best interests of subnational governments.

We also suggest that the authors talk with capital market regulators and stakeholders to learn how Mexico’s capital market operates and what conditions borrowers must meet in order to qualify for access to this market.

On p. 34 the authors write:

“EDII’s behavior confirms that the pipeline was neglected until the last few months of the activity when reported and presented evidence that they were focused on closing two potential clean energy projects.”

This statement is false. EDII did not “neglect” a pipeline. Financial work had proceeded to an appropriate point pending additional decisions and determinations by other entities. As noted above, projects cannot be financed until they have obtained the necessary permits and are formally authorized by a state’s or municipality’s legislative body.

The draft report statement is misleading for two reasons. One, the pursuit of the Veracruz transactions that would introduce the *fideicomiso acreditado* was authorized by USAID because this was a means of establishing a legal SPV mechanism that would be available to states and municipalities throughout Mexico, making it the equivalent of a Mexican national bond bank. Two, EDII’s work with Veracruz did not in any way interfere with or prevent energy project transactions. Other factors were involved, notably Hacienda’s determination that new LED public lighting systems do not meet the criteria for “productive projects” as defined by the *Ley de Disciplina Financiera*. Hacienda’s determination has halted multiple public lighting projects, including that of Iztapalapa. EDII expects these to go forward if Hacienda reconsiders this decision, which could reasonably occur with the change in government later this year.

LESSONS LEARNED

On pp. 34- 35 the authors write:

“OWNERSHIP An activity like the USAID/EDII partnership totally depends on the local governments’ and stakeholders’ will to make it work. It takes time to build the proper environment for a successful activity—to start identifying stakeholders, evaluating the market, determining barriers, exploring and offering potential solutions. Further, finance is always a very sensitive area at any level. Its management entails responsibility, respect for fiduciary duties, and managing risks even when the best intentions guide decision-making. Financial matters also have high political visibility. Consequently, Governors and Secretaries of Finance move very cautiously and are risk adverse. Innovation in local public finance is not their priority; they prefer to move within traditional practices.

Entities that can access financing may or may not care about the conditions for that financing. It is clear that many elected and appointed officials do not understand capital markets or why costs, transparency, and accountability is important.

However, EDII has seen time and again that incoming administrations are always interested in pursuing their own projects and are frustrated when predecessors have tied up future resources. Best practices and the judicious use of mechanisms like the Master Trust and now the Accredited Trust can help unlock borrowing capacity.

Supporters of the objective of this GDA Program include key capital market stakeholders, including private investors who want to invest in long-term instruments that have high credit quality. Market diversity is a positive feature for both borrowers and investors. Any effort to pursue a similar project elsewhere should include partners that have extensive knowledge and experience with capital markets, who can interact effectively with all market stakeholders.

“RESISTANCE Opening a new frontier for finance challenged the “business-as-usual” approach. There are sectors of local governments’ staff and some banks that benefit from the status quo and vested interest in the federal government that were uncomfortable or negatively impacted by the change.

The evaluation should expressly state that the GDA Program promoted transparency and accountability, which threatened corrupt interests at all levels of government.

“INSTITUTIONAL INERTIA Both at the local and at the federal level, a legal reform faces challenges for institutional adjustment, management styles and culture. People are adverse to innovation and risk.

EDII believes that this GDA Program has clearly demonstrated that people and institutions welcome innovations that help them address real problems. The innovations and best practices promoted by the USAID and EDII partnership require a lot of effort and commitment from subnational governments. Institutions that are not facing problems in accessing finance are less likely to embrace change for its own sake.

The draft evaluation report does not highlight the strong investor response to the innovations that EDII has introduced during the GDA Program. This obscures major achievements of the Program. Accessing finance is only possible when investors embrace the innovative structures that are introduced. The ratings assigned by multiple credit rating agencies provide independent confirmation that the new mechanisms address key risk concerns; but ultimately the fact that so many investors have engaged in these transactions with subnational governments is evidence that

HOW CAN USAID BUILD ON EDII’S SUCCESS AND WEAKNESSES TO ENHANCE THE POTENTIAL FOR IMPACT IN ONGOING AND FUTURE SIMILAR INITIATIVES? (p. 36)

EDII recognizes that the recommendations are the Palladium Group’s work product. However, given the key deficiencies of the draft report we believe that the recommendations of a team that included individuals with knowledge and experience of capital markets would be of greater value to USAID.

