

Report No. 1483-ME

Mexico Appraisal of the Baja California Tourism Project

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April 18, 1977

Tourism Projects Department

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CURRENCY EQUIVALENTS

Currency Unit	=	Peso (Mex\$)
US\$1	=	Mex\$19.9 <u>1/</u>
Mex\$1.0	=	US\$0.050
Mex\$1 million	=	US\$50,251

WEIGHTS AND MEASURES

1 meter (m)	=	3.28 feet
1 square meter (m^2)	=	10.76 square feet
1 cubic meter (m^3)	=	35.29 cubic feet
1 kilogram (kg)	=	2.205 pounds
1 metric ton (ton)	=	2,205 pounds
1 hectare (ha)	=	2.47 acres
1 kilometer (km)	=	0.62 miles
1 liter per second (l/sec)	=	22,800 US gallons per day
1 cubic meter per day (m^3/d)	=	264 US gallons per day

GLOSSARY OF ABBREVIATIONS

ASA	-	Airports and Auxiliary Services Agency
CFE	-	Federal Electricity Commission
CORETT	-	Land Regularization Committee
DGCA	-	Directorate General of Civil Aeronautics
FONATUR	-	National Fund for Tourism Development
FOVI	-	Fund for Operating and Banking Discounts for Housing
Hacienda	-	Ministry of Finance and Public Credit
IDB	-	Inter-American Development Bank
IMSS	-	Mexican Institute for Social Security
INFONAVIT	-	Housing Development Agency
NACOA	-	National Company of Aviation Combustibles
NAFINSA	-	National Financing Agency
Patrimonio	-	Ministry of the National Patrimony and Industrial Development
P y B	-	Ministry of Programming and Budgeting
RAMSA	-	Aeronautical Radio Company of Mexico
SAHOP	-	Ministry of Human Settlements and Public Works
SARH	-	Ministry of Agriculture and Hydraulic Resources
SCT	-	Ministry of Communications and Transportation
TELMEX	-	Telecommunications Corporation of Mexico
Turismo	-	Ministry of Tourism

GOVERNMENT OF MEXICO

FISCAL YEAR

January 1 to December 31

1/ The exchange rate was US\$1 = Mex\$12.5 until August 31, 1976.
The appraisal mission used US\$1 = Mex\$19.9 to convert base line costs.
The peso is now floating.

MEXICOAPPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECTTABLE OF CONTENTS

	<u>Page No.</u>
SUMMARY AND CONCLUSIONS	i-iii
I. INTRODUCTION	1
II. THE TOURISM SECTOR	2
III. THE PROJECT	
A. Project Background and Objectives	5
B. Project Description	9
C. Cost Estimates	12
D. Execution and Operation	12
E. Financing Plan and Lending Arrangements	16
F. Procurement and Disbursement	16
IV. JUSTIFICATION	
A. Market Demand	17
B. Development of Tourism Facilities	21
C. Financial Aspects	23
D. Economic Justification	25
E. Social Aspects	30
V. RECOMMENDATIONS	31

This report is based on the findings of a mission consisting of Messrs. I.A. Menezes, R. Bentjerodt, E. Echeverria, T. Iizuka, P. Murgatroyd and Ms. J. de Regt. While in the field, the mission received assistance from Messrs. L. Vera (tourism), E. Maisch (water supply), R. Overby (environment), and W.B.R. Zetterstrom (aviation).

Table of Contents (Continued)

Annex No.

- I. Project Cost Estimates
- II. Project Description
- III. Aeronautical Aspects
- IV. Water Supply and Sewerage
- V. The Tourism Sector
- VI. FONATUR
- VII. Market Demand
- VIII. Development of Accommodation Facilities
- IX. Financial Forecasts on Estate Operations
- X. Economic Justification
- XI. Social Aspects
- XII. Environmental Aspects

Chart

- 1. Schedule of Implementation

Maps

- IBRD No. 12647 - Mexico: Project Locations
- IBRD No. 12650 - San Jose del Cabo Area Plan
- IBRD No. 12651 - San Jose del Cabo Land Use Plan
- IBRD No. 12648 - Loreto Area Plan
- IBRD No. 12649 - Loreto Land Use Plan

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

SUMMARY AND CONCLUSIONS

i. This report appraises a project to provide facilities for tourism and urban development at Loreto and San Jose del Cabo in Mexico's southern state of Baja California. Tourism infrastructure to be provided includes streets, water, sewerage and drainage systems, and the improvement and expansion of airports, electric power, and telecommunications. Investments in the urban areas are intended to improve and expand the infrastructure in the existing towns and provide such facilities as health clinics, parks, marketplaces, and schools. The project also includes recreational facilities, some office and community buildings, funds for restoration of old buildings, investment promotion, nature conservation, community development activities, and studies. The two sites will in the first stage, covering a period of eight to nine years, comprise hotels with 2,100 rooms, apartels (apartment hotels) with 4,050 rooms, and 960 condominium units and tourist villas. Accommodation included in the project consists of one hotel of 250 rooms at each site.

ii. The project is the third major tourism development being undertaken by the Federal Government. In 1972 the Bank made a loan of US\$22 million equivalent to help finance the provision of infrastructure for a tourist resort in Ixtapa, near Zihuatanejo, on Mexico's Pacific coast. This project is now nearing completion with all of the loan expected to be disbursed by June 30, 1977. The Inter-American Development Bank has made loans totaling US\$41.5 million for a similar project at Cancun, on the coast of Yucatan.

iii. Mexico is one of the world's major and most richly endowed tourist destinations. Its formidable assets have attracted an increasing flow of visitors which numbered 3.2 million persons in 1975. This represented a slight drop, compared to 1974, in visitor traffic, which has despite its size been growing steadily at an average rate of 10% a year over the last 15 years. Foreign exchange earnings from tourism grew at an annual rate of 11.5% between 1960 and 1975, and amounted to US\$800 million in 1975 or more than 13% of exports of goods and nonfactor services. Tourism is now Mexico's largest single source of foreign exchange earnings.

iv. For the period 1961-1976 accommodation capacity more than doubled while visitor arrivals increased by 300%. The fastest increase in capacity has been in hotel rooms of international standard, which continue to enjoy relatively high occupancy rates. Further additions to capacity will be required in order to tap the potential market for Mexico. The costs of correcting the infrastructure and other inadequacies in existing destinations such as Acapulco to allow for such expansion, how-

ever, would be enormous. Further development of the new resorts of Cancun and Ixtapa-Zihuatanejo, which could be done at relatively low cost, will not be sufficient. Assuming improved promotion and better utilization of existing capacity, particularly during the off-season, Mexico in the next four years would need some 25,000 hotel rooms of international standard to maintain an average annual growth rate of 9% in visitor arrivals. Given these circumstances, the Mexican authorities have rightly considered the need to encourage tourism development in new areas while developing plans for improvement and expansion at existing destinations.

v. Tourism has been singled out by the Government of Mexico as the most promising sector to bring about social and economic development in Baja California. Its proximity to the western part of the United States, its natural attractions (beaches, sea, climate), and fishing potential provide Baja California with unique assets and an opportunity to tap one of the largest and richest tourist generating regions in the United States. Recognizing this potential and in light of the Government's national policy to diversify geographically Mexico's tourism facilities and its regional policy to promote Baja California through the establishment of strategically located tourism development poles, a total of six areas were selected after extensive studies. In 1975 the Government decided to proceed initially with the provision of tourism and other facilities at two of these sites: Loreto, located on the Sea of Cortez, 360 km north of La Paz, the state capital; and San Jose del Cabo, on the southern tip of the peninsula, 200 km south of La Paz.

vi. While the principal investments will be in infrastructure for the tourism zones and the airport, the Government would like to repeat in Baja California the successful urban development of the town of Zihuatanejo stimulated by the Bank's first tourism project. Accordingly, the proposed project includes significant investments in the towns of Loreto and San Jose del Cabo, designed not only to improve the quality of life of existing and future inhabitants of the towns but particularly to tackle the problems of the poorest sections of the population with sites and services, and guided self-help programs.

vii. Although strong interest in the proposed developments has been expressed by potential investors, no binding commitments have yet been made. Hotel investors are reluctant to be first in a new destination and generally tend to wait until the tourism infrastructure is in place before investing, which may be at least a year later than desirable from a financial and economic point of view. Moreover these first investments in superstructure facilities are crucial in setting the architectural tone, and demonstrating proper environmental standards for the resort. Accordingly, provision is made in the project for the construction of a first hotel of 250 rooms of medium category.

viii. The project is estimated to cost US\$84 million, including contingencies. The proposed Bank loan of US\$42 million would cover the foreign exchange component of the project. The Federal Government would provide the balance of the funds required to finance the project as well as any cost overruns.

ix. Major civil works and equipment contracts would be awarded on the basis of international competitive bidding. Project items have been grouped into packages in order to encourage such competitive bidding, but the bidder would also be able to bid on individual items. Some contracts, however, would be too small to attract foreign bids and it is proposed that they be awarded on the basis of locally advertised bids. The total value of such contracts is estimated not to exceed US\$4 million equivalent. Because of the need for standardization, navigational equipment for the airports (costing US\$0.7 million) would be negotiated directly with the company supplying such equipment to Mexico. In evaluating international bids for equipment and furniture, local manufacturers would be allowed a preferential margin of 15% of the c.i.f. price of competing imports or the prevailing level of customs duties, whichever is lower.

x. Basic responsibility for executing the proposed project would rest with FONATUR (Fondo Nacional de Fomento al Turismo) with the exception of electric power, telecommunications, and the airports, which would be carried out by other government agencies. FONATUR is a government agency charged with planning and promotion of integrated resort developments, including financing of needed infrastructure investments, hotels, and other tourism superstructure. FONATUR is well managed and fully qualified to execute, operate, and maintain the components of the project for which it is responsible. FONATUR would contract with the Federal Power Commission (CFE) and the Telecommunications Corporation (TELME^X) to design and construct the electric power and telecommunications networks. Responsibility for design and construction of the airport facilities would lie with the Ministry of Human Settlements and Public Works (SAHOP). All these agencies have considerable experience and the competence to execute their respective components.

xi. The economic rate of return on investments in Loreto would be 19% and in San Jose del Cabo 21%. When implemented, the project would directly employ 12,000 persons in hotel and other tourism facilities. Employment generated in construction, transportation, handicrafts, and other services would account for an estimated 13,000 additional jobs. Unskilled labor would fill more than 60% of the jobs created, and almost 40% of the jobs could be filled by women. Net foreign exchange earnings generated by the project are expected to be US\$19 million in 1985 and US\$89 million a year from 1990 onwards.

xii. As presently designed, no significant external environmental or social problem will result from the developments; rather than impoverishing the physical and social environment, the project will induce changes to the contrary.

xiii. The project is considered suitable for a Bank loan of US\$42 million equivalent for a term of 17 years, including a grace period of 3-1/2 years.

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

I. INTRODUCTION

1.01 In 1968 the Government of Mexico indicated an interest in obtaining assistance from the Bank for financing new tourism infrastructure. In 1972 the Bank made a loan of US\$22 million equivalent to help finance the provision of infrastructure for a tourist resort in Ixtapa, near Zihuatanejo, on Mexico's Pacific coast. After encountering some delays due largely to land acquisition problems, the project is now nearing completion with the loan expected to be disbursed by June 30, 1977, with the exception of some funds allocated to a small hotel school (US\$900,000) which has not yet been implemented because of jurisdictional problems (para. 2.12). In the tourist zone of Ixtapa, two hotels are open for business (534 rooms) and several others are under construction. By June 1977 over 1,500 rooms are expected to be available. The airport financed under the project is serving both Ixtapa-Zihuatanejo and the rapidly expanding industrial town of Lazaro Cardenas, an hour's drive from the airport.

1.02 In 1974, in continuance of its policy of geographic diversification of Mexico's tourism facilities, the Government, after extensive studies financed with local funds, requested that the Bank consider several sites for development along the Baja California peninsula. Subsequently, in the course of project identification and preparation missions in 1975 and 1976, agreement was reached to focus attention on two sites: Loreto, located on the Sea of Cortez, 360 km north of La Paz, the capital of the state of Baja California South; and San Jose del Cabo on the southern tip of the peninsula, 200 km south of La Paz.

1.03 The project consists of infrastructure and related facilities required for development of the two sites, which in the first stage will comprise hotels with 2,100 rooms, apartels with 4,050 rooms, and 960 condominium units and tourist villas. The financing of a first hotel at each site is included in the project. In addition, the Government would like to repeat in Baja California its successful efforts in urban development of the town of Zihuatanejo, and has hence included infrastructure and other investments in the project that would provide a significant improvement in facilities and services for the residents of the towns of Loreto and San Jose del Cabo.

1.04 Due to its complexity and the difficult land tenure and water supply problems in Baja California, the preparation of the project has required about two years. These problems were solved and the studies completed in time for an appraisal mission to visit Mexico in October 1976. The mission included Messrs. Menezes, Bentjerodt, Echeverria, Iizuka, Murgatroyd, and Ms. de Regt. While in the field, the mission received assistance from Messrs. Vera, Maisch, Overby and Zetterstrom. A further visit was made by Messrs. Menezes and Vera in February 1977, for discussions of certain project issues with the new Government.

II. THE TOURISM SECTOR

2.01 Mexico is one of the world's major and most richly endowed tourist destinations. Its attractions include the architectural remains of a series of major civilizations, entertainment that ranges from traditional to modern, a wealth of contemporary creative arts, shopping opportunities, an agreeable climate, excellent beaches along the Pacific and Caribbean sea coasts, and street scenes that reflect the varied cultural background of Mexico's multiracial populace. In addition, Mexico is an accessible and truly foreign destination for the United States and Canada, which make up one of the world's largest source of foreign tourists.

2.02 These assets have attracted an increasing flow of visitors in the past and constitute an important potential for the future. In 1975, over 3.2 million persons visited Mexico.^{1/} This represented a slight drop compared to 1974 in visitor traffic. Historically, visitor arrivals grew at a rate of 13.9% annually between 1961 and 1965, 10.1% between 1965 and 1970, and 6.7% between 1971 and 1975; an average of 10.4% from 1961 to 1975 (Annex V). Growing prosperity in the US and Canada, the provision of direct air access, and rapid expansion in accommodation and infrastructure combined to make this growth possible. The declining growth rate in the 70s is mainly attributable to the economic recessions in the US and to Mexico's uncompetitive position resulting from an overvalued peso.

2.03 Nearly 90% of visitors to Mexico are from the US and access from the US is excellent by every transport mode. In the past, a majority of foreign visitors traveled to Mexico by road, the bulk from the border states of Texas, California, Arizona and New Mexico. The pattern has now changed with air transportation becoming the dominant mode of access, as more distant destinations are opened up and the cost of air travel declines (Annex V).

2.04 Foreign visitors to the interior of Mexico (i.e., beyond the border zone) have in the past often visited more than one destination within the country and almost always included Mexico City in their itineraries. This pattern is also changing with a growing number of tourists visiting a single destination only, generally a beach based resort. An analysis of income levels of visitors indicates that Mexico seems to be geared toward a more diversified market and is attracting more lower- and middle-income visitors than the Caribbean, with which it is in competition. It has still to tap the full potential represented by this market, however (Annex VII).

2.05 An important phenomenon in Mexico in recent years has been the burgeoning domestic tourist market. It is estimated that Mexicans accounted for 14.8 million visits in 1975, or a total of 28.4 million visitor nights. A growing number of Mexicans are also buying second homes,

^{1/} These visitors tour the interior of the country and are to be distinguished from the Mexican/US border traffic, estimated at more than 70 million in 1975.

apartels, or condominiums, particularly along the coasts.

2.06 Because climatic conditions make Mexico an all-year-round resort area, visitor flows to Mexico show only a minor degree of seasonality. As a result, tourist facilities generally experience relatively high occupancies, much above those prevailing in many other tourist areas.

2.07 With high occupancies making investment in new capacity attractive, hotel and other accommodation capacity more than doubled, from 91,000 rooms in 1961 to 191,000 rooms in 1975, while visitor arrivals increased by 300%. The fastest increase in capacity has been in hotel rooms of international standard, which, in spite of the slowdown in the growth of visitors in 1974 and 1975, have continued to enjoy high occupancy rates.

2.08 Studies show that Mexico in the next four years will need some 25,000 additional hotel rooms of international standard to accommodate projected visitor growth rates of 9% per year. The appropriate strategy will include:

- (a) improved promotional efforts aimed at segments of the market which would result in even more visitors during the off-season, resulting in improved utilization of existing capacity (and yielding high returns);
- (b) expanding existing resorts, where new infrastructure requirements would be relatively inexpensive; and
- (c) encouraging development at new sites which might, through the diversification of attractions, enable Mexico to tap new markets.

With respect to promotional efforts, studies are required and both technical and financial assistance have been requested from the Bank (para. 4.26). With regard to existing areas, further expansion of accommodation at new resorts such as Cancun and Ixtapa-Zihuatanejo would be possible at relatively small cost. The costs of improving infrastructure and correcting other inadequacies in established sites such as Acapulco, however, would be enormous. While the Government proposes to continue encouraging the expansion of Cancun and Ixtapa-Zihuatanejo, as well as established resort areas, it has also rightly considered the need to encourage development at other sites to be able to tap fully the potential market of Mexico.

2.09 Until the 70s, government institutions concerned with tourism had little impact on the sector's development. Public sector expenditures for tourism development had been modest, and no coherent set of fiscal, credit or other specific sector policies had been instituted to stimulate the growth of the industry. Nevertheless, the private sector responded vigorously to the rapid growth in demand, with little or no government assistance except for uncoordinated efforts by federal, state, and municipal agencies to provide infrastructure facilities. Such private development tended, however, in the absence of well conceived government policies, to stress short-term profitability with little regard to the longer run impact of their activities on the social situation, the economy and the environment.

2.10 In response to these deficiencies and recognizing the importance of the sector, the Government created a special fund (INFRATUR) in the Banco de Mexico in 1969, to plan and promote integrated resort developments, including financing of needed infrastructure investments. Because of a growing scarcity of loan capital, the Government had a few years earlier established a trust fund (FOGATUR) in NAFINSA for the purpose of financing hotels and other tourism superstructure. In 1974, these two funds were merged. The new fund, called Fondo Nacional de Fomento al Turismo (FONATUR) integrates most activities of the public sector in the tourism field and strengthens the Government's hand in controlling the quality and pace of development of the sector (Annex VI).

2.11 FONATUR has mainly concentrated its development efforts in two sites: Ixtapa-Zihuatanejo on the Pacific coast and Cancun on the Caribbean coast. These projects, financed in part by the Bank and the IDB respectively, are nearing completion. To date FONATUR has invested Mex\$1.1 billion to develop infrastructure in Cancun and Mex\$0.7 billion in Ixtapa-Zihuatanejo. FONATUR has already earned a significant surplus in cash flow terms on its land development operations at Cancun and Ixtapa-Zihuatanejo, amounting to Mex\$37 million in 1973 and Mex\$240 million in 1976. In addition, over 4,000 hotel and other rooms are expected to be available in the two sites this year. The volume of FONATUR's hotel credit operations has expanded much faster than its investments in infrastructure development. As of August 31, 1976, FONATUR had approved 378 credit applications for a total of Mex\$2.8 billion to finance 19,000 new rooms throughout the country.

2.12 Serious attention is being given to employment in the sector, especially since tourism has become instrumental in creating a more balanced regional distribution of economic activities in Mexico. Recent studies estimate that direct employment in tourist activities amounts to between 300,000 and 400,000 persons. Significantly, most of those employed are drawn from the unskilled sector of the population and they have obtained relatively well paid jobs after little investment in training. Even a modest increase in training would improve the professional competence of personnel. Existing training institutions concentrate on training for higher management and supervisory levels, when the most pressing need is for trained staff at the lower and intermediate levels. Moreover, local unions have traditionally attempted to control these institutions further complicating the situation. There is also no clear delegation of responsibility for hotel and tourism training to a single organization capable of drawing up the necessary programs and implementing them. The new administration is pledged to revamping all vocational training with a view to improving the situation.

