



AID-FOR-TRADE: CASE STORY

INTER-AMERICAN DEVELOPMENT BANK (IDB)

The Mesoamerica Project (MP)

Date of submission: February 2011

Region: Mesoamerica

Country: Belize, Colombia, Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, and the Dominican Republic

Type: Program / Regional Integration, Infrastructure, Energy, Trade Facilitation

Author: Country Department Central America, Mexico, Panama, and Dominican Republic (CID), Inter-American Development Bank (IDB) Group

Contact Details: Ennio Rodríguez

ennior@iadb.org

Tel: 202-623-3587

The Mesoamerica Project (MP)

Executive Summary

Within the political framework of the Mesoamerican regional integration, the Mesoamerica Project (MP) was created in 2008 as the successor to the Plan Puebla Panama (PPP).¹ The MP is a dialogue, coordination, and cooperation mechanism supported by the IDB to articulate integration efforts and develop management and execution of projects aimed at improving quality of life in the region. The MP thus serves as the operational tool for furthering the integration of 10 countries: Belize, Colombia, Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, and the Dominican Republic. The MP seeks to foster the development, financing, and implementation of regional infrastructure and social development projects. It also works toward connecting markets within the region by reducing transport and trade costs.

The IDB has strongly supported the MP since its inception, providing financial and knowledge resources to implement the MP mechanisms. In particular, it has backed initiatives aligned with the Aid-for-Trade (AfT) Initiative to enhance the region's position in the global marketplace, including:

- Investments in road infrastructure that by 2015 will cut average freight travel time from around eight days to just 2.25 days
- Accelerated and harmonized customs procedures reducing average border crossing time from 60 minutes to eight minutes
- Improved power grid infrastructure necessary for creating an integrated, regional electricity market that would reduce power generation costs up to 20 percent
- Substantial progress towards completing groundwork for a regional telecommunications infrastructure that will increase competition in broadband services, and reduce the “digital gap” in Mesoamerican countries

1. Issues Addressed

Only by boosting trade and economic growth can the diverse development needs of Mesoamerican countries effectively be addressed. This, however, requires significant investment in capacity and infrastructure. For these investments to be made and pay off, however, the region must be integrated into the global economy. Only with better basic economic infrastructure —improved transportation, logistics, and telecommunications— will the regional private sector achieve greater competitiveness.

Significant supply-side challenges remain across Mesoamerican countries, which must be addressed if the region is to use trade as an instrument for growth and poverty alleviation. For some of these countries transport costs are significantly higher than tariffs, impacting imports, exports, and especially intraregional trade. In line with the AfT Initiative's goals, the MP encompasses diverse means for addressing these deficiencies and challenges, including institutional capacity-building, regulatory updates and harmonization, improved regional channels of communication and cooperation, and investments in economic infrastructure.

¹ The PPP was a multi-billion dollar development plan formally initiated in 2001, which intended to "promote the regional integration and development" of the nine Mexican southern states with the rest of Central America and Colombia.

2. Objectives Pursued

The MP's overall mission is to augment Mesoamerica's economic growth while preserving its environment and natural resources by developing collaboration channels between countries in the region. It seeks to develop, finance, and implement regional infrastructure and social development projects. In addition, it seeks to connect regional markets by reducing transport and trade costs, enhance trade competitiveness and increase foreign investment. Ultimately, the MP aims to provide the region's inhabitants with better economic and social opportunities to improve their quality of life.

At the time of the MP's creation in 2008, Mesoamerican heads of state pledged to continue building upon and consolidating the PPP's goals of institutional strengthening, coordination with the Central American Integration System (SICA), and project management. In addition, leaders also set out a new set of priority areas:

- Consolidation of coordinated campaigns to increase international cooperation
- Development of public-private partnerships that foster project development, implementation, and investment
- Continuation of coordination efforts with finance ministries and multilateral financial institutions
- Clearly communicating the mechanism's reach and results to the public

Heads of state meet on a yearly basis to monitor progress and revise priority areas and projects. Ministers also meet regularly to coordinate in their respective sectors, and an Executive Committee comprised of presidential appointees meets around twice a year to plan and supervise the activities of the officials in charge of day-to-day activities