Case Studies- Hidalgo, Quintana Roo, Michoacan.

p. 37

The case studies should be reviewed for English accuracy and readability.

p. 48

“The Michoacán financial transaction was innovative since it used this model for the first time in Mexico, by using an irrevocable private trust. This type of administration and payment trust intercepts cash flows from the Federation to the State, and prior to those entering the state treasury. In this way they maintained their credit quality of AAA.mx, and committed to the payment of future financial obligations. The Michoacán case, and the financial mechanism used, became the public funding standard in Mexico, and today, 15 years later, it is still valid and has allowed the State to mobilize more than MX 580 billion of Mexican pesos (equivalent to more than \$ 31 Trillion Dollars) for the development of productive public projects by sub-national entities in Mexico.

The amount of \$31 Trillion is incorrect. According to SHCP records, as of June 2018 the total amount of subnational debt in Mexico, including both long-term and short-term obligations, is \$27.2 billion. The total volume of long-term obligations secured using the Master Trust mechanism introduced with the Michoacan transaction is the peso equivalent of \$24.5 billion. The entire U.S. public finance debt market is roughly \$6 trillion.

Again, the Master Trust structure was a major achievement of the GDA Program. This innovation has helped multiple subnational governments access the capital market by allowing the funds placed in a restricted trust for debt service to retain the higher credit quality of the Mexican federal government. This should be highlighted by the evaluation.

ATTACHMENT 2: FEBRUARY 19, 2019

Attachment 2- SPECIFIC EDII OBJECTIONS February 19, 2019

EDII objects to the language used in the following segments of the latest draft evaluation report. All page numbers refer to the draft dated November 15, 2018.

p. viii

The work of the last years of the activity restructured the debt for the state of Veracruz, but did little to accomplish the specific objectives of the final agreement to finance projects focused on clean energy and crime prevention.

The Veracruz transaction introduced a new special purpose financing vehicle, the Accredited Trust, to Mexico. For the purposes of Mexican states and municipalities, the Accredited Trust functions like a bond bank.

As EDII states in our letter dated February 19, 2019:

1) **During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV).** The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

2) **EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period.** According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

p. x

A private sector partner and the U.S. Government have many coincidental interests; however, at some point, these can diverge. When the USAID-EDII agreement changed in 2015 to emphasize work on clean energy and crime prevention, which meant more focused work by EDII in the generation of an adequate and bankable pipeline of projects, there was a divergence of strategic interests.

This allegation is false. EDII pursued the objectives of the GDA partnership with USAID throughout all agreements. EDII discussed that the modifications to the Energy Reform in 2016 generated new requirements and opportunities for subnational governments and noted that the reform objectives were not supported by the legal framework for subnational borrowing in our comments dated September 25, 2018.

As EDII states in our letter dated February 19, 2019:

1) **During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV).** The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited

Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

2) EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

p.x

Further, USAID management would have benefited from having a deeper understanding of the complexity of the Mexican financial markets and political priorities that led local governments in this period to prioritize financing for other infrastructure projects unrelated to crime prevention and clean energy or chose traditional financing over the BB.

As noted in our comments dated September 25, 2018, neither EDII nor USAID sets the priorities for elected officials at any level of government.

pp. 1-2

The purpose of the evaluation was to provide a direct assessment of the work undertaken during the last few years of the activity, focusing on the types of transactions completed in this period through bond banks, within the context of the original objective.

The authors ignore the key achievement of the activity, the creation of the Accredited Trust SPV.

As EDII states in our letter dated February 19, 2019:

1) During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV). The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

2) EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

p. 4

The context was clear. The power swing in the country definitively was going to favor local governments seizing more autonomy and the financial aspect was crucial for its success. Despite the potential obstacles, this financial niche market was headed towards growth. The long-term strategic orientation indicated this opportunity was an inevitable pathway for Mexico, and the alliance between USAID and EDII could accelerate this transition and produce positive outcomes for all. EDII was not trying to leverage U.S. government funds, but rather using the partnership with the U.S. government to leverage private sector resources.

A constant objective throughout multiple agreements with USAID was to expand subnational government access to private investment through Mexico's capital market.

USG resources supported the technical assistance provide by EDII, and during the GDA phases USAID funds were matched by EDII and other implementing partners. The implementing partners, primarily Mexican states, contributed their resources by paying for the services of multiple financial service providers (specialized legal advisors, credit rating agencies, paying agents, trustees, mandatory public notices and other associated costs).