2.13 While views about the efficacy of Mexico's air access policies differ, it is clear that efforts to protect interests both in Mexico and the US have hindered the growth of tourism, particularly to new destinations. No bilateral agreement with the US (which generates nearly 90% of the visitors to Mexico) has been signed in the last six years, and even some of those airports currently in the agreement are not all being served by US carriers. Fortunately, charter traffic has provided some relief to the tourist industry. Bilateral negotiations with the US are scheduled for mid-1977 when the relevant issues are expected to be reviewed.

2.14 Current terms of lending for hotels in Mexico are from 10-15 years, 2-3 years grace, with 10% to 15% interest, and are attractive but less generous than in many other tourist receiving countries.

2.15 With relatively moderate investment costs and high occupancies, Mexican hotels in general are profitable. Hotel tariffs are controlled by the Government and increases are permitted only about every four years; however, hoteliers have in practice some flexibility in the rates they charge. Net profits may not be high, but other aspects of hotel investments are attractive, such as long-term capital gains, and high cash flow generation. With the expected upsurge in visitor traffic resulting from the devaluation of the peso, hotels in Mexico should in principle be further able to increase occupancies and profitability, but much would depend upon what happens to local costs and prices.

2.16 Average tourist expenditures in Mexico are high (about US\$24 a day) with even higher averages (US\$38 a day) for visitors arriving by air. In 1975, Mexico's gross foreign exchange earnings from tourism amounted to US\$800 million, excluding visitor transportation and border traffic earnings, and represented more than 13% of total exports of goods and non-factor services. The growth rate averaged 11.5% a year between 1960 and 1975 as compared to a growth rate of 10.7% annually in earnings from exports of goods and services. In the period 1970-1975, tourism earnings increased at a rate of 14% a year, despite a slowing down in the growth of visitor arrivals.

2.17 Handicrafts play an important role in distributing the benefits of tourism, particularly affecting the incomes of the very poor. In 1975, it is estimated that sales of handicrafts totaled Mex\$1.6 billion. This revenue directly affected the lives and incomes of at least 5 million Mexicans.

III. THE PROJECT

A. Project Background and Objectives

3.01 Baja California, the 1,300 km long rocky, desert peninsula stretching southward from the US border along Mexico's west coast, has been recently selected by the Government of Mexico for development that would also aim at preserving the delicate environment surrounding vast open spaces and kilometers of coastline that hold promise of providing sizeable tourist revenues. On the east side of the peninsula is the Sea of Cortez (Gulf of California); on the west, the Pacific Ocean. The climate is pleasantly dry, the vegetation is typical of desert lands. The peninsula's proximity to the west coast of the US, its natural attractions (beaches, sea, climate), its duty free status, and fishing potential provide Baja California with unique assets and an opportunity to tap one of the largest and richest tourist generating markets in the US. For this reason, tourism has been singled out by the Government of Mexico as the

most promising sector to bring about social and economic development in Baja California, especially in the southern part of the peninsula.

3.02 Tourism traffic to the southern part of the peninsula is limited, primarily due to lack of facilities. Population is sparse and the level of economic activity low, except in the capital city of La Paz. Tourists to this region in the past consisted of the wealthy who visited various points of interest in their own aircraft or yachts, particularly in the Cabo San Lucas area at the tip of the peninsula.

3.03 Recognizing this area's potential and in light of the Government's national policy to diversify geographically Mexico's tourism facilities, FONATUR undertook an analysis of several areas and sites along the whole length of the peninsula. The areas were studied with respect to the Government's regional policy to promote Baja California through the establishment of strategically located tourism development poles. Several sites were evaluated in conformity with economic criteria and with reference to such characteristics as physical conditions (nature of terrain, attractiveness, and climate); market potential; availability of infrastructure, including water supply and accessibility of the sites; land tenure situation; and proximity to existing urban areas. Out of a total of six potential areas selected on the basis of FONATUR's exhaustive study, the Government decided to proceed initially with the provision of tourism and other facilities in Loreto and San Jose del Cabo, both areas located in the southern half of the peninsula. These sites would permit Mexico to promote a diversified product and limit enclave-type development. They would provide an expanded opportunity to utilize more efficiently the large infrastructure investments already made by the Government and help spread the economic benefits of tourism throughout the state. The project would particularly cater to middle-income tourists, in contrast to the current high income tourists visiting the peninsula.

Loreto

3.04 Loreto is located on the Sea of Cortez, 360 km north of La Paz. The town, nestled between the sea and the mountains, is one of the earliest settlements in Baja California. Its population of 3,200 engages primarily in fishing and some agriculture. Visitors have been attracted by the scenic charm, but tourism development is still small and facilities inadequate.

3.05 The principal tourism zone would be located along the wide crescent beach at Nopolo, 7.5 km south of the town of Loreto. The site is one of great natural beauty. To the east lie the calm, blue waters of the Sea of Cortez, suitable for all types of water sports and fishing; to the west rise picturesque desert mountains. Average annual temperatures of 24°C, combined with a desert atmosphere, ensure constant pleasant weather. South of Nopolo is Puerto Escondido, a protected natural harbor surrounded by hills, and already popular with foreign visitors who arrive by sea or road.

3.06 A total area of 10,000 ha has been acquired by the Government at

Nopoló and Puerto Escondido for tourism purposes. The development, however, would be staged. The first stage, to be implemented over a nine-year period, envisages the construction of 1,000 hotel rooms, 2,000 apartel (apartment hotel) rooms and 655 condominium units and tourist villas.

3.07 At present, access to Loreto is provided by the recently completed 1,700 km paved transpeninsular highway. A jetty at Puerto Escondido, also recently completed, will connect the area with the mainland through ferry services. Air access to the area is poor. The airport near Loreto is small and capable of taking only light planes.

3.08 Project development will attract new residents to Loreto. The proposed project includes facilities for a population that is projected to grow from 3,000 to 25,000 in ten years. About 736 ha of land have been acquired by the Government and legal titles to property will be provided to present and future residents. Housing for new residents will be financed through programs already in operation in Mexico. To aid immigrant workers and the very poor who do not qualify for the federal programs, special arrangements will be made under the project to provide land, infrastructure, and temporary accommodation, as well as construction materials at cost and technical assistance for building houses.

San Jose del Cabo

3.09 The San Jose del Cabo site is located about 200 km south of La Paz on the southern tip of Baja California, a region long known to visitors from the west coast of the US. San Jose del Cabo is reminiscent of European towns with narrow, hilly streets. Beautiful beaches stretch for kilometers on both sides of the town, and an attractive sweet-water lagoon--a rarity in a desert region--offers special interest. The climate is like that of Loreto. The sea, however, is rougher than at Loreto and is more suitable for boating and fishing than swimming.

3.10 The region has benefited from both private and public investments in hotels and infrastructure. Several hotels have been built along the coast from San Jose del Cabo to Cabo San Lucas, 30 km to the southwest (425 hotel rooms); there are also small air strips, generally owned by the hotels. More recently, the Government initiated the construction of an international airport 20 km north of the town of San Jose del Cabo, but for budgetary reasons the project has not yet been completed. Road access is provided by the recently completed transpeninsular highway. The Government also recently completed the main works for water supply but has not yet provided the area with a distribution system.

3.11 The master plan for the development of this area will make use of investments already made in infrastructure facilities by integrating them and the town of San Jose del Cabo with the main tourism facilities to be built 2 km west of the town along a 10 km long beach of fine sand. A total area of 1,750 ha has been acquired by the Government, though not all land will be needed immediately. The first stage, to be implemented over nine years, envisages the construction of 1,100 hotel rooms, 2,050 apartel rooms and 305 condominium units and tourist villas.

3.12 Facilities in the towns of San Jose del Cabo will be upgraded and expanded to meet the needs of the local population which is projected, like Loreto, to grow from 3,500 to 25,000 in ten years. The town will benefit from project investments similar to those planned for Loreto, which would include investments to aid migrants and the poorer sections of the population. As part of the project, the international airport will be completed.

Project Integration and Environmental Considerations

3.13 The land use plans for the tourism and urban zones in both the project areas attempt to balance the best possible protection of the physical environment with the most economic use of land. In the tourism areas, land use has been studied, first, in terms of the likely pattern of visitor activity; second, in terms of space requirements and the needed physical facilities to accommodate those activities; and, third, in terms of the need to preserve the existing natural environment. For the towns of Loreto and San Jose del Cabo, special attention was paid to the expected structure and functioning of the towns' economy and to the spatial distribution of urban functions. Accompanying these land use plans are detailed zoning and building regulations. An important feature of these regulations is that all structures will have building density and height limitations so that visual integrity can be maintained.

3.14 Because of the fragile nature of the ecological system of the peninsula, special attention has been paid to the impact of the proposed projects and the measures that will need to be taken to avoid deterioration of the environment (Annex XII). As presently designed, no significant external environmental problem will result from these developments; rather than impoverishing the environment, the project will significantly induce changes to the contrary. Sewage pollution problems were analyzed and the solutions adopted will preserve the diversity of marine life of the sea. Large tracts of land have been reserved as "green areas"; buildings will be set back from the beach, and not allowed on dunes. Provision has been made for studies to initiate proper water management, as well as for preservation of the rare sea fauna and wildlife found in the area. The lagoon at San Jose del Cabo will be cleared, dredged, and conserved. Velocity check dams will eventually be built at San Jose del Cabo, both to preserve the lagoon and help recharge the existing aquifer. Provision has also been made for programs and studies for conservation of the environment around Loreto and Puerto Escondido, including the outer islands. The area has an extraordinary collection of sea lions, seals, birds, and animals which are of interest to tourists but which must be protected, possibly by creation of a marine or national park. The results of the wildlife conservation and coastal zone water management studies, and the appropriate actions to be taken will be reviewed with the Bank. In addition, four stations for fauna conservation and protection would also be built under the project and located at strategic points along the Sierra. In Puerto Escondido, facilities for trailers and boats would be provided to reduce the pollution being created by visitors. Finally, the urban plan for Loreto and the path of aircraft over San Jose del Cabo have been drawn up so as to avoid noise pollution.

3.15 Private hotel investors are reluctant to be first in a new destination and generally tend to wait until all tourism infrastructure is in place before investing, which may be a year or more later than desirable from a financial and economic point of view. These first investments in superstructure facilities are crucial in setting the architectural tone of the resort, and if left to private investors they may not match the painstaking planning that will characterize the Government's infrastructure investment. Accordingly, financing is included in the project for construction of a first hotel of 250 rooms of medium category at both Loreto and San Jose del Cabo, which would set the market and architectural tone of the resorts, demonstrate proper environmental standards, and accelerate the generation of benefits from investments in infrastructure and other facilities.

B. Project Description

3.16 In each of the Loreto and San Jose del Cabo sites, the project would include the following main elements, described further in Annex II.

- (a) infrastructure and other facilities for the tourist zones;
- (b) a medium category 250-room hotel for each development area;
- (c) infrastructure and other facilities for the towns;
- (d) airport facilities; and
- (e) investment promotion, community development activity, conservation studies and programs for both areas, and a tourism market and economic study.

Loreto

3.17 The road network in the tourism zone at Loreto (Nopolo) includes the construction of a two km long boulevard parallel to the beach, set back 200 to 300 meters, and an internal two-lane loop road that would provide access to single family cluster houses and condominiums. In addition, a central pedestrian spine with a series of squares and plazas would run parallel to the beach giving easy access to the community. At Loreto, a new entrance road would connect the transpeninsular highway with an improved street system and the center of the town. Landscaping, storm drainage facilities, and street lighting would be provided for the entire network.

3.18 To meet the electric power needs of both the tourism area and the town, a 115 kv transmission line will be constructed from the town of Villa Constitucion 150 km away, a less expensive undertaking than installing new generating capacity at Loreto. In addition, a new substation and transformer will be installed and a distribution system built.

3.19 An integrated telecommunications system will be installed to serve both tourists and local inhabitants. The new exchange building will be located in the town, and the long distance circuits will be tied into the regional microwave network.

3.20 Water supply for the tourism zone will be tapped from an aquifer about 5 km to the north. It would involve the construction of a 10 km distribution system and the use of an existing water storage tank. For the town, the presently used aquifer will continue to be the source of water supply, but the main distribution system will be expanded.

3.21 Storm water will be cleared from the tourism zone by allowing it to flow along street pavements to an artificial lake prior to being discharged into the sea. An open channel going through the middle of the existing town will intercept storm water from the upper portions of the town and discharge it into a nearby creek.

3.22 Sewage from the tourism zone will flow by gravity to two pumping stations and from there will be pumped to stabilization ponds for treatment. The effluent after treatment will be used for irrigation purposes. A similar but separate and smaller sewerage system will serve the town. A sanitary landfill site for disposal of solid waste has been located 5 km north of the town of Loreto. Garbage trucks and other equipment are included in the project.

3.23 The community and cultural center in the tourism zone, which will be the focal point of activities for the resort, will consist of a large central plaza surrounded by various facilities, including an auditorium, as well as rental space for a post office, shops, cafes, and restaurants. Other buildings would include an emergency clinic, and a fire and police station. A main recreation and landscape feature of the tourism area is an 18-hole golf course, of which nine holes and a clubhouse would be constructed under the project. Beach facilities would include a snack bar and restaurant. The town of Loreto would receive a variety of community facilities such as parks, playgrounds, a health clinic, schools, and a local market. The existing central plaza would be upgraded, paved, and landscaped. Some existing buildings around the plaza would be improved. Administrative offices would be located in the town.

3.24 Adjacent to the community and cultural center, a boat house and pier will be constructed for aquatic sports and fishing, as well as excursions to the neighboring islands. In addition, a year-round boat anchorage will be located at the southern end of the tourism zone at Nopolo, well protected by a 60 m rocky promontory. Public beach facilities will be provided to be used by the local population.

3.25 The project includes a 250-room hotel of medium category to be completed at about the same time as the infrastructure and other facilities. The exact location of the hotel in the tourism zone will be subject to Bank approval.

3.26 The small general aviation airport at Loreto will be upgraded and expanded to handle larger aircraft and larger volumes of traffic. Works would include the lengthening, widening, and strengthening of the existing runway, and the construction of a new taxiway, apron, and terminal building. Also included in the project will be the construction of a control tower, a three-bay crash, fire, and rescue building, a fuel farm, an access road, a parking area, and the installation of fencing, visual aids, communication and radio navigation equipment.

San Jose del Cabo

3.27 The road network at San Jose del Cabo will consist of a 1.6 km main boulevard extending from the transpeninsular highway to form a circuit around the community and cultural center and a two-lane road that connects the tourism zone with the town's main street. The town and the tourism zone will each have a focal point of activity, and a pedestrian way with small parks and plazas will connect the two. The entire network will have street lighting and appropriate landscaping.

3.28 With the installation of a 115 km transmission line between La Paz and San Jose del Cabo now nearing completion, San Jose and the surrounding area will be served with electric power from generating plants in La Paz. The project makes provision for a substation, transformers, and local distribution lines.

3.29 The existing telecommunications system will be expanded to serve tourism as well as the projected needs of the local population. A new exchange building will be built in the town and equipment installed in stages.

3.30 Water will be supplied by four wells that have been drilled and by a major aqueduct already constructed to serve several small towns in the area. Provision has been made for water storage facilities, pumping stations, and a distribution system.

3.31 The storm water drainage system consists of two interceptors that will collect storm water from the higher areas surrounding the town and the tourism zone. The interceptor in town will discharge the water into a nearby estuary, while another in the tourism zone will discharge the water into the sea.

3.32 The sewage from the tourism zone and the town will be pumped to stabilization ponds. The effluent after treatment will be used for irrigation. A landfill site will be located between the town and the airport for disposal of solid waste. Provision has been made for garbage trucks and other needed equipment.

3.33 Hotel and other accommodation in the tourism zone have been planned around a community and cultural center to be built under the project which will consist of a central plaza surrounded by various facilities, including an auditorium and rental space for shops, restaurants, and offices. Recreational facilities will include a fishing pier and boat dock, tennis courts, and some beach facilities. Because swimming is unsafe in front of the tourism zone during certain periods, a marine structure would be provided to allow a safe bathing area. Buildings included in the project consist of a police and fire station, an emergency clinic, schools, a health center, and some staff housing. In addition, some existing buildings in the town will be remodeled and repaired, and an old, interesting cemetery landscaped and preserved.

3.34 As in the case of Loreto, the project includes the construction of a 250-room hotel of medium category. The exact location of the hotel in the tourism zone will be subject to Bank approval.

3.35 The project makes provision for completion of the airport at San Jose del Cabo. This will include construction of a terminal building, a control tower, a three-bay crash, fire, and rescue building, a fuel farm, and an automobile parking lot. It will also include the installation of communication, navigation and visual aids as well as perimeter fencing.

3.36 Water management, conservation (para. 3.14), market and economic (para. 4.26) studies are also included in the project (Annexes II and X).

C. Cost Estimates

3.37 The cost estimates and the foreign exchange component of the project elements are summarized in Table 1 on page 13.

3.38 Baseline costs reflect October 1976 price levels, converted into US dollars at an exchange rate of US\$1 - Mex\$19.90, the rate current at that time. An allowance of 10% to 15% of civil works and equipment costs has been made to cover physical contingencies, depending on the degree of design detail available for individual project components. On average, the allowance amounts to 13% and is reasonable since most of the cost estimates are based on fairly detailed design work and equipment lists. Price contingencies have been calculated in dollar terms and take into account the projected implementation schedule as well as any likely increases in price levels during the construction period. Mexico has lately been experiencing major price increases, especially since the recent devaluation of the peso, the first in 22 years. Total provision for contingencies amounts to US\$24.5 million, which represents 41.3% of baseline costs, or 29.2% of total project costs (Annex I, Table 9).

3.39 Roads, water supply, and sewerage components of the project are in draft final design stage, requiring only minor revisions. The telecommunications and electric power component cost estimates are in line with costs of similar works recently carried out in Baja California. The hotel as well as community facilities and buildings were designed from detailed spatial programs for each element, accompanied by floor plans, elevations, and sections at a scale of 1:200. The Ministry of Human Settlements and Public Works (SAHOP) is in the process of preparing final design drawings for the airport components. Cost estimates for equipment procured locally include taxes, and transportation to sites, port, warehouse, and handling charges; charges are equivalent to about 15% of the c.i.f. prices. Since Baja California is a free zone, no import duties are applicable.

3.40 For the project as a whole, consultants' services are estimated to total 1,075 man-months over a 3-1/2 year period and to cost about US\$3.9 million. Some 64 man-months would be provided by foreign consultants.