3. Design and Implementation

The MP focuses on eight main policy areas, with the first four falling under the AfT Initiative: energy, transportation, telecommunications, trade facilitation, natural disaster mitigation, public health, environmental sustainability, and housing. The region's analogous conditions present a unique opportunity for the MP to identify and generate synergies advancing a regional integration strategy. This approach, in turn, can further the IDB's goals of regional integration for the Latin America and Caribbean (LAC) region as a whole. The IDB demonstrated its commitment to regional integration by setting a goal of investing USD 1.8 billion annually in integration projects for LAC, within the framework of the IDB's recent capital increase.²

The IDB has helped Mesoamerican countries implement and benefit from trade liberalization and enhanced market access by substantially contributing to the soft and hard trade-related infrastructure investments addressed in the MP. These AfT-related projects aim at connecting markets and tackling the transportation, trade facilitation, energy, and telecommunications challenges within the region. They are crucial for reducing transport and trade costs, enhancing trade competitiveness, attracting foreign investment, and efficiently delivering goods and services to the global marketplace. At the same time, the MP will seek to promote the convergence of the free trade agreements (FTAs) signed by countries in the

² In 2008, at the Annual IDB Board of Governors Meeting, the 48 member countries reached an agreement to boost the Bank's ordinary capital by USD 70 billion, raising it to more than USD 170 billion. The capital increase, the largest in the IDB's history, will allow it to double its lending capacity to USD 12 billion a year.

region, and also to create the institutional framework needed to reduce trade costs generated by inefficiencies and poor coordination among national markets.

From 2001 to the present, the IDB has been the main source of financing for the regional integration of Central America, allocating about USD 1.5 billion in investment loans. This amount is equivalent to 13 percent of the Bank's total portfolio for Central American countries, which amounts to USD 11 billion. In the same time period, the IDB has financed USD 50 million in non-reimbursable technical cooperation, devoting more than USD 20 million for pre-investment studies and technical assistance in 2009 alone. The figures are broken down as follows, grouped by area of investment:

Energy	USD 736.8 million
Transportation	USD 728.5 million
Natural Disasters	USD 103.6 million
Environment	USD 20.4 million
Trade Facilitation	USD 5.6 million
Telecommunications	USD 1.1 million
Health	USD 400,000

As part of its comprehensive AfT approach to the PM, the IDB has strongly supported the following projects:

- **The Pacific Corridor Highway (PC):** A 3,200-km highway that runs from Panama to Mexico and crosses six national borders, the PC is the main logistics corridor for the region, transporting 95 percent of all commercial goods, valued at approximately USD 6 billion. Once improvements are completed in 2015, the improved PC will cut this distance by approximately 300 km, saving considerable time and cost to its users. Currently the average speed of the corridor is 17 km/hour, which means that eight days (190 hours) are required to travel from Panama City to Puebla, Mexico. The goal is to increase average speed to 60 km/hour, reducing travel time to 2.25 days or 54 hours. It has been determined that USD one billion will be needed to complete the project, with the IDB funding 20 percent of the total. Currently, feasibility studies are being undertaken to further define detailed project characteristics and financing options for the project as a whole.
- **The International Transit of Goods (TIM):** Financed by IDB grants, the TIM is an innovative system for managing the movement of goods, based on cutting-edge technology, elimination of paper usage, and harmonization of customs control procedures.³
- **Electrical Interconnection System for Central America (SIEPAC):** This ambitious project to link six national power grids⁴ through 16 substations will provide Central America with a robust and reliable infrastructure, helping it to establish a regional electricity market with greater economies of scale than the existing networks. The IDB has invested around USD 300 million in loans and over USD 30 million in grants to promote policy coordination, regulatory harmonization and institutional development.
- **Mesoamerican Information Highway (AMI):** AMI aims to reduce the digital gap in Mesoamerican countries and enable the development of more efficient information and communication technologies by promoting further telecommunications and Internet public policy

³ For further information, please see separate IDB case story on the TIM, also submitted in preparation for the Third Global Review for Aid-for-Trade.