All financing transactions were completed in public, in full compliance with national laws and regulations in place at the time, and in fully compliance with state laws. With the sole exception of Mexico's subnational development bank, BANOBRAS, all potential investors participating in capital market transactions are private.

Table, p. 7

2015-2018		
Federal various municipalities	government, states and	

Set up an SPV under an Accredited Trust structure, a financial model similar to a bond bank. (State of Veracruz - \$2 Billion). The third party receives and holds the federally transferred funds, not the subnational entity; the third party transfers the resources to the entities or invests on their behalf. The PPP law was created in several states to structure projects and access financing using the SPV-Accredited Trust. However, concentrating on Veracruz distracted EDII's efforts away from USAID GDA priorities (clean energy and crime prevention projects).

This highlighted statement is false. EDII was not “distracted” away from USAID GDA Agreement priorities.

As EDII states in our letter dated February 19, 2019:

1) During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV). The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

2) EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

III. The Development of the Mexican Bond Bank

pp. 12-13

The trust account that holds these federal transfer funds can be an Accredited Trust, a

Master Trust structure or an institution, and in all cases it needs to be transparent and accountable to the local legislative body. The Master Trust—a mechanism whose introduction can be attributed to EDII’s work on developing the necessary legal framework—is available to all subnational entities in Mexico. EDII estimated that USD \$40 billion in state and municipal debt is now secured through a Master Trust structure (Annex X. EDII Response to Draft Evaluation, p. 25). By definition, the trust account needs to be created by a local law. A trust (Master or Accredited) at the federal level is its equivalent and requires the trust management to report on the transactions, which are also transparent, to the local authorities. These legal frameworks and financial mechanisms address credit concerns and increase the potential for attracting investors, thus creating greater competition. Bond bank transaction ratings to date have been higher than the stand alone ratings assigned to the states in which they were established (Annex X. EDII Response to Draft Evaluation, p. 21).

Neither the Master Trust nor the Accredited Trust is a “trust account.” The first is a revenue-intercept and debt repayment mechanism utilized by a subnational borrower; the second is a special purpose financing vehicle. Both the Master Trust and the Accredited Trust utilize multiple “accounts.”

As EDII states in our letter dated February 19, 2019:

1) During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV). The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

2) EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

p. 14

A representation of the way infrastructure finance was organized prior to the EDII/USAID Activity is presented in Figure 1. The differences in the structure of financial mechanisms after EDII’s work is completed is represented in Figure 2. In the

first model (Figure 1), financial resources flowed from the federal government to the state, and the governor was the main political person responsible for its use; the local Secretary of Finance was the responsible administrative official.

pp. 15-16

The diagrams included on these pages are incorrect.

p. 17 It took a long time to make the required changes to support SPV development. This apparent inefficiency was due to the technical and political complexities of the project, as the legal engineering required was highly innovative and many local governments were reluctant to change unless the situation was very favorable for it. An additional obstacle was Mexico's slow political processes. All state governors work both locally and nationally so the agenda moves accordingly with different election rhythms.

This qualitative descriptor should be removed. There is no basis for asserting that there was an “apparent inefficiency” in this development project.

p. 18

-Change in the federal government's approach, with the appointment of a new Finance Secretary in 2012, who aimed to recentralize financing and which created conflicts of interest. As a result, financial advisory firms were barred from working with state and municipal clients. EDII had to look to private firms seeking to develop PPP projects related to crime and prevention

See EDII's September 25, 2018 comments on the previous draft evaluation report. EDII noted that corruption has been an obstacle to work under its partnership with USAID and cited the fact that the Finance Secretary verbally directed states to work ONLY with a financial advisory firm in which he held a financial interest.

p. 19

During this phase, a new administration came into power and the incoming Federal Minister of Finance adopted new rules that stopped any further progress on bond banks. All local financial reforms and transactions would be dealt with by the firm where the new minister used to work—a major conflict of interest (confirmed by all the interviewees). After some efforts to continue working as before had failed, it was clear that other tasks should be undertaken.

See EDII's September 25, 2018 comments on the previous draft evaluation report. EDII noted that corruption has been an obstacle to work under its partnership with USAID.

These sections on pp. 18 and 19 of the draft report refer to a “conflict of interest.” The Secretary in question did not “adopt new rules” (which would create a written record) or simply

“recommend” a particular firm, he directed states to work exclusively with that firm. EDII sees this as an example of corruption during the prior presidential administration (2012-2018) that had a negative impact on the GDA activity.