D. Execution and Operation

3.41 Basic responsibility for executing the proposed project would rest with FONATUR with the exception of electric power, telecommunications, and the airports, which would be carried out by other government agencies. The

Table 1: Project Cost Estimates and Foreign Exchange Component

Project Items	Mex. \$ (million)			US\$ (million)			Percent of Foreign Exchange
	Local	Foreign	Total	Local	Foreign	Total	
<u>Tourism Area of Loreto</u>	75	138	213	3.8	6.9	10.7	64
Civil Works	54	93	147	2.7	4.7	7.4	
Equipment	8	42	50	0.4	2.1	2.5	
Consulting Services	13	3	16	0.7	0.1	0.8	
<u>Town of Loreto</u>	58	73	131	2.9	3.7	6.6	56
Civil Works	48	59	107	2.4	3.0	5.4	
Equipment	2	12	14	0.1	0.6	0.7	
Consulting Services	8	2	10	0.4	0.1	0.5	
<u>Tourism Area and Town of San Jose del Cabo</u>	82	106	188	4.2	5.3	9.5	56
Civil Works	63	64	127	3.2	3.2	6.4	
Equipment	7	38	45	0.4	1.9	2.3	
Consulting Services	12	4	16	0.6	0.2	0.8	
<u>Pilot Hotels</u>	91	109	200	4.6	5.4	10.0	54
Civil Works	71	65	136	3.6	3.2	6.8	
Equipment	7	42	49	0.4	2.1	2.5	
Consulting Services	13	2	15	0.6	0.1	0.7	
<u>Airports</u>	85	105	190	4.2	5.3	9.5	56
Civil Works	64	67	131	3.2	3.4	6.6	
Equipment	7	38	45	0.3	1.9	2.2	
Consulting Services	14		14	0.7		0.7	
Community Development	7	1	8	0.3	0.1	0.4	16
Pre-Opening Activities	27		27	1.4		1.4	-
Investment Promotion	3	17	20	0.1	0.9	1.0	88
Project Administration	57	11	68	2.9	0.5	3.4	16
Market and Economic Study	—	8	8	—	0.4	0.4	100
<u>Base-Line Cost</u>	485	568	1,053	24.4	28.5	52.9	54
<u>Contingencies:</u>	221	268	489	11.1	13.5	24.6	55
Physical Increase	43	71	114	2.1	3.6	5.7	63
Price Increase 1/	178	197	375	9.0	9.9	18.9	52
Land Acquisition	129		129	6.5		6.5	-
<u>Total Project Cost</u>	835	836	1,671	42.0	42.0	84.0	50

1/ Assuming an average price increase of 12% per year for 1977-1979 and 10% for 1980 except for equipment, for which an 8% increase per year has been assumed for 1977-1979 and 7% for 1980. Price contingencies are "dollar contingencies" and have been converted to Mexican pesos at an exchange rate of US\$ 1 = Mex\$ 19.9 for illustrative purposes only.

overall financial position of FONATUR is sound with adequate net working capital generated from its operations (Annex VI). FONATUR is managed by able and highly qualified individuals.

3.42 FONATUR has been concentrating its efforts in developing Cancun and Ixtapa-Zihuatanejo. These require diminishing attention, since the first phase of the Cancun project is completed while that of Ixtapa-Zihuatanejo is nearing completion. With the invaluable experience it has gained, FONATUR is now in a position to focus its attention on Baja California.

3.43 The land tenure system in Baja California has been an important consideration in designing the institutional arrangements to implement this project. In the tourism zone in Loreto (Nopoloo-Puerto Escondido), an area totaling 10,000 ha along 20 km of coastline was expropriated from private individuals and transferred to FONATUR. The town of Loreto, however, is built on ejidal land and titles to the existing urban property in and around the town were neither clear nor legal. In order to legalize the situation, the Government expropriated the urban land, including 4 km of coastline. The Government, however, cannot legally transfer the land directly to FONATUR. Therefore, a new trust fund will be established, with several public agencies as members, including the Land Regularization Committee (CORETT) and the state government. While this new trust fund will own the land, FONATUR will be solely responsible for the investment activities in the town under the project and for the sale of urban property. In San Jose del Cabo, a similar land situation existed in the town as well as in the tourism zone. Accordingly, about 1,750 ha of land were expropriated and will be transferred to another new trust fund which will also be managed by FONATUR. The satisfactory establishment of the trust funds would be a condition of loan effectiveness.

3.44 FONATUR will contract with the Federal Electricity Commission (CFE) and the Telecommunications Corporation of Mexico (TELME~~X~~) to design and construct the electric power and telecommunications networks. Responsibility for operation and maintenance will also be assumed by CFE and by TELME~~X~~. Technical designs and specifications of hydraulic works as well as water, sewerage, and storm water drainage systems would be subject to approval by the Ministry of Agriculture and Hydraulic Resources (SARH), although the actual implementation would be the responsibility of FONATUR. Operation and maintenance of these systems will be the responsibility of special local commissions (juntas) set up for the purpose, which in the initial years will receive support from FONATUR. Roads, streets, and solid waste disposal in the towns of Loreto and San Jose del Cabo will be maintained and operated by the local municipality. In addition, government agencies such as the Ministry for Health and the Ministry for Education will be responsible for providing health and education services, and for adequately staffing and maintaining the relevant facilities.

3.45 Responsibility for design and construction of airport facilities will be that of SAHOP and SCT. Four agencies will be responsible for their operation and maintenance, including SAHOP, the Airports and Auxiliary Services Agency (ASA), the Aeronautical Radio Company of Mexico (RAMSA), and the National Company of Aviation Combustibles (NACOA).

3.46 All these agencies have the requisite experience and competence to execute the respective components of the project. FONATUR will not later than June 30, 1978 enter into contractual arrangements with CFE and TELMEX on the scope of the electric power and telecommunications program, the cost and construction timing. The project areas, however, will have to be assured of services and facilities not financed under the project. Accordingly, assurances have been obtained that the project areas will receive adequate aviation, water supply, power, and telecommunication services. Also, to protect the project investments the Government has agreed to adopt not later than June 30, 1978 land use and zoning codes that would regulate development on land immediately surrounding the project areas.

3.47 To ensure proper supervision of design and construction as well as to coordinate efforts of other agencies, a Project Unit to deal with investments in Baja California would be set up within FONATUR (Annex VI). The Project Unit would have a Director, stationed in Mexico City, who would be responsible for the project and coordinate the activities in both sites through managers, who would spend half the time in Mexico City and the remainder in Baja California. In addition, each site would have a chief engineer stationed permanently in Baja California, and a staff of technicians, accountants, sociologists, community development workers, and procurement officers.

3.48 FONATUR would be responsible for the disposal of land to private investors for the construction of hotels, restaurants, villas, and other facilities. It would also be responsible, through the new trust funds, for disposal of the urban property in the two towns. In addition, in the tourism zones of Loreto and San Jose del Cabo, FONATUR will be responsible for various facilities including parks and plazas, roads and streets, landscaping, beaches, beach facilities, the community and cultural center, and recreation facilities. In the case of the pilot hotels, FONATUR plans to hand over operation and management to Nacional Hotelera, a Government owned hotel operating company in which FONATUR controls a majority share. Arrangements for financing, managing and operating the hotels would be subject to Bank approval.

3.49 No hotel training facilities will be constructed under the project. A large and modern hotel training center which includes a 109-room practice hotel has recently been constructed by the Secretariat of Tourism at La Paz, at a cost of Mex\$60 million. These facilities are considered adequate for the needs of the proposed project. The Government has already set up a trust fund to operate and manage these facilities as a hotel school and assurances were obtained that the Government will take such actions as are necessary to adequately satisfy the staff requirements of the hotels in the project areas.

3.50 Final designs, plans, and specifications for the project will be submitted to the Bank for approval. This would include architectural designs for the hotel, and land use and zoning regulations for both areas. Because of complex problems in coordinating the execution of all parts of the project on schedule, a critical path chart now under preparation will be completed. This chart would be reviewed by all parties concerned every three months and the results of such reviews would be communicated to the Bank.

E. Financing Plan and Lending Arrangements

3.51 Total estimated cost of the project is US\$84 million. It is proposed that the Bank loan of US\$42 million cover the foreign exchange component, or 50% of total project costs. The balance would be provided through budgetary allocations of the Government, which would also meet any cost overruns. The consolidated financing plan for the project including contingencies can be summarized as follows:

Table 2: Consolidated Financing Plan
(US\$ thousands)

Component	Estimated Cost	Source of Funds	
		Bank Loan	Government Contribution
Loreto	25,277	14,745	10,532
San Jose del Cabo	13,484	7,331	6,153
Pilot Hotels	15,410	8,236	7,174
Airports	14,293	7,948	6,345
Community Development	0,546	0,273	0,273
Proj. Admin. & Pre-Opening Expenses	6,548	2,262	4,286
Investment Promotion	1,402	0,701	0,701
Market & Economic Study	0,504	0,504	-
Land Acquisition	6,482	-	6,482
Total	<u>83,946</u>	<u>42,000</u>	<u>41,946</u>

3.52 In line with Government policy, and as was agreed by the Bank in the case of the Ixtapa-Zihuatanjo project (and by IDB for the Cancun project), it is proposed that the proceeds of the Bank loan for the Baja California project be made available to FONATUR as equity contribution for timely execution of project components. In order to maintain financial standards, however, certain safeguards have been adopted to ensure that FONATUR would have no difficulty in recovering its investment and earning a reasonable return (para. 4.22).

F. Procurement and Disbursement

3.53 Major civil works and equipment contracts would be awarded on the basis of international competitive bidding. Mexico currently has legislative guidelines for procurement of goods and services under public sector financed projects which are basically in line with Bank guidelines.^{1/} Project items have been grouped into packages (Annex I, Tables 2 to 6) in order to encourage such competitive bidding, but bidders would also be able to bid on individual items. A high percentage of the building materials required for the project is produced in Mexico; however, because of lower transport costs and the duty free status of Baja California, a large portion of goods may come from the US or Canada. In evaluating international bids for equipment and furniture, local manufacturers would be allowed a preferential margin of 15% of the c.i.f. price of competing imports or the prevailing level of customs duties, which-

^{1/} Law on Public Works and Contracts (Dec. 21, 1965) and General Bases and Standards for Public Works Contracts (Jan. 26, 1970).

ever is lower. Some civil works and equipment contracts for such items as earthworks, field offices and beach facilities would be too small to attract foreign bids. It is therefore proposed that these civil work contracts, each not to exceed US\$500,000 in value, and equipment contracts, each not to exceed US\$100,000 in value, would be awarded after local competitive bidding. The total value of such contracts would not exceed US\$4 million equivalent. Minor civil works such as landscaping, gardening and environmental sanitation, the total cost of which is estimated not to exceed US\$1 million equivalent, would be carried out on force account by FONATUR. Since the navaid equipment for the airports should be compatible with equipment used in all airports in Mexico, procurement of this equipment, valued at US\$700,000, would be negotiated directly with the supplier.

3.54 FONATUR would be responsible for advertising requests for tenders, issuing tender documents, evaluating bids, and awarding contracts for all project components, with the exception of the airports, electric power, and telecommunications. SAHOP and CFE have been past beneficiaries of Bank loans and would have no problem following established procedures. Because of the present setup of TELMEX and the manner in which that organization implements projects and procures equipment, the Bank loan will not finance the telecommunications component.

3.55 Disbursement of funds from the loan would be on the following basis:

- (a) 100% of foreign expenditures for directly imported equipment and furniture or 100% of the ex-factory cost of locally manufactured equipment and furniture;
- (b) 50% of total expenditures for civil works, consulting services, community development activities, investment promotion and project administration; and
- (c) 100% of total expenditures for wildlife, coastal water, conservation, market and economic studies.

3.56 A schedule showing the estimated rate of disbursement is given in Annex I, Table 8. Disbursements would be fully documented and any funds remaining in the loan on completion of the project would be cancelled. In order not to delay implementation of the project, it is proposed that a part of engineering expenditures incurred after December 1, 1976, and not exceeding US\$300,000 equivalent, be financed retroactively.

IV. JUSTIFICATION

A. Market Demand

Tourist Growth Rates and Projections

4.01 Foreign tourism to Mexico has been growing at an average rate of 10% a year over the last 15 years. In only two years since 1961 (1974 and 1975) has the growth rate been less than 8.7%. In 1974 the number of visitor arrivals increased by 3.7%; in 1975 it declined 4.3% (the first decline since 1953). This decrease was mainly attributable to the economic reces-

sion in the US and to Mexico's uncompetitive position resulting from an overvalued peso. Visitor arrivals totaled 3.22 million in 1975. Table 3 shows recent trends in foreign visitor arrivals.

Table 3: Foreign Visitor Arrivals (Thousands)

Origin	1970	1974	1975	1976 (est.)	Average	Annual
					1970/74	1970/76
United States	1,980	2,860	2,720	2,870	9.7	6.4
Canada	70	130	120	130	16.7	10.9
Other	200	370	380	330	16.6	8.7
Total	2,250	3,360	3,220	3,330	10.5	6.8

The factors that affected the total flow of visitors in the 70s had a smaller impact on visitors coming to Mexico by air. The average annual growth of visitors traveling by air was 16% in the 1970-74 period and 11% between 1970 and 1976.

4.02 In 1975, foreign visitors spent a total of 34 million nights in the country, which averaged to a stay of 10.6 nights per visitor. Hotel statistics indicate that they stayed approximately four nights in places such as Mexico City, Acapulco, and Puerto Vallarta, which indicates that tourists typically visit more than one destination while in the country. Foreign tourists, however, now seem to be following a single destination trend which in the long run may generate more tourism in the resorts along the coast. Mexicans also account for a significant share of overall tourism activities in Mexico (para. 2.05).

4.03 FONATUR, on the basis of its studies, projects both foreign and domestic tourism to grow at an average annual rate of 9% over the next ten years. These visitor and visitor night projections, as well as projections on a more conservative growth rate assumption of 6%, are summarized in Table 4.

Table 4: Visitor and Visitor Night Projections to Mexico

Item	1976	1980	1985	1990
<u>Number of Visitors (million)^{1/}</u>	(est.)			
Foreign (Growth Rate 9%)	3.3	4.7	7.2	11.1
Foreign (Growth Rate 6%)	3.3	4.2	5.6	7.5
Domestic (Growth Rate 9%)	16.5	23.3	35.8	55.1
Domestic (Growth Rate 6%)	16.5	20.8	27.9	37.3
<u>Number of Visitor Nights (million)</u>				
Foreign (Growth Rate 9%)	35.0	49.4	76.0	117.0
Foreign (Growth Rate 6%)	35.0	43.0	59.1	79.1
Domestic (Growth Rate 9%)	31.0	43.8	67.3	103.6
Domestic (Growth Rate 6%)	31.0	39.1	52.4	70.1

^{1/} Foreign visitors include Mexicans residing abroad.

4.04 Market projections for Baja California have been established on the basis of planned accommodation development and their likely utilization at Loreto and San Jose del Cabo (Table 5). Length of stay and occupancy rates are based on past experience in Mexico. Because of its vicinity to the US, roughly 70% of all visitors to these sites are expected to be foreigners (78% in Loreto and 61% in San Jose del Cabo), which is somewhat higher than in other Mexican resorts. The number of visitors has been calculated on the assumption that they will visit only one of the two project areas in the course of a trip to Baja California; the target number of visitors could be lower if some tourists (possibly up to a fourth) visit both project areas. The target figures range between 0.3% and 3% of the overall market projections for the number of guest-nights spent in Mexico over the 1980-1990 period under the conservative 6% growth rate (0.5% to 4% in the case of foreign visitors and 0.2% to 2% in the case of Mexicans). These targets are reasonably attainable if adequate air access and promotion are provided.

Table 5: Accommodation and Visitor Projections,
1980, 1985 and 1990

Item	1980/81	1985	1990
<u>Hotels and Apartels</u>			
Number of Rooms	800	4,950	6,150
Occupancies (%)	50	63	70
Double Occupancy Factor (guests/room)	1.8	1.8	1.8
Average Length of Stay (days)			
For Foreigners	4	4	4
For Mexicans	3	3	3
<u>Condominia and Villas</u>			
Number of Rooms	-	1,115	2,330
Occupancies (%)	-	50	50
Double Occupancy Factor (guests/room)	-	2.5	2.5
Average Length of Stay (days)			
For Foreigners	-	6	6
For Mexicans	-	10	10
<u>Market Targets</u>			
Visitors	66,000	600,000	800,000
Visitor Nights	250,000	2,500,000	3,900,000

Potential Market Competition for Baja California

4.05 FONATUR has undertaken market studies for Baja California resorts which indicate that in the case of foreign tourists the project will be particularly appealing to the market from the southwestern US, in particular from the state of California. It will also be in a position to compete with southern California resorts where some eight million Californian and non-Californian visitors spent some 35 million nights in 1975, and Hawaii where 2.8 million visitors spent 32 million nights in the same year. In addition, Baja California will have to compete with other northwestern

Mexican resorts where some one million visitors from the US and Canada spent some four million nights in 1975. The studies further indicate that more than two-thirds of the tourists would come by air, that the majority would need first-class rather than luxury-type accommodation, and that not all of the visitors to Loreto and San Jose del Cabo will come to Mexico solely because of the project. In the case of Mexicans, FONATUR's studies indicate that the project resorts will attract visitors, mostly from Mexico City, Guadalajara, and Monterrey, some of whom would normally travel to northwestern Mexico (in particular to Mazatlan and Puerto Vallarta) and to the southwestern United States.

4.06 The main market segments for the project^{1/} (and their projected annual growth rates) are the following: (a) US visitors to southern California who travel by air (2.2%); (b) US visitors to Hawaii (8.3%); (c) Canadian visitors to the west coast of the US who travel by air (4.4%); (d) car travelers from California, Nevada, Utah, and Arizona who travel more than 2,000 miles roundtrip (1.2%), and (e) US and Mexican visitors to Mazatlan and Puerto Vallarta (9.9%). Projecting the growth of each segment with these rates, the target numbers of visitors to the project areas by 1980 would represent only some 1% of the potential market attributed to the segments defined above, which clearly do not exhaust the market. Given that the project meets the major criteria that attract visitors to a given area (appealing climate and natural environment; reasonable vacation cost, including the cost of transportation; proximity to major markets), the visitor target number, both as a proportion of total projected volume of tourism to Mexico and as a proportion of the projected potential market, appears feasible. In order to compete with destinations in southern California and Hawaii, however, comparable facilities need to be provided. Room tariffs in 1975 in southern California and Hawaii averaged some US\$26 and US\$30 per night respectively. The market strategy for Baja California therefore calls for construction of facilities of good quality to be provided to visitors at prices slightly lower than in southern California and Hawaii. The projected average hotel room tariff in the two project areas is US\$25 per night.

Travel Modes and Expenditures

4.07 Most visitors to the proposed project areas are expected to travel by air. Experience at other resorts has demonstrated that attracting large numbers of foreign visitors by air to Mexico requires provision of flights from major points in the US. The airport at San Jose del Cabo is already included in the bilateral air agreement with the US and can be served by both US and Mexican airlines from Los Angeles, Tucson and Phoenix. Loreto, however, is not. Accordingly, assurances have been obtained from the Government that it will have Mexican scheduled airlines serve San Jose del Cabo and Loreto on domestic segments of international routes to and from major tourism generating countries to coincide with the opening of the first two hotels at each site. In addition, assurances have been obtained that the Government will make its best efforts to retain San Jose del Cabo in future bilateral air agreements and include Loreto in these bilaterals, so that scheduled inter-

1/ These segments comprise visitor flows rather than population groups. Since some people travel to more than one place during a one-year period, the segments overlap in terms of population, but not in terms of overall visitor flows.

national air service can be initiated to coincide with the opening of the first two hotels at each site. The flying time from Los Angeles to Loreto would be just over 1-1/2 hours and to San Jose del Cabo 2 hours, as compared to more than 5 hours to Hawaii. In addition to arrivals by air, it is expected that some 30% of the visitors will use the highway that connects the US border with the tip of Baja California peninsula, providing access to both Loreto and San Jose del Cabo. The road distance between Los Angeles and Loreto is some 1,500 km and some 2,000 km in the case of San Jose del Cabo.