⁴ Participating countries are Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and Panama.

coordination and regulatory harmonization. As an offshoot of SIEPAC, it uses that project's physical and legal infrastructure. AMI aims to build, in cooperation with the private sector, a high-capacity optical fiber connection in Mesoamerica. The project will increase competition in the telecom markets by adding a land-based connection in addition to the region's submarine cable networks. Eventually, the project will provide a land-based connection between South and North America.

4. Problems Encountered

The main problem the MP has encountered has been reluctance from some government agencies and other critical actors. Some agencies were reluctant to adopt the organizational and infrastructure framework necessary to operate at a supranational level. For example, there is resistance to abandon energy self-sufficiency goals when regional investments provide a more efficient solution, even after regulatory and public policy changes have been implemented and the multinational firm operating the grid established. The PC faces the challenge of coordinating investments when the roads may not have the same level of priority for all governments involved. If investments fail to happen in a timely fashion, the regional benefits will not fully materialize. Additionally, the participation of some Heavily Indebted Poor Countries (HIPC)⁵ implies additional financing constraints. Changes of government may lead to different priorities or, at the very least, the need to explain and rally support for ongoing projects.

5. Factors for Success/Failure

- **High-Level political commitment:** The main factor for success has been the strong commitment of many countries' political leaders. The periodic MP Heads of State summit, a high-level forum for examining regional priorities, ensures continuity of the program over the long-term and establishes an accountability framework in the individual projects.
- **Region's rich institutional network:** The Mesoamerican region is particularly rich in regional institutions, hence providing forums for policy and investment coordination and cadres of regional technocrats that can follow up on regional projects. The MP built on these assets and experience of regional coordination, which included a portfolio of regional projects at various levels of development.
- **External support:** Finally, given the challenges of coordinating regional projects over relatively long time periods, the support and finance by the regional banks, particularly the IDB has been critical. Given that there are ten participating countries, regional institutions and multilateral development banks (MDBs) have also helped to smooth transitions amidst frequently changing administrations.

6. Results Achieved

The MP's key achievements include:

- **Political Dialogue:** It has become a high-level political venue for reviewing regional challenges and opportunities, which in turn focuses attention on its mission and goals.

⁵ HIPC is a group of 40 least developed countries with high levels of poverty and debt overhang which are eligible for special assistance from the International Monetary Fund (IMF) and the World Bank.

- **Regional Integration:** It facilitates a strategic approach to national challenges from a regional perspective, hence ensuring the adoption of regional solutions that strengthen and boost economic convergence.
- **Specialization:** It promotes specific projects and supports or complements regional activities executed in other spaces and initiatives.
- **Resource Management:** It facilitates the funneling of resources from international cooperation agencies and multilateral development banks towards priority projects in Mesoamerica.
- **Regional Public Goods:** It favors the creation of public goods that benefit more than one country.

Below is an overview of the results of AFT-related projects supported by the IDB within the framework of the MP:

