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RESTRUCTURING PAPER

ON A

PROPOSED PROJECT RESTRUCTURING
OF
MX URBAN TRANSPORT TRANSFORMATION PROJECT
LOAN N^o 7883- MX APPROVED ON MARCH 25, 2010

TO THE

BANCO NACIONAL DE OBRAS Y SERVICIOS PUBLICOS, S.N.C

NOVEMBER 8, 2011

ABBREVIATIONS AND ACRONYMS

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| BANOBRAS | National Bank for Works and Public Services (Banco Nacional de Obras y Servicios Publicos S.N. C.) |
| CTF | Clean Technology Fund |
| GEF | Global Environmental Facility |
| GoM | Government of Mexico |
| IBRD | International Bank for Reconstruction and Development |
| PDO | Project Development Objective |
| PHRD | Policy and Human Resources Development Fund |
| PROTRAM | Federal Support Program for Mass Transit (<i>Programa de Apoyo Federal al Transporte Masivo</i>) |
| UTTP | Urban Transport Transformation Program |

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MX URBAN TRANSPORT TRANSFORMATION PROGR RESTRUCTURING PAPER

A. SUMMARY

1. The proposed change to the Urban Transport Transformation Program (UTTP) loan agreement seeks to enable the borrower to access a new financial product currently offered by the World Bank, namely “Spot Starting Conversions”.
2. This innovative financial product was included in the World Bank General Conditions on July 31, 2010 after the Urban Transport Transformation Program was approved. However, the task team and the borrower indicated a mutual interest during appraisal and negotiations to include the financial products as soon as it was incorporated into the General Conditions. In this context, this restructuring paper seeks to formalize the inclusion of Spot Starting Conversions into the UTTP IBRD loan agreement.

B. PROJECT STATUS

3. The UTTP is financed by a CTF loan in the amount of US\$200 million, and an IBRD loan in the amount of US\$150 million. Each source of financing has its own legal agreement. This Project Paper, however, includes modifications to only the IBRD Loan Agreement. The proposed change is not applicable to CTF financing. The borrower for the UTTP is BANOBRAS, with guarantee from the United Mexican States.
4. The UTTP project development objective is to contribute to the transformation of urban transport in Mexican cities toward a lower carbon growth path.
5. The project is currently under implementation and is performing in a satisfactory manner. The project is part of a larger green infrastructure strategy in Mexico and it is being implemented in collaboration and with support of a Global Environmental Facility (GEF) operation, funds from the Clean Technology Fund (CTF), a Fee-Based Service, a Policy and Human Resources Development Fund (PHRD) grant, and a Technical Assistance Program between the World Bank and the Government of Mexico (GoM) for related technical assistance. In addition, the UTTP partners with Mexico’s PROTRAM (Federal Support Program for Mass Transit) and the private sector to finance several urban transit projects throughout Mexican cities.
6. In this context, a pipeline of 41 urban transit subprojects has been generated and is moving forward. The selection and preparation of potential subprojects for financing under the loan has been facilitated by the adoption of the safeguards requirements to all PROTRAM projects, regardless of Bank financing.
7. The Bank has already given no objection to the first Bus Rapid Transit corridor under the program to be financed with UTTP proceeds. The first subproject will be implemented in the State of Nuevo León (Monterrey City) and will be financed with

US\$30 million of loan proceeds. Moreover, the cities of Mexico DF, Guadalajara, Chihuahua and Mexicali, have also expressed interest in applying for UTTP financing this year.

C. PROPOSED CHANGE

8. The proposed change only affects Section II of the Appendix (Modifications to the General Conditions) to the Loan Agreement for Loan 78830-MX. It will modify the aforementioned section by inserting a new paragraph 3 to read as follows:

“3. Paragraph 20 of the Appendix is modified to read as follows:

“20. "Conversion Date" means, in respect of a Conversion, the Execution Date (as herein defined) or such other date as requested by the Borrower and accepted by the Bank, on which the Conversion enters into effect, and as further specified in the Conversion Guidelines.”

9. The rationale for the proposed restructuring is as follows:

- Historically risk management options (e.g. currency conversions, interest rate fixings, etc.) embedded in IBRD loans could only become effective on interest payment dates (“forward starting”). This had the practical effect of leaving a borrower potentially exposed, for a period of up to six months, to interest rate and/or currency exchange volatility.
- In order to obviate this issue and to provide greater flexibility to IBRD borrowers, the General Conditions of the World Bank were modified as of July 31, 2010 allowing borrowers two different options with respect to the effective date of conversions, namely (i) “forward starting” conversions, which, as described above would become effective on the loan’s interest payment dates and (ii) “spot starting” conversions which become effective on any date regardless of the loan’s interest payment dates. Thus, IBRD borrowers can freely choose between these two options.
- The Urban Transport Transformation Program Loan (78830-MX) was approved on March 2010, before the revision of the General Conditions. The older version of the General Conditions that apply to the loan do not contain the modified definition of 'Conversion Date' that would permit "spot starting" conversions.
- However, it was always the World Bank’s intention and the borrower’s choice to include the “spot starting” option in the loan documentation. Because the legal clauses could not be included in the original loan documentation, the borrower could not take immediate advantage of the "spot starting" conversions. The proposed amendments, which have been extensively discussed with the borrower and the guarantor, would resolve this issue.

10. The proposed change does not affect the PDO or likelihood that it will be achieved. FM and procurement arrangements remain as originally planned, no changes in expenditure categories will take place, and no safeguard issues will emerge from the proposed restructurings.