4.08 In mid-1976, foreign visitors to Mexico spent an average of US\$24 per day, with visitors arriving by air spending more than US\$38 per day. The percentage of total guest-nights spent by Mexicans and foreigners and the average daily expenditures in late 1976 prices in the two project areas is expected to be as follows:

Loreto			San Jose del Cabo		
Mexicans	Foreigners	All Visitors	Mexicans	Foreigners	All Visitors
(25.7%)	(74.3%)	(100%)	(39.1%)	(60.9%)	(100%)
US\$25.8	US\$39.0	US\$35.6	US\$28.1	US\$42.7	US\$37.0

The average expenditure figures for foreign visitors to the project areas are a little more than the average for foreign air travelers to Mexico as a whole (many of whom do not use paid accommodation, therefore spending little, and who do not represent a typical resort visitor), but less than for foreign tourists to Mexico who stay ten days or less in the country and spend an average of US\$45 per day; for those who come on charter groups (US\$60); and for those visiting destinations such as Cancun and Ixtapa (US\$48). In projecting the levels of expenditures, it is assumed that foreign visitor expenditures will decline after the August 1976 devaluation. Also as a reflection of the devaluation, the projected expenditures of Mexican tourists are assumed would be lower than recent experience in Mexican resorts indicates (over US\$45 per day in Cancun in mid-1976). Overall, the expenditure projections are therefore reasonably conservative and consistent with the facilities offered.

4.09 Based on experience in other tourist resorts in Mexico, the breakdown of projected average expenditures of foreign visitors is calculated to be as follows: accommodation, food and beverages 58%; entertainment 14%; local transportation 11%; shopping 12%; and other 5%. The expenditure breakdown of Mexican visitors is only slightly different; they are expected to spend a higher proportion on accommodation and lower on shopping and local transportation.

B. Development of Tourism Facilities

4.10 The project calls for a gradual build up of accommodation capacity in both zones over the 1980-1987 period (see Table 6). Of the total projected accommodations, one-third would be of the pure hotel type and the remainder would be apartels.^{1/} There is no significant difference between hotels and apartels in terms of operation from the point of view of services received by the tourist (Annex VIII); ownership would be different in that apartel units would be sold to individual purchasers by the developer.

^{1/} Because of the small proportion of villa and condominium units, the expected development of these facilities are not shown in this table.

Table 6: Development of Capacity 1980-1987
(Number of Rooms)

Year	San Jose del Cabo		Loreto		Total	
	Annual	Cumulative	Annual	Cumulative	Annual	Cumulative
1980	400	400	400	400	800	800
1981	300	700	500	900	800	1,600
1982	300	1,000	400	1,300	700	2,300
1983	400	1,400	400	1,700	800	3,100
1984	450	1,850	600	2,300	1,050	4,150
1985	500	2,350	300	2,600	800	4,950
1986	400	2,750	200	2,800	600	5,500
1987	400	3,150	200	3,000	600	6,150

When fully developed, most of the accommodations are expected to be of the A category in line with market expectations rather than the AA or B type, as follows:

<u>Category</u>	<u>San Jose del Cabo</u>	<u>Loreto</u>	<u>Total</u>
AA	475	450	925
A	2,200	2,100	4,300
B	475	450	925

4.11 Private investors have long been interested in participating in tourism development in Baja California. Several projects have been submitted to the Government for approval but many have not gone forward for such reasons as land tenure problems and the absence of needed infrastructure. Recent discussions with potential hotel developers and investors have confirmed a strong interest in building at Loreto and San Jose del Cabo and the prospects for hotel and apartel investments are considered favorable. No binding commitments have been made, however. Investors are reluctant to be the first in a new development. Therefore, as noted previously (para. 3.15), provision is made in the project for the construction of a pilot hotel of 250 rooms of the A category at each site. In addition, for successful launching of the resorts, the Government is prepared to take all necessary action, including the provision of adequate financing, to ensure the construction and operation of an additional hotel with a capacity of not less than 150 rooms at each site, to be opened at the same time as the hotels being financed under the project and another 600 rooms at each site three years thereafter. The Government will also make its best efforts to have an additional 900 rooms in operation at each site seven years after the project is implemented to ensure the economic viability of the program of investments.

4.12 To test the financial viability of these facilities, operating projections for a typical 250-room hotel and 250-room apartel (Annex VIII) demonstrate the profitability of such investments. The rate of return on equity in hotel investments in the sixth year of operation is 12%, increasing to 14% in the tenth year. With respect to apartels, the rate of return on equity is 11% in the fourth year and 17% in the sixth year of operation. Investments in apartels are financially more attractive than in hotels because of lower capital and operating costs. The apartel concept also makes it easier for promoters to raise capital among small investors.

4.13 Under the Mexican Constitution, foreigners cannot directly own land within 100 km of international borders and 50 km of the coast. However, the Decree of April 29, 1971 permits accredited Mexican banks to act as trustees for foreigners. The banks can purchase land on behalf of foreigners and hold the land for them in trust for a 10-year period, renewable to a maximum of 30 years. After 30 years, foreigners can seek a new trust with another bank or instruct the bank to sell the land. This decree has helped to solve one of the thorniest problems that existed for private foreign investors.

C. Financial Aspects

4.14 For financial evaluation purposes, the proposed investments have been divided into three groups: (a) items relating to the development of the urban and tourism zones in Loreto and San Jose del Cabo, including commercial, recreational and urban facilities and some infrastructure, but excluding telecommunications and part of the investments in electric power, water supply and sewerage components; (b) the pilot hotels to be financed under the project; and (c) the airports at Loreto and San Jose del Cabo.

Urban and Tourism Development

4.15 The capital costs of urban and tourism zone development are estimated at US\$34.1 million including financial charges during construction but excluding price contingencies. Although these costs include the cost of electric power, water supply and sewerage distribution networks, they exclude: (a) investments in water supply and sewerage headworks and equipment which have been analyzed separately (para. 4.17) and (b) investments in electric power headworks and telecommunications for reasons explained in para. 4.18. The basic financial objectives which the urban and tourism zone investments are expected to meet is the recovery of investment costs and the earning of a reasonable rate of return. These would be achieved mainly by FONATUR through the sale of hotel, residential, and commercial sites in the tourism area, the sale of commercial and residential lots in the urban areas, and through charges for improvements made in the existing towns. FONATUR's operating policy calls for all developed land for sites of hotels and other superstructure to be sold, rather than leased, with the condition that no land may be acquired or held indefinitely for speculative purposes (Annex VI). The funds that will become available to FONATUR through the sale of land and various services are allocated by FONATUR's Technical and Resources Allocation Committee in accordance with the Government's priorities. This committee consists of representatives of various agencies including the Ministry of Finance, Presidencia and Patrimonio Nacional, and is chaired by the Minister of Tourism. For the project areas specifically, FONATUR will not later than June 30, 1978 prepare in consultation with the Bank, a statement of its financial policy, including methodology for calculating selling prices and rental charges, as well as procedures for their implementation. Average sale prices in Baja California are projected to range from US\$20 to US\$35 per m² for hotel, residential, and commercial sites, and from US\$10 to US\$12 per m² for land used for urban purposes. These prices are reasonable and compare favorably with the price of developed land elsewhere in Mexico and the United States.

4.16 Based on these estimates, the financial rate of return on investments in San Jose del Cabo in the fifth year of operation would be 24% (net cash flow on equity). The return would be of the same magnitude in the tourism zone in Loreto. However, when the financial projections for the tourism zone in Loreto and the town of Loreto are consolidated, the combined return is relatively low, 10% in the fifth year of operation. The lower consolidated returns in Loreto compared to San Jose del Cabo are largely due to the larger infrastructure investments needed in the town of Loreto.

4.17 Financial projections made separately for the water supply and sewerage components of the project are characterized by initial periods of losses and tight liquidity positions, followed by adequate profits and large cash surpluses (Annex IV). For Loreto, the annual financial rate of return on net fixed assets is 2.8% in the third full year of operations, increasing to 12.3% in the fifth year. For San Jose del Cabo, the annual financial rate of return is 8.3% in the fourth full year of operations, increasing to 14.6% in the fifth year. The losses in the initial years, followed by profits and cash surpluses in later years reflect the carrying costs of initial large investments required for a relatively complete system which operates for the first few years well below capacity. Assurances were obtained from the Government that all investment costs for water supply and sewerage systems in the project areas would be recovered through land sales and user charges, and that water and sewerage charges would be sufficient to cover: (a) the costs of operation and maintenance of such facilities, including depreciation based on a reasonable valuation of all headworks and equipment costs; (b) increases in working capital; and (c) the financing of minor expansion of the facilities.

4.18 No attempt has been made to evaluate separately the investments in electric power headworks and the telecommunications system, which form a minor portion of CFE's and TELMEX' national network. The charges levied by these agencies are standard tariffs for different classes of service applied throughout Mexico. The Bank has for many years lent to CFE for expansion of the electric power system in Mexico, and it has not been considered appropriate to carry out a detailed financial analysis of these general policies for the present project. With regard to telecommunications, which will not be financed by the proposed loan, consumers pay monthly tariffs and are obligated to pay for capital costs through purchase of company shares which can be traded in the stock market, ensuring that there is at least full cost recovery.

Pilot Hotels

4.19 The cost estimates for the pilot hotels to be built under the project are shown in Table 5 of Annex I. Capital costs per room average about US\$27,000 in 1976 prices, including interest during construction, working capital, the cost of land, and physical contingencies. Detailed financial projections for the pilot hotels are given in Annex VIII. Revenues from hotel operations are based on a projected occupancy rate of 50% in the first year of operation, increasing to 70% in the fifth year, a double occupancy factor of 1.8, and an average room rate of US\$25. Revenues from sale of food and beverages and other services are assumed to equal revenues

from room sales. Operating costs for the hotel operations have been estimated on the basis of current experience in existing facilities and standard ratios for comparable hotels in Mexico.

4.20 On these assumptions, the financial projections indicate that the hotels would be financially viable and have satisfactory rates of return. In the sixth year of operation the rate of return on equity would be 12%, rising to 14% in the tenth year of operation. The projected sources and application of funds show that the hotels would be able to generate sufficient income to meet their financial obligations, including debt service, management fees, and reserves for replacements. The projected balance sheet also indicates that the hotels' financial position would be sound and that dividends could be paid from the sixth year of operations onwards.

Airports

4.21 The revenues from the airports will be sufficient to pay for their operating expenses, but with little recovery of capital costs (Annex III), partly because departure taxes, a significant incremental revenue source of the airport, are traditionally not retained by the airport authorities. If departure taxes collected at the airports are included, the simple annual financial rate of return reaches 10.8% of average net fixed assets by 1986/87 in the case of Loreto and 17% in the case of San Jose del Cabo. Increased flights generated by the airport investments will significantly increase landings and, hence, landing fees at other Mexican airports, with little increase in operating costs or investments. The net return to the airport authority, therefore, is considerably higher.

Financial Covenants

4.22 FONATUR has agreed to develop and use not later than January 31, 1978, specific financial reporting formats acceptable to the Bank, which would include program budgets, progress reports, and project management accounting statements for each project area. These reports, which would be submitted to FONATUR's management and the Bank, would include comparisons of the actual operating results vs. budgeted financial and operating targets, with explanations for significant variations. FONATUR's financial records would be maintained according to generally accepted accounting principles and audited annually by independent auditors acceptable to the Bank. Audited financial statements would be submitted to the Bank within five months after the end of each fiscal year.

D. Economic Justification

4.23 For purposes of economic evaluation, the investment program has been defined more broadly than the project proper, and includes: (a) infrastructure for the tourism zones and the towns of Loreto and San Jose del Cabo, including the development of the airports and social infrastructure for the local population, such as health and civic centers, schools, and marketplaces; (b) superstructure facilities, including the first pilot hotels financed by the project, the commercial center, the golf club, and other common facilities; (c) community development expenditures, investment promotion, technical assistance, and studies; and (d) hotels, apartels,

condominia, villas, as well as restaurants and other tourism facilities not financed under the proposed project.

4.24 The basic assumption of the economic analysis is that the project would lead to the establishment of more tourism capacity in Mexico than if it were not undertaken. This incremental capacity will accommodate some tourists who would not otherwise come to the country. It will also divert some tourists, Mexicans as well as foreigners, from making expenditures elsewhere in Mexico. Deductions have therefore been made from the benefit and cost streams to reflect diversion of receipts (and variable operating costs) from other tourism facilities in Mexico.

4.25 The more rapid expansion of capacity due to the project would also have the effect of reducing, at least temporarily, the prices charged by other Mexican hotels, compared with the "without the project" case. These reductions have not been quantified, and are assumed to be compensated by similarly unquantified external benefits of the project. These consist of two main types. Firstly, some of the tourists who are induced to visit Mexico by the unique attractions of Baja California, will go on to visit other areas to the benefit of those areas and the Mexican domestic airlines. Secondly, the project will permit higher rates of utilization of existing tourism capacity in Baja California which has been insufficient to justify the minimum critical transport and marketing efforts necessary to launch a large tourism area.

4.26 The failure to quantify some of the above issues is not meant to deny their importance. But existing data are insufficient to give rise to reasonable expectations that even quite elaborate quantitative analyses of them would materially improve the design of the project. The project makes provision for studies designed to improve the collection of information, and to provide a careful analysis of some of the more important investment policy issues affecting the whole tourism sector, including sectoral growth targets, policies on taxation and pricing of tourism services, and sectoral investment criteria. The results of these studies and the appropriate actions to be taken would be reviewed with the Bank.

Gross Benefits

4.27 The gross benefits of the project would then be expenditures by visitors accommodated in Loreto and San Jose del Cabo (paras. 4.08 and 4.09), duly corrected for demand diversions, and the receipts from purchase of villas, condominium and apartel units by foreigners, plus the rental value to Mexican owners when they use these facilities. Demand diversion is estimated to be felt for only a two- to three-year period after accommodation capacity expands and to affect 40% of the revenues from foreign visitors to Loreto, 60% to San Jose del Cabo, and 75% of the revenues from Mexican visitors to both Loreto and San Jose del Cabo. In the urban areas, gross benefits generated by the project would consist of revenues from sale of urbanized lots plus the rental value of housing units built by the poorest sections of the population accommodated in the semi-urbanized lots. In both the urban and tourism areas, revenues from the electricity, telephone, and water and sewerage components of the project would come from tariffs charged to the incremental users of these facilities. Gross bene-

fits generated by the airports would consist of landing and parking fees, rent from commercial space leased, and the sale of other services.

4.28 Villas, condominia, and apartels in the project areas will typically be used by the owner for a few weeks each year, and rented the remaining part of the year. In addition to the gross benefits generated when rented to visitors, these units will generate gross benefits to the Mexican economy. The actual purchase price of these units by foreigners has been included as part of the gross benefits with the net financial returns to the owners treated as a cost. Selling prices are projected to range from US\$30,000 for a two-bedroom condominium to US\$45,000 for a three-bedroom villa, significantly lower than actual sale prices of such units in other parts of Mexico. The purchase of these units by Mexicans and the net financial returns they receive have been treated as transfers and are not incorporated in the economic analysis. However, the use of the facilities by the Mexican owners (about a month a year) is treated as a benefit at a price equal to the room tariff (or rental value). No rental values for foreigners are included.

4.29 All indirect taxes paid by Mexicans who would have traveled abroad without the project and those paid by foreign visitors to the project areas have been included in the gross benefits stream. No direct taxes, however, have been included.

Costs

4.30 Total capital costs associated with the project (excluding replacement costs) amount to US\$112.4 million in Loreto and US\$100.5 million in San Jose del Cabo. The cost of a few components such as the studies, health clinics and marketplaces, amounting to 2% of total project costs have been excluded from the analysis, on the assumption that their benefits equal their costs. The capital costs of constructing the airports and the telecommunications system are included as project costs, but the benefits directly generated by these investments have been excluded. With regard to the airports, revenues (excluding departure taxes) would cover operating costs with little surplus generated. The telecommunications components will be a small part of an integrated network; no information is available on marginal operating and investment costs, although as a whole the returns on the telephone company's investment have been traditionally high. The exclusion of net benefits on telecommunications, therefore, lends a conservative bias to the rate of return calculations.

4.31 In addition to the capital costs of the proposed project, the economic analysis includes the cost of hotels, apartels, villas, and other superstructure facilities. Average economic investment costs for hotels have been estimated at US\$24,000 per room, for apartels US\$18,000, and for villas and condominia at US\$11,000 per room, excluding the cost of land, and interest during construction. Additional investments that are likely to take place in local transportation, shops, and restaurants have also been taken into account. All relevant investment costs associated with the project are summarized separately for each area as follows:

Table 7: Investment Costs for Project Areas

Item	Loreto		S.J. del Cabo		Total	
	(US\$ M.)	(%)	(US\$ M.)	(%)	(US\$ M.)	(%)
Hotels, Apartels, Villas and Condominia	75.45	67.1	73.45	73.1	148.90	69.9
Shops, Restaurants, and other Facilities	8.45	7.5	11.30	11.2	19.75	9.3
Infrastructure Facilities	28.50	25.4	15.79	15.7	44.29	20.8
Total	112.40	100.0	100.54	100.0	212.94	100.0

4.32 Infrastructure represents about a fourth of the total project costs in Loreto and less than a fifth in San Jose del Cabo. This is a lower proportion than in similar projects elsewhere and reflects the fact that large investments in infrastructure have already been made in the area.

4.33 The projected operating costs for the facilities have been taken from financial statements drawn up for each component and deducted from gross benefits to arrive at net benefits. Given Mexico's unemployment of unskilled labor, wages for unskilled workers have been shadowpriced at 75% of their market wages.

Rates of Return

4.34 Separate rates of return are calculated for each project area. (Although it is arithmetically possible to calculate separate rates of return for the tourism and urban elements of the project, the necessarily arbitrary allocation of costs to each element would yield arbitrary results). On the basis of the above described assumptions and with an estimated economic life of 30 years, the internal economic rate of return on the investments in Loreto would be 19% and in San Jose del Cabo 21%. The discounted flow of costs and revenues (at a 10% discount rate) are US\$340 million and US\$420 million in Loreto, and US\$290 million and US\$370 million in San Jose del Cabo. The sensitivity rate of return to changes in key variables is shown in Table 8, on page 29. The rate of return would be particularly sensitive to changes in operating costs and prices. However, the risk of operating costs increasing more than 10%, with no parallel increases in revenues is considered small. Similarly, a fall in prices (revenues) over the life of the project is considered unlikely. Because of the infrastructure facilities already available, the project is feasible even if only 75% of the revenue-earning superstructure facilities are implemented. The "best estimate" rate of return does not include the proportion of the project revenues which are considered non-incremental, as explained in para. 4.25. Such revenues are generated by visitors who would come to Mexico even without the project and thus represent demand diverted from elsewhere in Mexico. The rate of return calculations are not too sensitive to changes in the proportion of non-incremental total revenues.

Table 8: Sensitivity Tests (in %)

		<u>Loreto</u>	<u>San Jose del Cabo</u>
<u>Best Estimate</u>		18.7	20.6
<u>Changes</u>			
Investment Costs	+10%	17.3	19.0
	+20%	15.9	17.6
Operating Costs	+20%	13.1	15.1
	+10%	16.1	17.9
	-10%	21.3	23.1
Prices (revenues)	+10%	21.9	25.1
	-10%	14.2	16.0
One Year's Delay in Project Implementation		16.1	17.0
Only 75% of Superstructure Constructed		16.2	17.8
No Shadow Pricing of Unskilled Labor		17.2	18.9

4.35 The proposed project and related investments are expected to increase Mexico's gross foreign exchange revenues from tourism by US\$34 million in 1982 and by US\$110 million a year from 1990 onwards. Because the projects are located near the US and in a duty free area, imports would be higher than in the rest of Mexico. Nevertheless, net foreign exchange earnings in the year 1990 would amount to about US\$84 million. This compares with the estimated foreign exchange component of the proposed project of US\$42 million, of the total program of US\$158 million and the gross foreign earnings of tourism as a whole in Mexico of US\$800 million in 1975.