This verbal instruction prevented EDII from working directly with state governments until a new Finance Secretary was in place.

p. 19

In mid-2016, with a change in political leadership, EDII began working with officials in the State of Veracruz (SoV). From this point on, EDII focused the majority of its time and resources to solving the debt crisis in SoV. The work in the State of Veracruz was a significant deviation from the objectives, which were to focus market access to further finance USAID/Mexico’s priorities. Further, the work did little to accomplish the specific objectives of the final agreement to finance projects focused on clean energy and crime prevention.

In our comments dated September 15, 2018, EDII explained that the firm recognized that assisting Veracruz presented a key opportunity to establish a new special purpose financing vehicle that would expand capital market access for subnational governments. EDII consulted with USAID before committing to work with Veracruz.

As EDII states in our letter dated February 19, 2019:

1) During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV). The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

2) EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

EDII claimed credit for money devoted to a crime prevention fund established by the State of Veracruz that was available as a result of the debt restructuring. The crime fund fits within the topic of crime prevention, which was part of EDII’s agreement with USAID.

This statement is not true; EDII did not “claim credit.” The firm reported the amount that was made available for crime prevention projects by the State of Veracruz thanks to the debt restructuring transactions. The state documented that it had in fact budgeted this amount to this purpose.

p. 19

While EDII acknowledged that the SoV work was a major distraction from the specific objectives listed in the final extension, EDII personnel noted that the SoV was immersed in a critical financial crisis and in a very delicate political situation. All the eyes of the nation turned towards this case and EDII engaged in a drive to complete a dramatic restructuring of a debt of around USD \$2 billion.

This statement is not true and should be removed. The work with Veracruz resulted in the full legal implementation of the Accredited Trust SPV.

As EDII states in our letter dated February 19, 2019:

1) During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV). The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

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p. 20

The EDII staff offered three reasons to argue the relevance of expending these into this case. One reason was that the national attention and impact that such a high transaction, were it successful, would have could highlight the relevance of using the Accredited Trust structure (fideicomiso acreditado) for better management of state debt. EDII helped introduce this structure as a new and nationally applicable SPV, and, the EDII staff noted, it is effectively a national bond bank, the creation of which was an objective of the original GDA agreement (Annex X. EDII Response to Draft Evaluation,

p. 28). The second reason was that obtaining better credit conditions in a very difficult case would show others the benefits of this new scheme for any purpose. A third reason is that it was potentially consistent with crime prevention work dictated by the agreement with USAID.

In our interviews with the authors and in our comments dated September 15, 2018, we noted that EDII saw Veracruz debt crisis as an opportunity to introduce a new special purpose financing vehicle in part because this crisis presented a dilemma for the federal government. Allowing the state to suffer through cascading defaults would impact all creditors and could potentially freeze new lending to subnational governments. Providing any cash advance to avert a cascading default scenario would contradict the policies that have effectively separated Mexico's sovereign credit standing from that of underlying states and municipalities. Any new SPV would require modifications in national law and regulations, and therefore it was important to work on a transaction that coincided with the political objectives of the federal government. Without the debt restructuring the new state administration would have no resources for its crime prevention program. EDII explained this to USAID and it was determined that EDII should work with the state under the GDA partnership.

As EDII states in our letter dated February 19, 2019:

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2) EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

p. 20

2) The SoV case was considered successful by EDII because its national visibility helped adverse political parties understand that an SoV bankruptcy would not benefit anyone.

The Veracruz transaction(s) were successful because the state received the funds needed to

restructure its debt. The transaction(s) also accomplished the introduction of the Accredited Trust SPV, which represented a key achievement for the USAID-EDII GDA program.

As EDII states in our letter dated February 19, 2019:

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p. 20 The work of the last three years of the agreement was a deviation from the new objectives included in the final GDA agreement between EDII and USAID.

This statement is not true. The work during this period reflected EDII's efforts to adapt to market conditions and the national legal environment in order to pursue GDA Agreement objectives. The authors even refer to the pipeline of energy and crime prevention projects that EDII worked with. (Draft Report dated November 15, 2018, p. 21).

