THE WORLD BANK
Treasury

CASE STUDY

# Securing Long-Term Financing for Clean Technologies in Mexico

## OVERVIEW

Mexico plans to move towards a lower carbon growth path by overhauling its urban transport system, a project requiring US$2.7 billion. The project's overall viability was not only dependent on securing additional long-term financing, but also on cost. Blending two resources enlarged the pool of low-cost financing available, enabling the project's implementation.

## Background

Mexico, ranked fourth in the world behind Sweden, Germany, and Iceland in the Climate Performance Index, has emerged as a global leader in the climate change arena. Despite fuel technology improvements and the enactment of a national strategy for climate change mitigation and adaptation, Mexico is still among the more carbon-intensive economies in Latin America. The transport sector, characterized by the highest motorization rate in the continent, poorly maintained old buses, inefficiently allocated road space for public transport, and inadequate fuel specifications, accounts for 18% of Mexico's total Green House Gas (GHG) emissions.

An integrated mass transit program has the potential of reducing 20% of the sector's carbon footprint, thereby contributing to the transformation of Mexican cities to a lower carbon growth path. To that end, Mexico has committed to overhauling its urban transport system by developing operational strategies, infrastructure, and low carbon technology that reduce GHGs.

## Financing Objectives

The transformation of Mexico's urban transport system requires more than US$2.7 billion of financing, US$2.4 billion of which was sourced from the national infrastructure fund (FONADIN), local governments, and the private sector. The project's overall viability was not only dependent on securing additional long-term financing, but also on cost. Mexico was, therefore, seeking to meet the shortfall with loans at highly concessional rates.

## IBRD Financial Solution

The Clean Technology Fund (CTF), managed by the International Bank for Reconstruction and Development (IBRD) with participation from other multilateral development banks, provides financing at concessional terms to scale-up demonstration, deployment, and transfer of low carbon technologies. IBRD's financial solution to Mexico's financing challenge for the Urban Transport Transformation Project was to blend US$200 million in concessional financing from CTF with a US$150 million loan from IBRD. The blending of the two sources of financing provides a very competitive funding cost for the project, enabling its implementation. The state-owned bank, BANOBRAS, is the designated borrower of both loans. The IBRD loan was customized to suit BANOBRAS' requirements. The repayment schedule was linked to disbursements, and set up to be "annuity-type," which will allow BANOBRAS to pay the principal in increasing installments as project revenues materialize. This means BANOBRAS will be making lower repayments at the onset of the project.

Moreover, the loan's flexible terms give the borrower the option to request disbursements in either US dollars or Mexican pesos, at fixed or floating rate to facilitate asset-liability management.

## Outcome

The blending of these two resources enlarges the pool of low-cost financing available, and reduces the financial barriers associated with this type of investment, facilitating countries' decisions to adopt low-carbon systems. By blending CTF and IBRD loans, Mexico was able to mobilize the necessary volume of funds at financial terms that met its requirements to enable the project's implementation. This co-financing scheme also allows the Bank and CTF to jointly support Mexico's efforts to take its climate change agenda forward. Moreover, the flexible terms of the IBRD loan and embedded risk management options will allow Mexico to manage interest rate, currency, and repayment risk.

| IBRD Loan | |
|---|---|
| **Amount** | **US$150 million** |
| Maturity/Grace Period | 13 years/3 years |
| Repayment Schedule | Annuity type |
| Interest Rate | 6-month LIBOR +80 bps[1] |
| Front-End Fee | 0.25% |
| Currency | USD, with the option to convert to MXN |

| CTF Loan | |
|---|---|
| **Amount** | **US$ 200 million** |
| Maturity/Grace Period | 20 years/10 years |
| Repayment Schedule | Level repayment |
| Service Charge | 0.75% per annum |
| Front-End Fee | 0.25% |
| Currency | USD |

| Indicative Blended Rates as of March 26, 2010[2] | | |
|---|---|---|
| **Loan Type** | **Equivalent Fixed Rate (%)[3]** | **Equivalent to:** |
| US$150 million IBRD Loan | 4.67% | 6M LIBOR +84 bps |
| US$200 million CTF Loan | 0.77% | 6M LIBOR -350 bps |
| IBRD/CTF Blended Rate | 2.12% | 6M LIBOR -201 bps |

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[1] Fixed spread of 80 basis points (bps) applies to the loan (average maturity between 10 and 14 years).
[2] Pricing is subject to market conditions.
[3] Equivalent fixed rate includes annualized front-end fee.



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