4.36 The direct employment created by the proposed facilities is estimated to be around 12,000.^{1/} In addition, an estimated 13,000 jobs would be generated by the investments in sectors such as handicraft production, food processing and transportation. Unskilled labor would fill more than 60% of the jobs created. Some 40% of the jobs could be filled by women.

4.37 The Government would benefit both directly and indirectly from the investments in the project area. In addition to the revenues earned by government agencies involved in the project, such as FONATUR and the utility companies, the Government would capture revenues through an air-

^{1/} The project's investment cost per man-year of direct employment generated is US\$1,800, with both investments and employment streams being discounted at 10%. This figure compares favorably with the urban poverty lending "benchmark" for Mexico on employment generation grounds.

port tax and a 4% sales tax and direct taxes paid by commercial enterprises. The estimated incremental accumulated cash flow (excluding the Bank loan, which is considered untied to the project, and FONATUR's hotel lending operations) accruing to the Government is estimated to be US\$31 million in the tenth year of project operation and US\$124 million in the fifteenth. The internal rate of return on the Government's cash flow is over 20%.

4.38 Around 36% of the project's net financial benefits generated in the two areas would be captured by the Government and 27% by unskilled labor, with the remainder accruing to owners of hotels, shops, restaurants and other facilities.

E. Social Aspects

4.39 Mexico has welcomed foreign tourists for many decades. Because of its close ties with the US, whose influence has been strongly felt through mass media, education, consumer products, and large numbers of visitors, the project as such is not likely to affect the value systems of the local population in scope or direction other than those already occurring in the present day Mexican society. The influx of tourists who have come to enjoy Mexico's music, folkloric dances, handicrafts, archaeological sites, and remnants of a colonial past, have in fact brought about a stronger and deeper appreciation among Mexicans of their cultural heritage. However, to bypass the local population while developing facilities for foreign tourists could cause severe problems, as has been witnessed in both Mexico and the nearby Caribbean.

4.40 Drawing on FONATUR's experience in Cancun and Ixtapa-Zihuatanajo, the project in Baja California provides a major, rational means of integrating tourism and urban development. Socio-economic surveys of the existing towns (already complete as part of the project preparation exercise) and special provisions for the existing and new population in the project areas, have resulted in a plan which shows the Government's concern for the effects of tourism and rapid urban growth on the local population.

4.41 Implementation of the project would mean the creation of employment opportunities and a resulting increase in population in the project areas. The population in Loreto and San Jose del Cabo, which are basically rural communities, is expected to grow from about 3,000 to about 25,000 in each town in less than ten years. Although the planned rate of growth of tourism facilities is based on market projections and financial-economic criteria, and not on the social "carrying capacity" of the population, the project attempts to anticipate the stress resulting from the fast growth in population and makes provisions that would attempt to solve these problems. This is unusual for major investments in any sector and increases both the project preparation efforts and financial resources required. Aside from increased employment and income, the population in the towns under the project would benefit from improved and expanded infrastructure facilities as well as facilities such as parks, plazas, and marketplaces, all to be provided in the context of a well designed urban plan. Social services include day-care centers for working mothers, schools, and health clinics. Training centers to be provided would permit

local residents to learn a new trade or improve their present skill levels. The ejido members would benefit from monetary compensation for land expropriated, and from revenues and employment in tourism ventures owned and managed by them. Those with steady jobs and incomes would have the opportunity to purchase developed lots and qualify for assistance under current federal housing programs. For the newly arrived or the jobless, the project offers temporary accommodation as well as housing lots with some minimal infrastructure connections. For those who wish to build modest shelters, construction materials would be sold at cost, and technical assistance would be available.

4.42 In order to minimize any adverse impact, FONATUR, as part of project preparation, has assembled a community development team to handle day-to-day problems. This team will ease the transition from rural settlements to modern urbanized centers and will also provide avenues for local participation in the planning decisions. Assurances have been obtained that FONATUR will, through this team, assist migrant workers and the poorer sections of the population by, among other things, providing land, technical assistance, and construction materials at cost for building houses.

4.43 Loreto (a more cohesive, more rural community), is probably better equipped to adapt to the new environment and take advantage of its opportunities than San Jose del Cabo, because Loreto's stronger social structure will provide its inhabitants with support and will enable the community as such to cope with changes. At present, both communities favor tourism as a means for earning or increasing their incomes. It will be up to the community development team, however, to further this positive feeling and guide the population toward realistic expectations of, and pride in, being a host and support community for tourism.

V. AGREEMENTS REACHED AND RECOMMENDATIONS

5.01 During loan negotiations, agreement was reached and assurances were obtained on the following major points:

- (i) With the Government:
 - (a) that the project areas would receive adequate airline, water supply, power, telecommunications, education, training and health services (paras. 3.44, 3.46, 3.49, 4.07);
 - (b) that land use and zoning regulations would be adopted to control development on land immediately surrounding the project areas (para. 3.46);
 - (c) that all necessary action would be taken to ensure the construction and operation of 750 hotel rooms in each of the project areas in addition to the pilot hotels being financed under the project (para. 4.11); and

- (d) that investments in the water supply and sewerage systems would be fully recovered and that charges would be sufficient to cover operation and maintenance costs and the financing of minor expansion (para. (para. 4.17)).

(ii) With FONATUR:

- (a) that the Bank would be consulted on the results of the wildlife conservation, coastal zone water management, and market and economic studies and the appropriate actions to be taken (paras. 3.14, 4.26);
- (b) that final designs, plans, specifications and regulations for the project, including the pilot hotels, would be submitted to the Bank for approval (paras. 3.25, 3.34, 3.48, 3.50);
- (c) that improved financial reporting formats would be adopted and the relevant reports sent to the Bank (para. 4.22);
- (d) that the Bank would be consulted on the financial and operating policies for the proposed project (para. 4.15); and
- (e) that assistance would be given to migrant workers and the poorer sections of the population (para. 4.42).

5.02 The satisfactory establishment of the trust funds for the developments envisaged in Loreto and San Jose del Cabo (para. 3.43), will be a condition of loan effectiveness.

5.03 Subject to the condition of effectiveness described above, the proposed project would constitute a suitable basis for a Bank loan of US\$42 million equivalent to Nacional Financiera, S.A., acting for and with the guarantee of the Government, for a period of 17 years, including a grace period of 3-1/2 years.

ANNEX I

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

PROJECT COST ESTIMATES

The attached tables contain project estimates and schedules of expenditures and disbursements. These tables and schedules are listed below:

1. Breakdown of Total Project Cost by Major Project Items and Areas
2. Project Cost Estimates - Loreto Tourism Area
3. Project Cost Estimates - Town of Loreto
4. Project Cost Estimates - Town of San Jose del Cabo and Tourism Area
5. Project Cost Estimates - 250-Room Pilot Hotels (2)
6. Project Cost Estimates - Loreto and San Jose del Cabo Airports
7. Schedule of Expenditures by Year and Quarter
8. Estimated Schedule of Disbursements
9. Contingency Allowances

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Breakdown of Total Project Cost
(in US\$ 000)

	<u>Land Acquisition</u>	<u>Civil Works</u>	<u>Equip-ment</u>	<u>Consultant Services</u>	<u>Community Developm.</u>	<u>Pre-Opening Expenses</u>	<u>Promotion</u>	<u>Project Admin.</u>	<u>Total Cost</u>
1. Loreto Tourism Area	3,518	7,382	2,503	816		363	500	1,404	16,486
2. Town of Loreto	854	5,366	717	487	211	221		723	8,579
3. Loreto Pilot Hotel		3,423	1,239	373		241			5,276
4. Loreto Airport (Sub-Total)	100	4,636	1,116	460					6,312
	(4,472)	(20,807)	(5,575)	(2,136)	(211)	(825)	(500)	(2,127)	(36,653)
5. Town of San Jose del Cabo and Tourism Area	2,010	6,393	2,274	783	211	316	500	1,275	13,762
6. San Jose Pilot Hotel		3,423	1,239	373		241			5,276
7. San Jose Airport (Sub-Total)		1,962	1,116	246					3,324
8. Market and Economic Study				400					400
<u>Baseline Cost</u>	6,482	32,585	10,204	3,938	422	1,382	1,000	3,402	59,415
<u>Contingencies:</u>									
Physical Increase (10.7%)		4,138	1,529						5,667
Price Increase 1/ (35.6%)		12,625	2,718	1,231	124	641	402	1,123	18,864
(Total Contingencies)		(16,763)	(4,247)	(1,231)	(124)	(641)	(402)	(1,123)	(24,531)
<u>TOTAL COST</u>	6,482	49,348	14,451	5,169	546	2,023	1,402	4,525	83,946
<u>Foreign Exchange Component</u>									
Percentage		53.7	85.0						
Total		26,483	12,282	1,200	16.5		87.8	15.8	50.0
					90		1,231	714	42,000

<u>1/ Price Increase</u>	<u>Civil Works</u>	<u>Equipment</u>
1976	14%	10%
1977	12%	8%
1978	12%	8%
1979	12%	8%
1980	10%	7%

December 1976

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

LORETO TOURISM AREA
(in US\$ 000)

	Civil Works			Equipment			Total Cost			Expenditures				
	Local	Foreign	Total	Local	Foreign	Total	Local	Foreign	Total	Year-I	Year+I	Year+II	Year+III	Year+IV
<u>BID PACKAGES</u>														
1. Earthworks & storm drainage	340	590	930				340	590	930		262	329	245	94
2. Electricity (headworks)	429	1,179	1,608	103	584	687	532	1,763	2,295	608	855	631	201	
3. Electricity & street lighting (installation)	32	161	193	43	240	283	75	401	476	118	186	137	35	
4. Telecommunications 1/	214	820	1,034	102	578	680	316	1,398	1,714	446	649	478	141	
5. Water supply (head works)	171	93	264	6	35	41	177	128	305	84	111	82	28	
6. Other infrastructure	714	801	1,515	32	184	216	746	985	1,731	476	626	463	166	
7. Golf course	28	106	134	40	231	271	68	337	405	99	161	117	28	
8. Environmental sanitation	14	17	31	6	25	31	20	42	62	16	24	17	5	
9. Buildings	719	806	1,525	45	249	294	764	1,055	1,819	497	661	490	171	
10. Wildlife conservation (Sub-Total)	70	78	148				70	78	148	42	52	39	15	
	(2,731)	(4,651)	(7,382)	(377)	(2,126)	(2,503)	(3,108)	(6,777)	(9,885)	(2,648)	(3,654)	(2,699)	(884)	
<u>ACTIVITIES:</u>														
1. Promotion					61	439	500			200	200	100		
2. Pre-Opening activities					363	363				272	272	91		
3. Project administration					(1,182)	(222)	(1,404)	(140)	(282)	(421)	(421)	(421)	(140)	
(a) headquarters					591	222	813	90	155	244	244	80		
(b) field office					591		591	50	127	177	177	60		
4. Consulting Services:					(672)	(144)	(816)	(296)	(322)	(99)	(99)	(99)		
(a) final design					420	74	494	296	198					
(b) supervision					252	45	297		99	99	99			
(c) special studies						25	25		25					
(Sub-Total)					(2,278)	(805)	(3,083)	(436)	(604)	(720)	(992)	(331)		
<u>Baseline Cost</u>														
<u>Contingencies:</u>														
Physical increase	(1,355)	(2,355)	(3,710)	(147)	(832)	(979)	5,386	7,582	12,968	436	3,252	4,374	3,691	1,215
Price increase	365	657	1,022	56	319	375	(2,312)	(3,481)	(5,793)	(35)	(959)	(1,920)	(2,085)	(794)
	990	1,698	2,688	91	513	604	1,891	2,505	4,396	35	586	1,402	1,702	671
Land acquisition	(4,086)	(7,006)	(11,092)	(524)	(2,958)	(3,482)				3,518	3,518	1,267	1,145	1,106
										11,216	11,063	22,279	1,738	5,356
														7,400
														5,776
														2,009

1/ not to be financed by the Loan

December 1976

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

TOWN OF LORETO
(in US\$ 000)

	Civil Works			Equipment			Total Cost			Expenditures				
	Local	Foreign	Total	Local	Foreign	Total	Local	Foreign	Total	Year-1	Year+1	Year+II	Year+III	Year+IV
BID PACKAGES														
1. FONATUR's administration buildings & housing works	190	190	380	2	13	15	192	203	395		395			
2. Earthworks & infrastructure works	1,658	1,660	3,318	21	119	140	1,679	1,779	3,458	968	1,232	915	343	
3. Electricity (headworks)				35	198	233	35	198	233	53	97	71	12	
4. Electricity & street lighting (installations)	107	605	712				107	605	712	201	252	187	72	
5. Telecommunications 1/	49	148	197	27	151	178	76	299	375	96	144	106	29	
6. Environmental sanitation	16	15	31	4	27	31	20	42	62	16	24	17	5	
7. Buildings (Sub-Total)	364	364	728	19	101	120	383	465	848	232	308	227	81	
	(2,384)	(2,982)	(5,366)	(108)	(609)	(717)	(2,492)	(3,591)	(6,083)	(1,961)	(2,057)	(1,523)	(542)	
ACTIVITIES:														
1. Community development							176	35	211	18	53	64	76	
2. Pre-Opening activities							221		221			166	55	
3. Project administration:							(609)	(114)	(723)	(72)	(145)	(217)	(217)	(72)
(a) headquarters							217	114	331	43	67	99	99	23
(b) field office							392		392	29	78	118	118	49
4. Consulting services							(414)	(73)	(487)	(182)	(183)	(61)	(61)	
(a) final design							231	73	304	182	122			
(b) supervision							183		183		61	61	61	
(Sub-Total)							(1,420)	(222)	(1,642)	(272)	(381)	(342)	(520)	(127)
Baseline Cost														
Contingencies:	(1,154)	(1,457)	(2,611)	(43)	(244)	(287)	(1,679)	(1,770)	(3,449)	(71)	(676)	(1,059)	(1,193)	(450)
Physical increase	332	418	750	16	91	107	348	509	857	265	296	219	77	
Price increase	822	1,039	1,861	27	153	180	1,331	1,261	2,592	71	411	763	974	373
Land acquisition	(3,538)	(4,439)	(7,977)	(151)	(853)	(1,004)				854	854	308	278	268
TOTAL COST							6,445	5,583	12,028	651	3,296	3,726	3,236	1,119

1/ not to be financed by the Loan

December 1976

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

TOWN OF SAN JOSE DEL CABO AND TOURISM AREA
(in US\$ 000)

	Civil Works			Equipment			Total Cost			Expenditures				
	Local	Foreign	Total	Local	Foreign	Total	Local	Foreign	Total	Year-1	Year+1	Year+II	Year+III	Year+IV
BID PACKAGES:														
1. FONATUR's administration buildings & housing	119	118	237	4	24	28	123	142	265	265	218	162	62	
2. Earthworks & storm drainage	308	307	615				308	307	615	173				
3. Electricity (headworks)	14	41	55	75	422	497	89	463	552	128	226	165	33	
4. Electricity & street lighting (installations)	83	331	414	42	234	276	125	565	690	179	262	193	56	
5. Telecommunications 1/	94	285	379	116	657	773	210	942	1,152	282	456	334	80	
6. Water supply (headworks)	68	68	136				68	68	136	38	48	36	14	
7. Other infrastructure	1,638	1,148	2,786	72	410	482	1,710	1,558	3,268	895	1,187	879	307	
8. Environmental sanitation	34	34	68	10	58	68	44	92	136	34	52	39	11	
9. Buildings	778	875	1,653	22	128	150	800	1,003	1,803	500	647	480	176	
10. Wildlife conservation (Sub-Total)	25	25	50				25	25	50	14	18	13	5	
	(3,161)	(3,232)	(6,393)	(341)	(1,933)	(2,274)	(3,502)	(5,165)	(8,667)	(2,508)	(3,114)	(2,301)	(744)	
ACTIVITIES:														
1. Community development							176	35	211	18	53	64	76	
2. Promotion							61	439	500		200	200	100	
3. Pre-Opening activities							316	316				237	79	
4. Project administration:							(1,074)	(201)	(1,275)	(112)	(269)	(383)	(383)	(128)
(a) headquarters							538	201	739	74	147	222	222	74
(b) field office							536	536	38	122	161	161	54	
5. Consulting services:							(589)	(194)	(783)	(260)	(349)	(87)	(87)	
(a) final design							329	104	433	260	173			
(b) supervision							260	260		86	87	87		
(c) special studies							90	90		90				
(Sub-Total)							(2,216)	(869)	(3,085)	(390)	(671)	(734)	(983)	(307)
<u>Baseline Cost</u>							5,718	6,034	11,752	390	3,179	3,848	3,284	1,051
<u>Contingencies:</u>	(1,563)	(1,566)	(3,129)	(133)	(752)	(885)	(2,456)	(2,632)	(5,088)	(99)	(881)	(1,606)	(1,819)	(683)
Physical increase	442	425	867	52	289	341	494	714	1,208		321	449	331	107
Price increase	1,121	1,141	2,262	81	463	544	1,962	1,918	3,880	99	560	1,157	1,488	576
Land acquisition	(4,724)	(4,798)	(9,522)	(474)	(2,685)	(3,159)				2,010	2,010	718	646	646
TOTAL COST							10,184	8,666	18,850	1,207	4,706	6,100	5,103	1,734

1/ not to be financed by the Loan

December 1976

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

250-ROOM PILOT HOTELS (2)
(in US\$ 000)

	Civil Works			Equipment			Total Cost			Expenditures				
	Local	Foreign	Total	Local	Foreign	Total	Local	Foreign	Total	Year-1	Year+1	Year+II	Year+III	Year+IV
<u>BID PACKAGES:</u>														
1. Buildings & external works	3,365	3,054	6,419				3,365	3,054	6,419		2,696	2,978		745
2. Electrical, mechanical & hydraulic installations	144	118	262	157	891	1,048	301	1,009	1,310		189	1,091		30
3. Furniture, fixtures & special equipment (Sub-Total)	91	74	165	215	1,215	1,430	306	1,289	1,595		176	1,399		20
	(3,600)	(3,246)	(6,846)	(372)	(2,106)	(2,478)	(3,972)	(5,352)	(9,324)		(3,061)	(5,468)		(795)
<u>ACTIVITIES:</u>														
1. Pre-Opening activities							482		482					482
2. Consulting services: (a) design							(634)	(112)	(746)		(466)	(140)		(140)
(b) supervision							354	112	466					466
(Sub-Total)							280		280					140
							(1,116)	(112)	(1,228)		(466)	(140)		(140)
														(482)
<u>Baseline Cost Contingencies:</u>														
Physical increase	(1,918)	(1,728)	(3,646)	(176)	(998)	(1,174)	(2,568)	(2,772)	(5,340)		(190)	(1,345)	(3,269)	(536)
Price increase	360	324	684	56	316	372	416	640	1,056		315	661		80
	1,558	1,404	2,962	120	682	802	2,152	2,132	4,284		190	1,030	2,608	456
	(5,518)	(4,975)	(10,493)	(547)	(3,104)	(3,651)	—	—	—		—	—	—	—
<u>TOTAL COST</u>							<u>7,656</u>	<u>8,236</u>	<u>15,892</u>		656	4,546	8,877	1,813

December 1976

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

LORETO AND SAN JOSE DEL CABO AIRPORTS
(in US\$ 000)