- **Transport:** Between May and June 2010, a careful inspection of the state of the Pacific Corridor Highway, known as the Road Safety Caravan, was performed under the auspices of the Acceleration Program. The Caravan was composed of vehicles equipped with sophisticated equipment to collect and analyze road conditions. The current status of the corridor is uneven, with some road segments in poor condition. During 2011 feasibility studies will be completed to upgrade all segments of the corridor to international standards. The corridor, together with trade facilitation measures, will improve regional competitiveness by reducing transportation costs and facilitating access to markets and the integration of value chains. Transportation times will decrease from 190 hours (eight days) to 54 hours (2.25 days) over the next five years.
- **Trade Facilitation:** Border authorities have implemented the TIM, cutting red tape at border checkpoints. For instance, average border-crossing time has decreased from 60 to eight minutes at the El Amatillo crossing between El Salvador and Honduras. TIM is currently being used at six checkpoints in Mexico, Guatemala, El Salvador and Honduras, and is scheduled to be extended to Nicaragua, Costa Rica and Panama in the first quarter of 2011. Eventually, TIM is expected to be adopted at all Central American border checkpoints – on land, and at seaports and airports.
- **Energy:** By the end of 2010, 98 percent of the necessary infrastructure for SIEPAC was completed. The project included the creation of a regional regulatory body, a multinational company that operates the grid (EPR) and a public sector regional council. This institutional development was tailored to the needs of SIEPAC. The existing shared power grid between Guatemala and Mexico, launched in October 2009 as the first electricity export project in the region, complements this grid infrastructure. A project to connect Panama and Colombia is currently in development. The IDB's investment in SIEPAC has generated 1,000 jobs. In the long-run, SIEPAC is expected to improve power supply, increase investment, and reduce consumers' electricity costs by up to 20 percent in participating countries.
- **Telecommunications:** Completion of the fiber optic cable, like SIEPAC, currently stands at over 90 percent. The Central American Optical Fiber Network (REDCA), a subsidiary of the EPR, was created to develop, design, finance, build, maintain, and operate the optical fiber networks and to interconnect the telecommunications systems of the region. While the necessary infrastructure is put in place, REDCA conducted a market study on the telecommunications sector for its business plan. In addition, AMI countries selected Nicaragua as REDCA's administrative, operational, and commercial headquarters. REDCA has been conceived as a "carrier of carriers" which will compete with submarine cable services currently connecting the region with the rest of the world. Institutions are now being developed to facilitate regulatory harmonization and strengthen public sector telecom and IT forums.

7. Lessons Learned

- **Active involvement of Heads of State is pivotal:** High-level coordination proved essential for ensuring continued attention and commitment of resources by national and regional agencies.
- **Ensuring compliance at the government level builds trust:** Mutual trust results from the full commitment of all participating agencies in every country. Strengthening government agencies' capacity to follow-up on regional issues would help build this trust.
- **Regional projects should be designed to complement physical investment with institutional development:** Issues to look at include the possible need for regulatory harmonization and development of regional regulatory agencies, strengthening existing or establishing new public discussion forums and/or decision-making bodies, and the establishment of multinational firms.
- **Public-private partnerships should be considered as a means to increasing private sector participation:** Fiscal constraints demand innovative financing options be explored, including public-private partnerships.
- **Long-term commitment by MDBs is a factor of success:** Individual governments do not always recognize the positive externalities of regional projects, which may appear as collective action problems. The IDB has been a key MDB in identifying such externalities, formulating projects, and providing financial and institutional support to complete them.
- **Regional technical cooperation accompanying infrastructure projects has strengthened institutions:** Regulatory coordination has been boosted thanks to the strengthening or creation of institutions and/or policy coordinating mechanisms that came with regional infrastructure projects. It is hence pivotal to keep these technical cooperation and capacity-building components as part of any financial instruments for regional technical cooperation projects.
- **Measuring, reporting and communicating results:** MDB-funded projects have improved metrics to measure projects' impacts. This should be effectively communicated to interested stakeholders and the public at large. Previous efforts to engage civil society in the PPP ended up galvanizing opposition based mainly on ideological grounds. A more effective communications strategy should be grounded on the new metrics, demonstrating positive impacts of collective action.

8. Conclusion (applicability to other programs)

- Regional projects are often based on a need for collective action not registered by markets or governments. Regional institutions could help orchestrate such action. In the developing world, however, such institutions, if they do exist, tend to be under-funded and their mandates limited to secretarial roles of intergovernmental coordination.
- MDBs can play the critical role of providing technical and financial support to regional initiatives to help overcome institutional weaknesses, which may be limiting regional collective action.
- Infrastructure projects can further develop regional integration once trade liberalization has been accomplished. Road projects interconnecting countries or regions, border-crossing infrastructures and border trade facilitation measures should be developed simultaneously to maximize potential benefits, particularly with regard to trade.

- Integrated electricity markets can facilitate more efficient investment and production decisions. This requires institutional and regulatory action. Electricity transmission infrastructure provides the opportunity for fiber optic interconnection, opening opportunities for reducing the digital gap in participating countries.
- Last but not least, high-level political commitment is necessary to advance regional integration projects.