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public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

p. 21

In Phase Five, it appears that Evensen Dodge focused more attention on activities that would create future business opportunities within the private sector rather than on fulfilling its obligations to USAID as agreed to in the GDA. EDII participated in developing a pipeline of projects related to energy and crime reduction, including the Iztapalapa public lighting project, the Hidalgo waste-to-energy project, and the proposed Coahuila solar park, amongst others. These projects remain in process or pending for reasons unrelated to EDII's work under the GDA Agreement.

The highlighted statement is false and should be removed. EDII fulfilled its obligations under the GDA partnership Agreement with USAID. The statement that the energy projects remain pending for reasons unrelated to EDII's work under the Agreement is correct.

As EDII states in our letter dated February 19, 2019:

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p. 21

This most critical and binding reform came with the issuance of the “Ley de Disciplina Financiera de las Entidades Federativas y los Municipios” (Financial Discipline Law of Federal Entities and Municipalities) in April 2016. The law was created by combining different elements contained in other (previous) fiscal legal instruments with new elements.

The authors appear to imply that EDII was involved with the drafting and adoption of the Ley de Disciplina Financiera. That is not the case.

p. 21

Prior to joining in a partnership with USAID/Mexico, EDII had already engaged in the task of generating change in the Mexican financial markets to enhance access for local governments. When USAID agreed to support EDII's work, EDII's role was substantially improved. Having the support from a major development actor in Mexico enhanced public trust in EDII's work. USAID was viewed as an influential partner and some U.S. Ambassadors appeared in EDII's work: related meetings with Mexican authorities and other stakeholders in the early years of the Activity.

Both USAID and EDII benefitted from this development partnership. The underlying purpose of the partnership was to expand subnational government access to capital market financing. USAID officers accompanied EDII to meetings with state and local officials from time to time over the course of 16 year partnership. One U.S. Ambassador, Carlos Pascual, introduced EDII to cabinet officials during the Felipe Calderon administration, noting that the firm was as a USAID partner in this GDA project. From time to time senior USAID Mission officials and various U.S. Ambassadors participated in events that celebrated the achievements of specific state administrations. None "appeared" in EDII's work.

p. 26

Public safety and water management, it was learned from key informants, appeared to be higher priorities at this time. For example, in the State of Quintana Roo, officials pooled financing for water and sewer infrastructure, specifically to provide maintenance and expand its systems to satisfy the growing demands of the population. New drinking water infrastructure benefited 77,012 inhabitants. New sewer and sanitation infrastructure benefited 146,879 inhabitants.

The authors are apparently referring to the Quintana Roo bond bank transaction in support of the state's water and sewer utility, CAPA. The CAPA transaction occurred in 2007. EDII was not involved with any financing by the State of Quintana Roo during the period of the most recent GDA Agreement (2015-2018).

p. 27

EDII's expertise is in the field of providing financial advisory services and EDII worked mainly on the financial side to make project finance possible for any type of project. In this regard, EDII's work in the financial sector has been praised as highly professional and effective. EDII had less expertise in the later priority sectors for USAID—clean energy and crime prevention. EDII maintained that increasing clean energy and energy efficiency demand were not areas in which it had a great deal of expertise. Just as important, EDII argued, they were respectful of state sovereignty and did not push for a specific agenda or type of transaction—such as clean energy—but supported what local governments proposed as projects to be financed. One approach that EDII adopted to address the interest in clean energy projects was to hire external clean energy experts.

EDII has significant expertise as a financial advisor to subnational governments and works across all government infrastructure sectors. EDII makes recommendations regarding financing options to government clients, and government officials determine if and when they pursue specific projects and transactions. EDII's advisory services in Mexico focus solely on public finance matters.

No financial advisory firm in Mexico has experience in successfully financing energy projects owned by subnational governments because these were only enabled by the Energy Reform of 2016. Because the National Law of Financial Discipline has not been modified to enable financing subnational energy projects, no financings have taken place to date.

p. 27

EDII was slow to meet the objectives of the GDA to generate transactions for clean energy and crime prevention projects to meet the objectives of the last three years of the GDA.

This qualitative statement about EDII being “slow” is incorrect. The authors imply that there's a standard timeline for introducing capital market innovations and that transactions that were ready to go to the market were left undone.

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p. 28

One solution that would guarantee more stability for highly professional and skilled staff in this financial arena would be to create an institutionalized bond bank (an

autonomous institution that is independent from the state government and the state parliament), with state of the art organizational and labor standards.