	Civil Works			Equipment			Total Cost			Expenditures				
	Local	Foreign	Total	Local	Foreign	Total	Local	Foreign	Total	Year-1	Year+I	Year+II	Year+III	Year+IV
BID PACKAGES:														
	(a) <u>Loreto Airport</u>	(2,405)	(2,231)	(4,636)	(167)	(949)	(1,116)	(2,572)	(3,180)	(5,752)		(2,667)	(3,085)	
1.	Maneuvering areas	1,337	1,337	2,674				1,337	1,337	2,674		1,136	1,538	
2.	Terminal buildings	962	788	1,750	25	142	167	987	930	1,917		848	1,069	
3.	Fuel storage & supply	106	106	212	16	91	107	122	197	319		157	162	
4.	Visual aids and electrical supply				76	432	508	76	432	508		317	191	
5.	Navigational aids & communications				50	284	334	50	284	334		209	125	
	(b) <u>San Jose del Cabo Airport</u>	(806)	(1,156)	(1,962)	(167)	(949)	(1,116)	(973)	(2,105)	(3,078)		(1,531)	(1,547)	
6.	Terminal buildings	700	1,050	1,750	25	142	167	725	1,192	1,917		848	1,069	
7.	Fuel storage & supply	106	106	212	16	91	107	122	197	319		157	162	
8.	Visual aids & electrical supply				76	432	508	76	432	508		317	191	
9.	Navigational aids & communications				50	284	334	50	284	334		209	125	
	(Sub-Total)	(3,211)	(3,387)	(6,598)	(334)	(1,898)	(2,232)	(3,545)	(5,285)	(8,830)		(4,198)	(4,632)	
Consulting Services:														
	(a) final design						(706)		(706)		(441)	(132)	(133)	
	(b) supervision						441		441		441			
							265		265			132	133	
Baseline Cost														
Contingencies:														
	Physical increase	(1,788)	(1,879)	(3,667)	(138)	(784)	(922)	(2,094)	(2,663)	(4,757)	(69)	(1,833)	(2,855)	
	Price increase	399	416	815	50	284	334	449	700	1,149		554	595	
		1,389	1,463	2,852	88	500	588	1,645	1,963	3,608		69	1,279	2,260
	Land acquisition (at Loreto)	(4,999)	(5,266)	(10,265)	(472)	(2,682)	(3,154)	100		100	40	30	30	
	TOTAL COST							6,445	7,948	14,393	40	540	6,193	7,620

December 1976

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Schedule of Expenditures by Year and Quarter
(in US\$ 000)

	Year - I		Year + I				Year + II				Year + III				Year + IV		Total
	Q. - 2	Q. - 1	Q. 1	Q. 2	Q. 3	Q. 4	Q. 5	Q. 6	Q. 7	Q. 8	Q. 9	Q. 10	Q. 11	Q. 12	Q. 13	Q. 14	
LORETO COMPLEX																	
Land Acquisition	808	807	364	363	363	363	351	351	351	351	3,072	3,073	3,072	3,072	1,559	1,275	4,472
Civil Works			1,263	1,264	1,264	1,264	2,849	2,850	2,850	2,850	939	939	939	939	151	122	31,577
Equipment			473	474			728	728	728	729	27	28	27	27			7,889
Consulting Services	274	275	324	325	325	324	112	112	112	112	124	125	125	125			2,794
Community Development	5	14	15	15	15	16	21	21	21	21	27	28	27	27			273
Promotion							64	65	65	65	72	73	73	72	84	68	701
Pre-Opening Activities											246	247	247	246	123	100	1,209
Project Administration	142	142	130	130	130	130	207	207	207	207	232	232	233	232	157	128	2,846
(Sub-Total)	(1,229)	(1,238)	(2,569)	(2,571)	(2,097)	(2,097)	(4,332)	(4,334)	(4,334)	(4,335)	(4,712)	(4,717)	(4,716)	(4,713)	(2,074)	(1,693)	(51,761)
SAN JOSE DEL CABO COMPLEX																	
Land Acquisition	359	359	161	161	162	162	162	162	161	161	1,752	1,753	1,753	1,752	956	783	2,010
Civil Works			644	644	644	645	1,611	1,611	1,611	1,612	831	832	832	832	104	86	17,771
Equipment			339	340			591	591	592	592	70	71	71	71			6,562
Consulting Services	173	173	242	243	243	242	68	68	68	68	27	28	27	27			1,871
Community Development	5	14	15	15	15	16	21	21	21	21	72	73	73	72			273
Promotion							64	65	65	65	173	174	174	173	84	68	701
Pre-Opening Activities											138	139	139	139	66	54	814
Project Administration	69	70	74	74	74	75	123	124	124	124	(3,063)	(3,070)	(3,069)	(3,066)	106	87	1,679
(Sub-Total)	(606)	(616)	(1,475)	(1,477)	(1,138)	(1,140)	(2,640)	(2,642)	(2,642)	(2,643)					(1,316)	(1,078)	(31,681)
TOURISM MARKET STUDY																	
Total Expenditures p.Q.	1,835	1,854	4,044	4,048	3,293	3,295	7,069	7,073	7,073	7,075	7,775	7,787	7,785	7,779	3,390	2,771	83,946
Total Expenditures p.Y.							14,680				28,290				31,126	6,161	
Cumulative p.Y.							18,369				46,659				77,785	83,946	

December 1976

ANNEX I
Table 8

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Forecast of Disbursements
(in US\$ 000)

Implementation Quarter	Disbursements				Undisbursed Balances	
	Quarterly	Percent	Cumulative	Percent	Quarterly	Percent
<u>First Year:</u> Q. 1					42,000	100.0
Q. 2	1,266	3.0	1,266	3.0	40,734	97.0
Q. 3	1,905	4.5	3,171	7.5	38,829	92.5
Q. 4	1,937	4.6	5,108	12.1	36,892	87.9
<u>Second Year:</u> Q. 5	1,660	4.0	6,768	16.1	35,232	83.9
Q. 6	3,707	8.8	10,475	24.9	31,525	75.1
Q. 7	3,710	8.8	14,185	33.7	27,815	66.3
Q. 8	3,849	9.2	18,034	42.9	23,966	57.1
<u>Third Year:</u> Q. 9	3,912	9.3	21,946	52.2	20,054	47.8
Q. 10	4,105	9.8	26,051	62.0	15,949	38.0
Q. 11	4,373	10.4	30,424	72.4	11,576	27.6
Q. 12	4,339	10.3	34,763	82.7	7,237	17.3
<u>Fourth Year:</u> Q. 13	4,108	9.8	38,871	92.5	3,129	7.5
Q. 14	3,129	7.5	42,000	100.0	0	0.0
TOTAL	42,000	100.0				

February 1977

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Contingency Allowances
(in US\$ 000)

	Land Acquisition	Civil Works			Equipment			Consulting Services			Community Development			Pre-Opening Expenses		Promotion			Project Administration		Total Contingencies				
		Local	Foreign	Total	Local	Foreign	Total	Local	Foreign	Total	Local	Foreign	Total		Local	Foreign	Total	Local	Foreign	Total	Local	Foreign	Total		
<u>TOTAL PROJECT COST EXCLUDING CONTINGENCIES</u>	6,482	15,087	17,498	32,585	1,532	8,672	10,204	3,015	923	3,938	352	70	422	1,382	122	878	1,000	2,865	537	3,402	30,837	28,578	59,415		
Percentage of Total	100.0	46.3	53.7	100.0	15.0	85.0	100.0	76.6	23.4	100.0	83.4	16.6	100.0	100.0	12.2	87.8	100.0	84.2	15.8	100.0	51.9	48.1	100.0		
CONTINGENCIES																									
(a) Allowance for Probable Price Increases:																									
(i) Percentage	39.0	38.5	38.7	26.6	26.6	26.6	31.6	30.0	31.3	29.5	28.6	29.4	46.4	40.2	40.2	33.0	33.0	29.1	34.6	31.8					
(ii) Amount	5,880	6,745	12,625	407	2,311	2,718	954	277	1,231	104	20	124	641	49	353	402	946	177	1,123	8,981	9,883	18,864			
(b) Allowances for Unforeseen Factors:																									
(i) Percentage	12.6	12.8	12.7	15.0	15.0	15.0															6.9	12.4	9.5		
(ii) Amount	1,898	2,240	4,138	230	1,299	1,529															2,128	3,539	5,667		
(c) Total Contingency Allowances:																									
(i) Percentage	51.6	51.3	51.4	41.6	41.6	41.6	31.6	30.0	31.3	29.5	28.6	29.4	46.4	40.2	40.2	33.0	33.0	33.0	36.0	47.0	41.3				
(ii) Amount	7,778	8,985	16,763	637	3,610	4,247	954	277	1,231	104	20	124	641	49	353	402	946	177	1,123	11,109	13,422	24,531			
(iii) Percentage of Total	46.3	53.7	100.0	15.0	85.0	100.0	77.5	22.5	100.0	83.9	16.1	100.0	100.0	12.2	87.8	100.0	84.2	15.8	100.0	45.3	54.7	100.0			
<u>TOTAL PROJECT COST INCLUDING CONTINGENCIES</u>	6,482	22,865	26,483	49,348	2,169	12,282	14,451	3,969	1,200	5,169	456	90	546	2,023	171	1,231	1,402	3,811	714	4,525	41,946	42,000	83,946		
Percentage of Total	100.0	46.3	53.7	100.0	15.0	85.0	100.0	76.8	23.2	100.0	83.5	16.5	100.0	100.0	12.2	87.8	100.0	84.2	15.8	100.0	50.0	50.0	100.0		

December 1976

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

PROJECT DESCRIPTION

A. General

1. The project would consist of the following main elements:

For Loreto:

- (a) infrastructure and other facilities for the tourist zone at Nopolو, located 7.5 kms south of Loreto and some minimal trailer park and other facilities at nearby Puerto Escondido;
- (b) a medium category 250-room hotel to be located at Nopolо;
- (c) infrastructure and other facilities for the existing town itself; and
- (d) airport facilities.

For San Jose:

- (a) infrastructure and other facilities for the town as well as the adjacent tourism zone;
- (b) a medium category 250-room hotel; and
- (c) airport facilities.

2. The project also makes provision for promotion, community development activities and conservation programs for both areas. In addition, a tourism market and economic study is included that would provide Mexico with needed information on the sector as a whole. These components are discussed in greater detail below, except the water supply, sewerage and drainage systems, the airport facilities and the studies which are discussed more fully in Annexes III, IV and X.

B. Loreto Tourism Zone and Puerto Escondido

3. In the tourism zone (Nopol), infrastructure in the first stage will serve an accommodation program of 3,000 hotel and apartel rooms plus 655 condominium-type apartments and villas, along with recreation, community and cultural facilities. The hotel and apartel accommodations have been planned around a community and cultural "animation" center within the primary hotel zone that would provide day and night activities for the resort. Included in the project is the construction of a first 250-room medium category hotel.

4. A central pedestrian spine would run parallel to the beach giving easy access to all the community facilities from the hotels. A series of squares and plazas along the pedestrian way would form the entrances to the hotel clusters. Thus a pedestrian town would be created along the beach front in contrast to the traditional separate and individual lots with no visual linkage except the road. The pedestrian spine would serve as a visual link in which the tourist can move under cover of vegetation and arcades.

5. On the west side of the main boulevard, clusters of condominium apartments and villas have been planned along with three apartel sites. While there is flexibility in the plan in terms of size and shape of the lots, the type of accommodation designated for each site has been selected to permit optimum development of the land.

6. Roads. The hotel zone would be served by a main boulevard (2 km long, 30 m wide, 4-lane) parallel to the beach, but set back 200 to 350 meters. The main entrance to the zone is located at the north end of the site--nearest the airport--and provides direct access to the beach boulevard. The boulevard ends in a cul-de-sac to the north and continues as a two-lane road serving the southern end of the development. It connects to the main highway to provide a secondary entrance.

7. As part of the road infrastructure, an internal 2 km long, 18 m wide, 2-lane loop road provides access to single family cluster housing, condominium apartments and villas at the back of the site as well as a tennis center and other recreational facilities. The system has been so designed that the sites can be developed without tearing up the curbs and gutters of the main road system. Landscaping and street lighting have been included for the entire road network. The storm water drainage network would be open channels, except for discharge structures.

8. Power Supply and Distribution. The Federal Electricity Commission (CFE) builds and operates all the power supply and distribution for the country. The project would require a new overhead transmission line to be constructed from Villa Constitucion to service the projected demand of 12,000 kv. From the substation in Villa Constitucion, 150 km away, a 115 kv transmission line with controls and

protection circuit breakers would be constructed under the project, with conductors supported on concrete posts. A new substation would be constructed at the town of Loreto, and electricity delivered to the tourism zone via a 34.5 kv overhead transmission line. These headworks and transmission lines from Villa Constitucion would take about 36 months to construct. Work would be initiated in the first year and completed early in the third year to serve the complex by early 1980.

9. The local distribution for both Nopolo and Loreto would consist of 34.5 kv overhead lines reduced to 220/127 volts by transformers to service each lot. A total of 66 transformers would be provided along the major boulevard from which underground service to individual sites would be provided.

10. Telecommunications. Telecommunications in Mexico are built and operated by TELMEX, a government owned agency. In Loreto, an integrated system would be installed that would serve both the town and the tourism zone until 1988. Under the project, a new exchange building will be built and located in the town. The local exchange equipment would consist of AFRm/6B multiplex equipment. One thousand lines on 60 circuits would be provided to meet projected demand.

11. The long distance circuits will be tied into the regional microwave with 120 channels initially, 8 repeaters and 2 terminals. A booster station to be constructed would include rectifiers, amplifiers, battery cells and emergency equipment.

12. The local distribution lines would be placed in underground conduits. Initially 1,550 lines would be placed in service. In addition, each hotel will be required to purchase their own PABX private exchange which they will operate. The system will take about three years to install. It is programmed for completion by early 1980.

13. The entire system will be installed by one of the sister companies of TELMEX: Teleconstrucciones, Contelmx or Cycxsa. TELMEX, the operating agency will be charged for the costs of the installation and connection, and TELMEX in turn will charge FONATUR.

14. Recreational Facilities. A community and cultural center would be built under the project and would consist of an auditorium with a capacity of 500 seats and a central plaza with space for shops, offices, cafes, travel agencies, restaurants, banks, pharmacies, a post office and an emergency health clinic. Adjacent to the center, a boat house and pier would be constructed for safe and easy boarding of boats (motor and sail), for all forms of aquatic sports as well as excursions. The pier would be constructed of precast, reinforced concrete piling and cross ties with a treated wooden deck, handrails and bumpers. Water and fuel service would be available at the end of the pier from underground tanks. A concessionaire would manage the rental of all boats.

15. Based on the oceanographic data and bathymetric surveys along with configuration and orientation of the beach, a site has been earmarked to provide year-round anchorage and protection for boats. Located at the southern end of the complex the protection would come from a 60 m rocky promontory. Anchorage would be provided for 25 boats attached to mooring buoys (fore and aft) and secured to a system of anchors below. A small recreation center will be constructed for the beach area and would include a restaurant, restrooms, changing rooms and parking facilities.

16. A main recreation and landscape feature of the project is an 18-hole golf course, of which the first nine holes and clubhouse would be constructed under the project. The clubhouse (with pro-shop, snack bar, changing rooms and office) is a single structure and has been located at the junction of the beach and main entrance boulevard. Equipment such as golf carts and an irrigation system have also been included in this component. The fairways have been designed to open up residential properties for condominium and villa development on both sides for maximum exposure. The alignments of the fairways take advantage of the natural vegetation and would need minimum grading. The course would be irrigated by the treated effluent of the sewage lagoons located 2.5 km west from the site. In this manner, the hydrological cycle would be complete. Only natural storm drainage run-off would enter the sea. An ample site at the southern end of the inner loop has been provided so that private interests could develop a 16-lawn tennis club in a "park-like" setting along one of the golf course fairways. On the other side of the transpeninsular highway, land has been reserved for riding stables and a practice ring. Visitors would be able to ride up into the spectacular gorges and escarpments of the Sierra Range to enjoy the panoramic views of the surrounding region.

17. Buildings. A service building for fire and police would be built under the project with adequate space for parking, storage, and maintenance of equipment. This component also includes fire fighting and police vehicles and equipment.

18. Environmental Sanitation. For the first three years of project implementation, an environmental sanitation program would be undertaken consisting largely of pest control. Areas infested with flies and mosquitoes would be treated and measures will be taken to eliminate any source of contamination. In a nearby small lagoon, top feeding minnows will be introduced to control larvae population. Special controls will be maintained around the area of the oxidation ponds and the sanitary landfill.

19. Flood Protection. Along the Primer Agua Creek, a protection wall would be built under the project to avoid any flooding of the tourism zone.

C. The Town of Loreto

20. Infrastructure and other facilities for the town of Loreto are aimed at upgrading present living conditions of inhabitants and providing for the expansion in population, which is projected to grow from 3,000 to 25,000 in about 10 years. For this purpose, 736 ha of land were expropriated, and an urban plan prepared.

21. The urban plan calls for the redensification of the old town to accommodate some of the increase in population. A large proportion of the expanded population, however, would be accommodated in a new residential area. Because of aircraft flight lines and aircraft noise the new district will be built 600 m west of the old town, with green areas and parks separating the two. Under the project, parks, playgrounds, health clinics, schools and shops would be built so as to ensure that newcomers do not overload the present facilities. Offices for FONATUR personnel and some staff housing will be built in the new residential area. FONATUR's offices include offices for accounting, engineering, community development and promotion activities. The offices will be furnished and personnel provided with vehicles. Single family or cluster housing and apartments in the new residential area would be financed through existing federal housing programs.

22. Roads. A new 4-lane (1 km long and 28 m wide) entrance road, adequately lit and landscaped, would connect the transpeninsular highway with the center of the town. Roadworks will also include construction of a 16 km long street network to serve the new district and the upgrading of existing streets in the old town.

23. Electric Power. The transmission line from Villa Constitucion will also deliver electric power to the town of Loreto. The existing distribution system will be expanded with 34.5 kv overhead lines and will include transformers and street lighting.

24. Solid Waste Disposal. A large solid waste disposal site has been selected 5 km from town and would serve the needs of both the town and the tourism zone. Equipment would include three covered garbage trucks and one tractor to help the sanitary landfill process.

25. Urban Renewal. The central plaza in the old town would be improved, paved and landscaped. A recreation beach facility would be provided with snack bar and changing rooms to serve the town. Portions of the old buildings around the plaza would be renovated.

26. Other Facilities. The area of the aircraft flight cone between the old town and the new residential area has been reserved for recreation facilities, cemeteries and other non-residential uses. Rigid height and use restrictions would be applied to ensure the safety and welfare of

existing and future residents. A new wholesale market will be built mid-point between the new residential area and the existing town. A nursery-kindergarten for about 100 children would be built in the new district for infants as well as pre-school children of working mothers. A new health center would be built for the new residential area. Vocational training in basic skills such as carpentry, electricity, plumbing, and masonry, would be provided in a building located in the industrial zone. The Mexican Institute for Social Security (IMSS) would equip and operate the facility. At the far end of the industrial area, a slaughter house would be built and equipped under the project. All the above facilities would be provided in the first year and a half of the development program. A boat ramp will be built at the edge of the "ejido" settlement on the outskirts of the town of Loreto where boat repairs and maintenance would be undertaken. Adequate space has been provided for the storage and repairs of 25 boats. This activity if properly managed has the potential of evolving into an important industry in the future.

27. Sites and Services. To accommodate the poorer sections of the population and the migrant worker seeking employment, 500 lots in three to four locations distributed throughout the new residential area have been planned. A road would be constructed for access to each cluster of 150 m^2 lots. Common water taps would be available along the road for every 15 to 20 houses. Each lot would be provided with a graded site, and a simple toilet in a utility structure. The houses would be built on a do-it-yourself basis and in the future could be integrated into the town. Power would be available along the streets, along with street lighting. To facilitate the construction of houses, the building materials for a two-room structure would be provided by FONATUR at cost along with technical assistance and supervision.

28. Facilities for Puerto Escondido. Puerto Escondido is a natural sheltered harbor with a small hidden entrance. It is already popular with tourists who come here with their boats and trailers. However, pollution is increasing and threatens the beauty of the area. The water quality is excellent, but the beach quality is inferior to Nopolo, although acceptable for limited tourism activities. Most of the land is steep rocky slopes and undevelopable in any major way. The harbor today serves as a yacht anchorage and can accommodate over 200 boats. At the entrance, a ferry boat terminal was recently constructed. Ferry service to Guaymas on the mainland will begin in the near future. The project provides for minor improvements to a general commercial pier adjacent to the terminal to serve small cargo vessels. A modest administrative building would be provided to control the area. Along the inner harbor, a trailer park for 50 trailers and campers would serve tourists coming by road. Minimum site work is required to develop clustered campsites. Office, restaurant, shops, changing rooms and bathing facilities have been included in the project. Water supply would be provided from a nearby existing well. Sewage from the area would be processed in a package treatment plant. It would be located inland from

the harbor and disposal of the effluent would be through leaching drain fields. Power supply would come from a small diesel plant located at the entrance to the area.

D. San Jose del Cabo

29. The San Jose master plan calls for the integrated development of the town and the tourism zone. Presently two kilometers apart, they will be merged, with only a large hill that will visually separate the two. Tourist facilities would be located at the west of a long beach that extends for 10 kilometers. About 1,800 hectares have been expropriated for the purpose.

30. Infrastructure facilities will serve 3,150 hotel and apartel rooms and 305 condominium-type apartments and villas along with community, cultural and recreation facilities. Like Loreto, the hotels and apartels have been planned around a community and cultural center. The center is linked to the beach by several plazas to facilitate pedestrian circulation. In back of the primary hotel zone, apartments and villas are clustered around common courts which form part of the pedestrian network. While there is flexibility in the plan in terms of size and shape of the lots, the type of accommodation designated for each lot has been selected to permit optimum development of the land. Included in the project is the construction of a first 250-room medium category hotel.

31. Power Supply and Distribution. At present, the area, including the town of San Jose del Cabo, is served by a small diesel generating plant located at Cabo San Lucas. To meet the increased demand for power, a 115 kv transmission line is under construction that would bring electric power from large generating plants in La Paz. These works were scheduled to be finished by March 1977. Under the project, the present substation at San Jose will be expanded to meet projected urban and tourism needs. Local distribution would be by 13.3 kv overhead lines. From the main streets, service would be underground to each individual lot.

32. Road Network. The road network includes a main entrance boulevard (4-lane, 1.6 km, 30 m wide) from the transpeninsular highway which borders the western edge of the tourism area. This main boulevard is curvilinear and forms a circuit around the "cultural center. A two-lane road extends to the east to connect with the town's main street, along which the main utility lines would run. The secondary roads would have cul-de-sacs that could be extended in the future to connect with the town's street system. Turnoffs and junctions have been provided for the residential clusters and recreation facilities so that the sites can be developed without tearing up the curbs and gutters of the main road system. Landscaping and street lighting have been included for the entire network.

33. Telecommunications. The telephone system in San Jose del Cabo has 125 lines which will be expanded under the project to 1,260. A new exchange building would be built in the town. Local exchange equipment would be installed in stages and consist of AFRm/6B type multiplex equipment.

34. The long distance circuits will be tied into the regional microwave system and would have 120 channels with 6 repeaters. The booster station facilities include rectifiers, amplifier battery cells, emergency equipment of 50 kw and 15 tons of refrigeration. To meet projected demands, 1,040 local distribution lines would be constructed in underground conduits. Each hotel would be required to purchase PABX exchange equipment. It would take about two years to construct and install these facilities. As in the case of Loreto, the system will be installed by one of TELMEX's sister companies: Teleconstrucciones, Contelmx or Cycxsa. TELMEX, the operating agency, will be charged for the costs of installation connection, and in turn will charge FONATUR.

35. Recreational and Other Facilities. A community and cultural center would be constructed in the first stage and would consist of an auditorium (capacity 500) and a central plaza with space for shops, cafes, bars, restaurants, banks, pharmacies, and a post office to provide the tourist with essential as well as recreational services .

36. Two small recreation centers have been planned for the beach area and would contain a swimming pool, snack bar, a restaurant, toilets, changing rooms and parking. One located on the east side would serve primarily the town population, while the second--in front of the cultural center--would serve visitors to the tourism zone. Although not financed under the project, space has been reserved for sport activities such as tennis and handball, which will be developed by the private sector. Land has been reserved at the base of the mountains for riding stables and a practice ring. Visitors would be able to ride into the foothills for panoramic views of San Jose del Cabo and the sea beyond. South of the site, at Punta Palmilla, a fishing pier and boat dock would be provided for deep-sea sports fishing. Water and fuel service would be available and a small boat house for storage of equipment. Adjacent to the pier a marine structure would be provided to create a safe bathing area for visitors because during certain periods the beach in front of the resort is unsafe.

37. On the south side of the town between the fishing pier and the tourism area a trailer park has been constructed, owned and operated by "ejidatarios." Under the project, the park will be improved and FONATUR plans to assist the "ejidatarios" to run the park.

38. Urban Facilities. The town of San Jose del Cabo is projected to grow from about 4,000 to 25,000 by 1988. A new residential area will be constructed near the existing town on the west side of the transpeninsular

highway. This area would accommodate 200 "ejidatario" families whose land was expropriated and population of the lowest income category, including migrant workers (500 lots). The level of urbanization would be minimal with stabilized roads serving each lot of 150 m². A common water tap, located in the center of the block, would serve 10 houses. Each lot would be graded and provided with a simple toilet. Power would be available along the streets. To implement the aided self-help housing program, building materials would be provided for each eligible person along with technical assistance and supervision. In both neighborhoods, space has been provided for community facilities, including schools, parks and playgrounds.

39. A kindergarten for about 100 children would be provided to serve both infants as well as pre-school children while mothers work. It would be located midway between the tourism zone and the old town. Also located midway would be a health center. Vocational training in basic skills (carpentry, electricity, plumbing and masonry) would be provided at a building north of the town. It would be equipped and operated by the IMSS who are presently operating similar facilities in Zihuatanejo and the town of Cancun. Small scale industries will be promoted adjacent to the training school to increase the town's economic base.

40. While the character of the "colonial" town with the extended pedestrian plaza is attractive, many of the old buildings and facades are in need of extensive repairs. Six important buildings of fine colonial style in the town would be repaired under the project, and 25 blocks of building facades would be given a "face-lift." Parks and plazas will be built along the main pedestrian way connecting the center of the old town with the tourism zone. Adjacent to the existing slaughter house 2 km north of the town in the industrial service area, land has been reserved for a wholesale market. A solid waste disposal site has been selected in the flight line of the new airport. Covered garbage trucks and a tractor would be provided for the sanitary landfill process.

41. Environmental Sanitation. For the first three years of project implementation, sanitation programs consisting mainly of pest control would be undertaken. Areas such as the lagoon would be studied for mosquito control. Areas infested with flies would be treated and measures taken to eliminate the source of contamination. Special controls will be maintained around oxidation ponds, the sanitary landfill area and the stables.

42. Buildings. A fire station would be provided with space for dormitories, administration offices, storage and garaging of fire trucks. It will be located between the town and the tourism zone. FONATUR's field offices and some staff housing would be located in the tourism zone. Furniture, office equipment and vehicles would be provided under the project.

E. Conservation Programs and Studies for Both Project Areas

43. In Loreto along the coastline there are a number of areas that would be protected under the project by means of planting new material and limited reforestation. In Puerto Escondido, which is barren, a variety of palms and plant material would be developed along the beach of the inner harbor. Dune grass along the outer edge of the beach would protect it. Cactus and ground cover planted in clusters would stabilize the soil and give cover for wildlife. In addition, the north and south end of Nopolo Beach would be planted with palms and ground cover. There are also a few lagoons that are potential bird sanctuaries where wild rice and other natural foods would be planted to support a sizeable bird population. Tree planting would also be extended along the coastline north to the airport.

44. Outside the immediate project area in Loreto a wide conservation zone has been planned that extends up into the foothills to the top of the watershed. Behind the tourism zone, a natural spring feeds an oasis of lush tropical vegetation and desert palms which have been cultivated for the last century. It is surrounded by barren high rocky crags and cliffs, providing a dramatic contrast. Under the project this "oasis" will be used as a plant nursery, and serve as a center of tourist attraction.

45. Out in the sea itself, is an extraordinary treasure of natural life. Sea lions and seals inhabit the eastern tip of an island called Isla Coronados. Birds have nests on the rocks on top of the island while a complete rookery of bird life exists at the western end. In order to preserve the natural life on this island, studies are required. It is estimated that four man-months of naturalists will suffice to analyze the present conditions and develop a program of conservation and wildlife management. The potential for a "marine" park, that would include creating under-water trails on the reefs at the western end of the island, would also be studied.

46. A second study to be undertaken would evaluate the vegetation and wildlife surrounding Puerto Escondido and determine what portion of the bay should be a wildlife sanctuary. The study would also include a general reconnaissance of the large Isla del Carmen, 5 km east of Puerto Escondido, which is presently used for salt extraction. These studies would provide the necessary inputs for a conservation program and a coastal land management plan for the entire area.

47. In San Jose del Cabo the main conservation objectives are to protect an attractive sweet-water lagoon adjacent to the town and tourism zone, to develop a water management plan to conserve precious water in the area, and to maximize the lagoon's long-term beneficial contribution to the local population and the visiting tourists.

48. Under the project, the lagoon will be dredged to provide for sufficient depth so that plant and fish population could increase. Access to the lagoon will be controlled and new plant material introduced around the edge and on the island in the lagoon. Palm varieties will be added to the existing royal palm clusters on the south side of the lagoon. The lagoon contains a substantial quantity of fresh water, and a significant feeding station would be established for the migratory bird population. Wild rice would be planted for this purpose. Dune grass and ground cover will be planted on the fragile primary beach to protect the land bridge in front of the lagoon. In addition, similar planting would be extended along the 2.5 kilometers in front of the resort for greater soil stability. Wooden catwalks would be constructed across the primary and secondary dunes at 4 or 5 locations, and regulations prohibiting the crossing of the dune anywhere else would conserve the dune from the erosion of daily use.

49. Under the project, SARH would undertake a study of the watershed for San Jose del Cabo to prepare a water management plan that would assure the area of permanent and safe groundwater supply. The study would include the identification of strategic points for the construction of velocity check dams. A limited program of reforestation would be implemented to control erosion. These dams and programs will help recharge the aquifer. It would also preserve the lagoon as a natural attraction for visitors.

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

AERONAUTICAL ASPECTS

1. Direct air access to the two tourism sites is critical to the success of the project. San Jose del Cabo at present has a recently completed 2,200 x 45 m runway of suitable strength, but there are no buildings, visual, navigational, or communication aids. At Loreto there is a small general aviation airport that can handle only light aircraft. Expanding and improving these airports and providing the necessary facilities is estimated to cost US\$14.4 million, which is expected to be disbursed over the first three years of project implementation. The airport facilities are discussed below, separately for each area.

A. San Jose del Cabo

2. The terminal building at San Jose del Cabo will have about 2,500 m² of operational space on the ground floor with a modest restaurant, kitchen and offices on an upper level. Since Baja California is a free zone, there will be no incoming customs clearance but there will be an outgoing customs clearance for flights proceeding to domestic points within Mexico. Health, emigration and immigration check points will be required for all international flights. The processing areas have been designed for about 200 peak-hour passengers in each direction.

3. A standard control tower, with adjacent technical block, will be constructed to one side of the terminal building. The tower cab floor will be about 25 meters above the ground. The technical block will contain offices, equipment rooms, generator and pumping equipment.

4. A three-bay crash, fire and rescue (CFR) building will be constructed on the other side of the terminal. The ground floor will contain offices, a dining room, kitchen and a training room as well as the CFR vehicles. The upper level will house the dormitories and baths.

5. A fuel farm will be constructed to one side and at the rear of the terminal area. Turbine fuel will be supplied from there to the apron by an underground hydrant system, while gasoline will be dispensed by fuel tank trucks.

6. An automobile parking area will be constructed in the forecourt of the terminal building and internal access roads will be constructed as necessary.

7. A VOR/DME and NDB (radio navigational equipment) will be installed on airport property. Each will be provided with standby electrical power. The VOR will be located in such a position that the southern approach radial will pass over agricultural land between the tourism facilities to be provided under the project and the development planned for a second stage (see Map).

8. Both VHF and HF radio equipment will be provided for air/ground and point-to-point communications by the tower (air traffic control).

9. Visual aids in the form of VASIS (visual landing aid) runway and taxiway edge lights, apron lights and runway marking will be provided. Perimeter fencing will also be installed.

B. Loreto

10. At Loreto, buildings and equipment identical to those described above for San Jose del Cabo would be provided except that there is no need for a special location for the VOR. In addition, the following will be provided:

- (a) refurbishing of the existing terminal for use as a general aviation terminal and repair of the existing apron and taxiway for use of light aircraft;
- (b) widening of the existing 1,410 x 30 m runway (16-34) to 45 m and lengthening to 2,200 m;
- (c) strengthening of the existing runway;
- (d) construction of a new taxiway and apron for large aircraft and rectification of any existing drainage problems; and
- (e) construction of an access road to the new terminal from the main highway.

C. Airport Zoning Ordinances

11. Zones along the sides of both airports would be established and land use restricted to types insensitive to aircraft flight requirements and noise.

12. Zones at the ends of each runway under the approach and departure paths of aircraft would be established with height restrictions for buildings in addition to land use restrictions.

D. Utilities

13. Electrical services will be brought from the main distribution substations at San Jose del Cabo and Loreto to the airports. Distribution within the airports will be under various contracts depending upon the ultimate use.

14. Potable water will be provided through the use of bore holes and underground storage tanks. Pressure for the domestic system will be provided by pneumatic tanks. High pressure pumps will be provided for the fire hydrant ring system.

15. Sewage disposal will be accomplished by means of septic tanks and leaching fields. Aircraft sewage wastes will be passed through a treatment plant to neutralize the antiseptic solutions prior to introduction into the airport sanitary system.

16. Solid wastes from the aircraft and airport will be incinerated.

E. Aeronautical Considerations

17. Procedures have been developed based on the VOR/DME for both approach and departure from the airways and the airports. The provision of an NDB will provide a means for aircraft not equipped with VOR/DME to navigate and land at the airports.

18. In the future, either end of the runways could be fitted with instrument landing systems (ILS). Such installations should be seriously considered as soon as heavy aircraft traffic develops, since vertical and lateral guidance during landing approaches is highly desirable for large jet aircraft.

19. Although San Jose del Cabo is listed in the existing US/Mexico bilateral agreement on three US routes and two Mexican routes serving a total of four US cities, assurances have been obtained during negotiations that the Government would make its best efforts to retain as a minimum these points in future bilateral agreements and that scheduled international air service be initiated to coincide with the opening of the first hotels.

20. Loreto is not listed in any bilateral agreement. Accordingly, assurances were obtained during negotiations that the Government will make its best efforts to include Loreto in future bilaterals and that scheduled international air service be initiated on these routes as soon as the first hotels are opened. In the event that the signing of bilateral air agreements are delayed beyond the opening date of the first hotels, the Government has agreed to begin unilaterally scheduled international air service to the United States from Loreto by adding Loreto to the end, in each direction, of existing international routes.

This might necessitate changing the flight number of a through aircraft at the previous terminal point of the flight. An example of such a flight could be illustrated by adding Loreto at each end of the existing flights-- Puerto Vallarta, Monterrey, Houston, Monterrey, Puerto Vallarta or Mazatlan, Puerto Vallarta, Guadalajara, Dallas, Guadalajara, Puerto Vallarta, Mazatlan. Actual flights to accomplish this purpose would in all likelihood be different.

F. Engineering Services

21. All engineering work associated with the airports will be done by the Secretariat of Human Settlements and Public Works (SAHOP) with technical assistance provided by the Secretariat of Communications and Transport (SCT) Airports and Auxiliary Services (ASA), Aeronautical Radio of Mexico (RAMSA), and National Company of Aviation Combustibles (NACOA). SAHOP has designed and supervised the construction of many airports in the past and is fully competent to execute this component of the tourism project.

G. Environmental Considerations

22. At San Jose del Cabo, because of prevailing winds, 90% of the landings and take-offs will be from the south. The problems of noise at San Jose del Cabo will be minimized through the adoption of flight procedures which place aircraft over agricultural land (12 km away).

23. At Loreto the approach will be over the water about 90% of the time. The departure zone will cross the existing town (6 km away). The urban plan has been so designed however, that no residences will be constructed in the path of aircraft flights.

24. The leaching fields associated with the sewage disposal systems will introduce a pure effluent directly into the ground water with no harmful effects. Aircraft and industrial wastes will be treated prior to their introduction into the sanitary system to remove all harmful elements.

25. Solid wastes will be incinerated in furnaces designed to release no unburned material into the air. Ashes will be buried in landfill areas on the airports.

H. Cost Estimates

26. Detailed cost estimates for the airport component are shown in Annex I, Table 6. The cost estimates were developed by SAHOP and are based on quantities obtained from field survey data and preliminary architectural drawings. The unit costs used are comparable to costs of similar work designed and constructed under the supervision of SAHOP, and are considered reasonable. Construction is expected to take two years.

I. Procurement

27. A high percentage of the material required for the project is produced in Mexico. However, because of lower transportation costs and of the duty free aspect of Baja California, a large portion of the material may come from the United States. Contractors for airport construction are fairly numerous in Mexico and are generally the only tenderers on airport work. However, the location of the airports may encourage US contractors to bid. The manufacture and installation of the communications equipment will be done by foreign contractors.

28. A portion of the navaid equipment will be obtained from Wilcox Electric Company, Division of American Standard, Kansas City, Missouri. The cost of this procurement will be about US\$700,000 and will consist of the manufacture and installation of two Wilcox VOR/DME's. There is ample justification for purchasing this equipment from this manufacturer. All VOR's in Mexico (47) are Wilcox; supply support is based on this one type of equipment; the electronic maintenance technicians are trained for this equipment; test equipment for this specific VOR is available in quantity in the country. The only DME's in Mexico (20) are Wilcox and the Wilcox DME is specifically designed to mate with Wilcox VOR.

J. Aviation Administration

29. The responsibility for the administration and operation of aviation in Mexico devolves upon four organizations. The design and supervision of construction of airports and their buildings is the responsibility of two divisions within SAHOP. After construction, the maintenance of the field lighting and collection of landing and rental charges is that of ASA. RAMSA is responsible for the operation and maintenance of the navaids, communication gear and their operational areas (control tower, etc.) and is in complete control of enroute and terminal air traffic. The Directorate General of Civic Aeronautics is in charge of establishing air routes and procedures, licensing, negotiating bilateral air agreements and other policy type matters. DGCA is a governmental agency and reports to SCT. RAMSA, which is a corporation partially owned by the Government and partially by airlines serving Mexico, also reports to SCT. ASA, the airport operator, is a governmental agency but reports to neither SAHOP nor SCT. It reports directly to the Secretariat of the Presidencia.

30. A fifth organization operates the fuel services. NACOA is a partially government owned corporation which operates under very exacting standards. The fuel being processed is continually under test to assure the airlines that the fuel meets their specifications. Since the fuel being processed actually belongs to the airlines involved, the only income NACOA realizes is derived from a through-put charge. This charge is established by SCT, not by NACOA.