This statement summarizes why EDII's initial effort focused on establishing a national bond bank. However, as noted in our comments dated September 25, 2018, no federal government entity was willing to sponsor and host this kind of SPV during the 2015-2018 period of the most recent GDA Agreement.

As EDII states in our letter dated February 19, 2019:

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pp. 28-29

The legal reforms and additional mechanisms providing financing to states and municipalities has opened the possibility for growth in clean energy projects. Some state governments proposed and developed energy projects, even prior to the final GDA agreement, specifying this as a priority goal.

As noted on p. 21 and elsewhere in the draft report dated November 15, 2018, EDII worked with several entities that sought to develop clean energy generation projects and to replace old system with energy efficient public lighting. The National Law of Financial Discipline sets the conditions under which states and municipalities may borrow; it has not been amended to address financing for the energy projects that were enabled under the 2016 Energy Reform. No subnational energy projects have been financed during the period of the most recent GDA Agreement (2015-2018).

As EDII states in our letter dated February 19, 2019:

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p. 29 The potential for generating clean energy projects exists, through relatively few have been developed to date. EDII sees these approaches as opportunities to continue expanding their portfolio.

The authors do not cite any examples of subnational energy and/or crime prevention projects that were financed during the GDA Agreement period because none exist.

As EDII states in our letter dated February 19, 2019:

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2. Once EDII completed the highly visible case of restructuring the debt of the State of Veracruz, EDII turned back to the clean energy agenda. However, it was too late to close a transaction on clean energy before the end of the Activity in July 2018.

EDII is fully capable of working with multiple clients simultaneously to help them meet their financing objectives. We outlined the reasons why no subnational energy projects have been financed in our comments dated September 25, 2018.

As EDII states in our letter dated February 19, 2019:

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p. 30

One important question that emerged during the evaluation was “Why have no additional bond banks been established since the two existing banks were created in 2006, 12 years ago?” Three main factors appear to be constraining the development of additional banks: institutional inertia, the political support needed to create a bank, and concerns raised by EDII’s somewhat uneven performance in the last three years of the GDA.

EDII objects to this baseless and offensive statement. It should be removed from the final document.

As EDII states in our letter dated February 19, 2019:

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p. 31

Interviews with project developers in the area of waste-to-energy and clean energy, who were engaging with EDII to complete financing for projects, revealed that there was some loss of reputation for the approach as a result of their interactions. The developers expressed a loss of trust and increased uncertainty about the prospect of completing the financial transaction for their project after their interactions with EDII. One company reported frustration that EDII's commitment on financing has not been delivered yet. An official of a fourth company expressed disappointment with the process and withdrew from the project.

EDII strongly disputes these allegations, as we did in our comments dated September 25, 2018. All of the projects referenced involve partnerships with subnational government entities. No subnational project of any kind, in any sector, may proceed to the financing stage until all permits are in place and the state legislature or municipal council authorizes the financing. EDII is not responsible in any way for obtaining the required permits.

If the authors decide to retain this paragraph, our objection and its basis should be included in the final report.

p. 31

Further, the local private sector appears to be turning to alternate sources of financing. Mexican firms are gaining market share and appear to be taking the place of EDII.

These qualitative statements are vague and unsubstantiated, and therefore are not relevant to this evaluation of USAID's project. They should either be substantiated or removed from the final report.

p. 33

Creation of a National Bond Bank: Partially Achieved

One model, originally targeted by the Activity, was to create a single national bond bank. During the evolution of the activity, creating state bond banks was achieved and the idea of a nation-wide bond bank lost priority.

This statement is false. When it became clear that no federal entity was willing to host a bond bank during the Pena Nieto administration (2012-2018), EDII pursued an alternative SPV that could also function for Mexican states and municipalities to help them access capital market financing.

As EDII states in our letter dated February 19, 2019:

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p. 33

Investments in Clean Energy and Crime Prevention: Not Achieved

The creation of bond banks/SPVs has the capacity to contribute to enhancing the development possibilities opened by the energy reform. To date, there is little evidence of direct investment in energy efficiency and renewable energy projects using the bond bank/SPV vehicle. In the last phase of the activity, EDII placed secondary emphasis on the GDA objective of promoting clean energy and crime prevention while focused primarily on restructuring of Veracruz's debt. One outcome of the Veracruz debt restructuring was the creation of a crime prevention fund and, over time, more investments may be seen as a result. With greater oversight, USAID may have been able to better steer program activities to meet USAID's and the GDA's objectives.

There is no record of any subnational energy projects being financed at all, according to SHCP's National Registry of Public Debt.

In our comments dated September 25, 2018, EDII outlined how the conditions that expressly permitted subnational government financing under the National Law of Financial Discipline did not reference the opportunities for subnational ownership of energy efficiency and renewable energy generation projects established by the revised Energy Reform of 2016. The federal government did not take action to “unlock” the potential for subnational financing for subnational energy projects during the term of the GDA Agreement.

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p. 33

EDII has overlooked the waste-to-energy pipeline, with unclear support for projects. EDII’s uneven performance in this sector has generated a reputational cost (a poor reputation) for them and for USAID within the Mexican waste treatment industry.

This statement is incorrect and contradicted by information presented on p. 21 and elsewhere in the draft evaluation report. EDII worked on behalf of a public-private partnership waste-to-energy project for the state of Hidalgo.

As noted in our comments dated September 25, 2018, an individual threatened to make negative comments about EDII to the evaluation team. EDII believes that in person is the source of these spurious comments, and for this reason these should be removed from the evaluation report.

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A private sector partner and the U.S. Government have many coincidental interests, however, and at some point, those can diverge. When the USAID-EDII agreement changed to emphasize work on clean energy and crime prevention, which meant more focused work by EDII in the generation of an adequate and bankable pipeline of

projects, there was a divergence of strategic interests. While USAID wanted to take concrete steps in clean energy and crime mitigation areas, EDII was more focused on expanding its influence as a reliable and highly qualified financial advisor.

While EDII is a reliable and highly qualified financial advisor, the assertion that EDII did not work toward the objectives of the GDA Agreement at any point is false. EDII has always worked toward USAID's geographic and sectoral interests, while pursuing the broader goal of expanded subnational government access Mexico's capital market.

As EDII states in our letter dated February 19, 2019:

1) During the term of the GDA Agreement EDII introduced the Accredited Trust special purpose financing vehicle (SPV). The Accredited Trust SPV, for the purposes of Mexican states and municipalities, shares the functions of a national bond bank. The Accredited Trust acts as the intermediary on behalf of the subnational borrower(s), it achieves a higher credit rating, it promotes transparency. The accredited trust transactions that took place during the period of the GDA Agreement each received two independent credit ratings and are registered with the SHCP Registry of Public Debt. Multiple private investors participated in the accredited trust transactions, thus demonstrating that private capital accepts this SPV. The Accredited Trust SPV may be used to obtain financing for infrastructure projects across all sectors, including energy and crime prevention.

2) EDII worked toward a goal of obtaining capital market financing for subnational government energy and/or crime prevention projects, include public-private partnership projects, throughout the agreement period. According to the SHCP Registry of Public Debt, no subnational energy or crime prevention projects were financed during the period of the GDA Agreement. The draft evaluation report insinuates that projects were financed but offers no examples whatsoever that contradict the record of the National Registry of Public Debt.

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EDII's data confirms that the pipeline was neglected until the last few months of the Activity, when they reported and presented evidence that they were focused on closing two potential clean energy projects.

This statement mischaracterizes EDII's efforts under the GDA Agreement. No subnational energy projects were financed during the period 2015-2018 because the National Law of Financial Discipline does not address whether or not states and municipalities could apply debt financing to these projects.

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To ensure a process to improve reporting of progress and achievement of results from the different transactions and projects supported by the USAID/Mexico Activity, it is recommended that EDII submit state and/or municipal reports, including more evidence to support the actual outcomes achieved versus indicators. This report should present data on findings selectively and in an understandable manner, organize data around objectives and major themes, and use charts and tables. Conclusions should be clearly connected to evidence on performance.

EDII submitted all reports required under the GDA Agreement and met regularly with USAID's AOR and other Mission staff. EDII is always available to answer USAID's questions and work to address any concerns the AOR or others express.

All transactions completed with technical assistance provided by EDII under the GDA Agreements fully comply with Mexican national and state laws and regulations, and all are recorded in the National Registry of Public Debt. None of these transactions have been challenged in any way.

EDII has submitted substantial sets of documentation related to transactions, most recently the November 2017 transactions to restructure the debt of the state of Veracruz. These documents include formal filings with Mexico's market regulators, as well as the legal opinions of independent credit rating agencies and multiple law firms who reviewed the proposed Accredited Trust special purpose financing vehicle.

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