31. The various other charges are also established by SCT, although some are upon the recommendation of the operating services. For example, enroute communication charges and navigational aid user charges are established by SCT upon the recommendations of DGCA and RAMSA; landing charges for each category of airport and terminal building rental charges are established by SCT upon recommendations of ASA. The responsibility for collecting these charges rests with RAMSA and ASA respectively.

K. Financial Aspects

32. Projected Statements of Income and Expense in 1976 prices for Loreto and the San Jose del Cabo airport for the seven years 1980/81 to 1986/87 are shown in Tables 1 and 2 of this annex. It is assumed that both airports will be operated as independent units. While the responsibility for the administration and operation of aviation in Mexico falls on five organizations, the financial projections assume a consolidation of activities as though it were one organization. It is also assumed that all new airport investment costs will become assets of the airports and that existing assets are not an incremental project cost and can be transferred on a zero book value basis.

33. Assumptions used in projecting revenue include:

- (a) Commercial landing fees are the primary revenue source. These fees, set nationally, vary with weight and presently average 2000 pesos for a DC-9 (flown by AeroMexico) and 3000 pesos for a 727. It is assumed that these charges will be raised 20% from present levels in accordance with Bank recommendations (Loan 1022) prior to initiation of significant activity in 1980.
- (b) General aircraft landing fees are assumed to average 10% and other income, including rentals, fuel throughput and concessions will average 9% of commercial landing fee income.
- (c) 70% of all tourists will arrive by air. 60% of these air passengers will embark from Mexican origin points and 40% will embark elsewhere. The number of tourists is derived from occupant days as projected in Annex VII and assumes an average duration of stay of four days in hotel/apartels and ten days in condominiums and villas.
- (d) Half of the tourists arriving from points within Mexico will travel by 727 and half by DC-9. Planes will operate at 60% of occupancy. Two-thirds of the passengers arriving from international destinations

will arrive by chartered 727 averaging 90% of capacity and the remainder will arrive by commercial 727 averaging 50% of capacity. It is assumed there is no seasonality in the traffic.

- (e) Air cargo and non-tourist air traffic will not be significant.
- (f) 40% of departing air passengers will pay a Mex\$50 international departure tax and 60% will pay a Mex\$10 domestic departure tax. These taxes are assumed to represent project revenues although in practice they will not be retained by the airport authority but will go directly to the national treasury.

34. Assumptions used in projecting expenses are:

- (a) All operating expenses, i.e., labor, materials, services, and SAHOP maintenance costs will be the same US dollar equivalent as projected for the Bank's 1974 financial analysis for a similar operation at Villahermosa Airport. These projections assumed a conversion rate of Mex\$12.50 to US\$1 and a 2% increase in costs per year in real terms.
- (b) An ASA overhead allocation of about 16% of operating costs will be levied on the two airports.
- (c) Depreciation on a 20-year straight line basis will be charged only on the incremental project investment excluding price contingencies to express the expense in 1976 dollars.
- (d) No interest expense or loan amortization requirements will be imposed.

35. The projected financial results on the basis of these assumptions, including departure taxes as revenues, are:

- (a) For Loreto, the project achieves an operating cash surplus in 1981/82, the second full year of operation and achieves a positive net operating revenue position in 1983/84 following deficits during the construction years and three years of full operation. Thereafter, the simple annual financial rate of return improves steadily reaching 10.8% of average net fixed assets by 1986/87.

- (b) For San Jose del Cabo, the airport project achieves an operating cash surplus in 1982/83, the third full year of operation, and achieves a positive net operating revenue position in 1984/85, the fifth full year of operation. Thereafter, the simple annual financial rate of return improves steadily reaching 17% of initial average net fixed assets by 1986/87.
- (c) Increased flights generated by the airport investments will significantly increase landings and, hence, landing fees at other Mexican airports, with little increase in operating costs or investments. The net return to ASA, therefore, is considerably higher than the projections suggest.

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

LORETO INTERNATIONAL AIRPORT

PROJECTED OPERATING INCOME AND EXPENSES

<u>Fiscal Year Ending June 30</u>	<u>1981</u>	<u>1982</u>	<u>1983</u> US\$ '000	<u>1984</u> (1976 prices)	<u>1985</u>	<u>1986</u>	<u>1987</u>
<u>Total Revenues</u>							
Commercial Landing Fees	49.7	148.9	244.0	349.3	458.9	533.5	574.8
Miscellaneous Landing Fees	5.0	14.9	24.4	34.9	45.9	53.4	57.5
Other Income/ ^a	4.5	13.4	22.0	31.4	41.3	48.0	51.7
Sub-Total	59.2	177.2	290.4	415.6	546.1	634.9	684.0
Departure Taxes	31.2	93.6	153.4	219.7	288.6	335.4	361.4
Total Revenue	90.4	270.8	443.8	635.3	834.7	970.3	1045.4
<u>Operating Expenses</u>							
Labor	92.2	94.1	96.0	97.9	99.8	101.8	103.8
Materials ^b	11.9	12.1	12.4	12.6	12.9	13.2	13.4
Services	32.9	33.5	34.2	34.9	35.6	36.3	37.0
SOP Maintenance Costs	28.8	29.4	29.9	30.5	31.1	31.7	32.4
Total Working Costs	165.8	169.1	172.5	175.9	179.4	183.0	186.6
Operating Revenue Before Allocations and Depreciation	(75.4)	101.7	271.3	459.4	655.3	787.3	858.8
Less ASA Overhead Calculation	27.0	27.5	28.0	28.6	29.1	29.7	30.3
Less Depreciation	348.0	348.0	348.0	348.0	348.0	348.0	348.0
Net Operating Revenue Including Departure Taxes (loss)	(450.4)	(273.8)	(104.7)	82.8	278.2	409.6	480.5
Net Operating Revenue Excluding Departure Taxes (loss)	(481.6)	(367.4)	(258.1)	(136.9)	(10.4)	74.2	119.1
Annual % Return on Net Fixed Assets Including Departure Taxes	(6.9)	(4.4)	(1.8)	1.5	5.4	8.5	10.8
Annual % Return on Net Fixed Assets Excluding Departure Taxes	(7.4)	(5.9)	(4.4)	(2.5)	(.2)	1.5	2.7

^a Includes rentals, fuel through put, concession, etc.

^b Includes cleaning electricity, water, telephone, etc.

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

SAN JOSE DEL CABO INTERNATIONAL AIRPORT

PROJECTED OPERATING INCOME AND EXPENSES

<u>Fiscal Year Ending June</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>	<u>1987</u>
			US\$ '000	(1976 prices)			
<u>Total Revenues</u>							
Commercial Landing Fees	20.8	91.1	140.6	206.8	283.3	363.8	438.3
Miscellaneous Landing Fees	2.1	9.1	14.1	20.7	28.3	36.4	43.8
Other Income ^a	1.9	8.2	12.7	18.6	25.5	32.7	39.4
<u>Sub-Total</u>	<u>24.8</u>	<u>108.4</u>	<u>167.4</u>	<u>246.1</u>	<u>337.1</u>	<u>432.9</u>	<u>521.5</u>
Departure Taxes	13.0	57.2	88.4	130.0	178.1	228.8	275.6
<u>Total Revenue</u>	<u>37.8</u>	<u>165.6</u>	<u>255.8</u>	<u>376.1</u>	<u>515.2</u>	<u>661.7</u>	<u>797.1</u>
<u>Operating Expenses</u>							
Labor	92.2	94.1	96.0	97.9	99.8	101.8	103.8
Materials	11.9	12.1	12.4	12.6	12.9	13.2	13.4
Services ^b	32.9	33.5	34.2	34.9	35.6	36.3	37.0
SOP Maintenance Costs	28.8	29.4	29.9	30.5	31.1	31.7	32.4
<u>Total Working Costs</u>	<u>165.8</u>	<u>169.1</u>	<u>172.5</u>	<u>175.9</u>	<u>179.4</u>	<u>183.0</u>	<u>186.6</u>
Operating Revenue Before Allocations and Depreciation	(128.0)	(3.5)	83.3	200.2	335.8	478.7	610.5
Less ASA Overhead Calculation	27.0	27.5	28.0	28.6	29.1	29.7	30.3
Less Depreciation	186.3	186.3	186.3	186.3	186.3	186.3	186.3
Net Operating Revenue Including Departure Taxes (loss)	(341.3)	(217.3)	(131.0)	(14.7)	120.4	262.7	393.9
Net Operating Revenue Excluding Departure Taxes (loss)	(354.3)	(274.5)	(219.4)	(144.7)	(57.7)	33.9	118.3
Annual % Return on Net Fixed Assets Including Departure Taxes	(9.9)	(6.7)	(4.3)	(.5)	4.5	10.5	17.0
Annual % Return on Net Fixed Assets Excluding Departure Taxes	(10.3)	(8.4)	(7.2)	(5.0)	(2.1)	1.4	5.1

^a Includes rentals, fuel through put, concession, etc.

^b Includes cleaning, electricity, water, telephone, etc.

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

Part I. Water Supply, Sewerage and Storm Drainage for Loreto

I. Project Description

A. Water Supply

(a) Loreto-Tourism Zone

1. The project foresees the provision of water for the tourism zone of Nopoló from the aquifer of Primera Agua drainage basin, about 5 km north of the tourism zone and, if necessary, complemented by water extracted from the aquifer of the Loreto Creek Valley. The facilities include:

- (i) a transmission main of asbestos cement pipe, 8" and 10" in diameter and 10.5 km in length, with an intermediate booster pumping station;
- (ii) use of an already constructed water storage tank to provide for peak demands of the tourism zone (Nopoló) and for reserve storage;
- (iii) distribution system inside the tourism zone which will include 9.6 km of asbestos cement pipe, ranging from 3" to 16".

(b) Town of Loreto

2. Water from Loreto Creek Valley aquifer is presently used for supplying the local population of Loreto and will continue to be the source for the expanded system. The distribution system is composed of 8 circuits, representing 12.7 km of asbestos cement pipe ranging from 4" to 12". In addition, there will be 41.4 km of secondary service mains of 3" pipe.

B. Sewerage

(a) Loreto-Tourism Zone

3. Sewage collected in the tourism zone will flow toward two pumping stations. The sewage arriving at the pumping station in the southern part of the tourism zone will be elevated to a point from which it can reach by gravity the north pumping station. This second station will pump the total

sewage flow to stabilization ponds through a 10" asbestos cement pipe of about 2 km in length. The effluent, after treatment, will be used for irrigation purposes. The length of the sewer to be installed is about 10.6 km. Sewer lines will be made of concrete pipe in diameters up to 18" and of reinforced concrete for larger pipes.

(b) Town of Loreto

4. The sewage from the entire town will flow to a pumping station located near the seashore, and from there pumped back through a 10" asbestos cement pipe of about 5 km in length to the stabilization ponds. The effluent will be used for irrigation purposes. The sewerage system of Loreto includes about 5 km of collectors ranging in diameter from 10" to 24", lateral sewers of 8" and house connections of 6".

C. Storm Drainage

(a) Loreto-Tourism Zone

5. Storm water will be allowed to flow on the street pavement to a low point, where an outfall - 150 m long - has been provided to discharge the water into a nearby estuary. To assure the surface flow, some cuts and fillings will be made in a number of streets to obtain continuous descending slopes.

(b) Town of Loreto

6. An open channel crossing the middle of the town will intercept the storm water from the upper portions of town and discharge it into a nearby creek. For the lower portions of the town, 4 outfalls have been provided which will discharge the storm water into the sea.

II. Cost Estimates

7. The estimated cost of the water supply, sewerage and storm drainage is summarized in Annex I. Cost estimates were prepared by consultants to FONATUR and based on the Unit Price Catalogue issued by SARH, and adjusted to take into account the effects of devaluation. Unit costs represent the Mexican cost of goods and civil works and appear reasonable.

III. Administration of the Project

8. FONATUR will employ consultants for the final design of the project, which will be prepared in accordance with SARH standards. Supervision of construction will be done by FONATUR, with the assistance of SARH. The system will be operated and maintained by a Junta Local de Agua Potable, with representatives of the state government, local authority, SARH and FONATUR.

Part II. Water Supply, Sewerage and Storm Water Drainage
for San Jose del Cabo

I. Project Description

A. Water Supply (Tourism and Urban Areas)

9. A major aqueduct has been constructed by SARH to serve the towns in the southern tip of Baja California peninsula. The water is extracted from four wells located between San Jose Viejo and Santa Anita in the valley of San Jose Creek. The transmission line is an 18" asbestos cement pipe which runs down the valley to San Jose del Cabo and then along the coast to Cabo San Lucas. The capacity of the aqueduct is 200 l/sec, of which about half would be designated for the project.

10. As the selected tourism zone is close to the town of San Jose del Cabo, the water storage facilities will be common for both areas. There will be two systems, one for the main sections of the town and the tourism zone (areas located from sea level to 40 m above sea level), and the second for the areas between 40 m to 60 m above sea level.

11. The low lying areas will be supplied by gravity from the aqueduct to storage tanks at an elevation of 55 m, and from there by gravity to the distribution systems. The required storage capacity is 1,200 m³. The higher sections will be supplied from the aqueduct through a pumping station to the storage tanks and from there by gravity to the distribution systems. The distribution system for the town and tourism zone will include 23.6 km of asbestos cement mains ranging from 2½" to 16" in diameter and the installation of 1,593 connections with water meters.

B. Sewerage (Tourism and Urban Areas)

12. The sewage from the town of San Jose del Cabo will flow by gravity to a low point in the area, from where it will be pumped to stabilization ponds. From the ponds the effluent, after treatment, will flow by gravity to agricultural areas below. The length of sewers to be installed is 14 km, ranging from 8" to 30" in size. Sewer lines will be made of concrete, with diameters varying from 8" to 18" and of reinforced concrete from 18" to 30".

C. Storm Water Drainage (Tourism and Urban Areas)

13. A system of two interceptors is proposed to collect and divert the storm water from the higher areas surrounding the town of San Jose del Cabo and the tourism zone. The north interceptor will protect the tourism zone and will be an open channel 1,300 m long. Roads and streets have been designed with proper slopes to carry the rainfall into the sea.

D. Cost Estimates

14. The estimated cost of the water supply, sewerage and storm drainage components of San Jose del Cabo town and tourism zone is summarized in Annex I. Cost estimates were prepared by consultants to FONATUR and based on the Unit Price Catalogue issued by SARH. Unit costs are based on the Mexican cost of goods and civil works and appear reasonable. Engineering and administrative costs have been estimated at 10% of construction cost.

E. Administration

15. FONATUR will employ consultants for final designs of the project which will be prepared in accordance with SARH standards. Supervision of construction will be carried out by FONATUR with the assistance of SARH. The system will be operated and maintained by a junta local which will have representatives of the state government, the municipality, SARH and FONATUR.

Part III. Financial Aspects--Loreto and San Jose del Cabo

16. Financial projections were made for the water supply and sewerage components in the form of income statements, balance sheets, and sources and applications of funds statements for the eight years 1977/78 to 1984/85. These projections are shown in Tables 1 to 6 of this annex. All projections are in current US thousands of dollars assuming international annual inflation rate projections for export prices.

17. Underlying assumptions on which these projections are based include:

- (a) Both the Loreto/Nopolo and San Jose del Cabo water and sewerage operations will be operated as independent units managed by a local commission or junta.
- (b) All new headworks and equipment investments will become assets of these new organizations. Existing system assets in San Jose del Cabo will be retained by SARH while those in Loreto will be transferred to the junta. Distribution network investment (with the exception of network equipment) and the cost of professional services will be borne by FONATUR's real estate operations and are not carried on the financial statements of the juntas.

- (c) Tariff assumptions for Loreto and San Jose del Cabo are Mex\$1.90 per m³ for hotels, Mex\$5.00 for condominiums and villas and Mex\$4.00 for urban sales. These tariffs are the same as those established in 1976 for parallel services in a similar situation at Cancun. Tariffs are assumed to increase through 1982/83 in Loreto and 1983/84 in the case of San Jose del Cabo in line with inflation. Bad debt expense is 5% of urban sales. Connection fees, the same as at Cancun, are Mex\$1,000 per room for hotels, Mex\$5,000 for condominiums and villas and Mex\$1,000 for urban homes. Recycled water will be sold at Mex\$0.25 per cubic meter and will be used for irrigation purposes.
- (d) Consumption assumptions are 0.6 m³ per occupant day for tourists; 0.2 m³ per day for the urban population. Wastage and free municipal use will total 25% of revenue producing consumption. Occupant days are derived from projections in Annex VII. Population is projected to rise from 3,000 in 1976/77 to 18,800 by 1985 for Loreto and from 4,000 to 18,500 in 1985 for San Jose del Cabo, based on employment generation projections in Annex X and assuming 1.5 workers per household, 5 people per household and 100% connections. Construction workers are assumed not to have separate connections.

18. Operating expense assumptions include:

- (a) Direct employment by the junta to operate and maintain the system will rise gradually to 46 people in Loreto and 32 people in San Jose del Cabo. The lowest paid personnel, e.g., meter readers and messengers will receive Mex\$50,000 per annum including fringe benefits while skilled personnel will receive multiples of 1.25 to 3 times this base.
- (b) Electricity costs are based on national tariff rates of US1.5 cents per kWh and chlorine on current prices of US.30 cents per kg. Usage would vary directly with production.
- (c) Annual maintenance costs are 6% of initial equipment investment costs, 3% of initial headwork investment costs, and 1.5% of initial network investment costs, excluding the costs of permanent professional staff. Administrative costs are estimated at US\$15,000 per year.

- (d) Depreciation is straight-line and is 2.5% per year for headworks and 20% for equipment. In lieu of depreciation, an annual reserve of 1.5% of the value of network and professional services is set aside for future replacement, but does not represent a deduction from income.
- (e) Interest expense of 18% per annum on average balance outstanding is incurred on short-term borrowings. No interest income is accrued for excess cash on hand.
- (f) The junta in San Jose del Cabo will purchase water in bulk from SARH at a price of US7.8 cents per m³. Of this tariff, US1.6 cents represents current expenses, US4.1 cents represents depreciation over twenty years and US2.1 cents goes to a reserve fund for future expansion. The current expense portion is adjusted upward for inflation at the end of the fifth year and each year thereafter.

19. Balance sheet assumptions include a minimum cash balance of 30 days operating expenses, average accounts receivable of 36 days, current liabilities of 60 days operating expenses, no dividends, and replacement of equipment on terms of 20% down payment, 18% interest and a ten year repayment period.

20. The projected financial results on the basis of these assumptions are:

- (a) For Loreto, the simple annual financial rate of return reaches 2.8% of average net fixed asset investment in the third full year of operations (the sixth year from initiation of construction) and 12.3% in the fifth year assuming tariffs rise with inflation through 1983. The junta must resort to short-term borrowing in amounts reaching as high as U\$87,000 over the two-year period 1980/81 to 1981/82 to cover cash deficits. While the projected current ratio, assuming repayment of the loan drops to a low of .37 in 1980/81, no serious liquidity problem should arise because of the strong equity position and adequate additional borrowing power.
- (b) For San Jose del Cabo, the annual financial rate of return reaches 8.3% of net fixed asset investment in the fourth full year of operation (the sixth year from initiation of construction) and 14.6% in the fifth year assuming tariffs rise with inflation through 1984. The junta must resort to short-term borrowing in amounts reaching as high

as US\$139,000 during the six-year period 1978/79 to 1983/84 to cover cash deficits. While the projected current ratio drops to .26 in 1980/81, this does not constitute a serious liquidity problem because of the strong equity position and adequate borrowing power.

- (c) Both projects are characterized by initial periods of losses and tight liquidity conditions followed by higher profits and the creation of high cash reserves in later years.
22. During negotiations, assurances were obtained that all of the investment costs for the water supply and sewerage systems in the project areas would be recovered either through land sale prices or user charges and that water supply and sewerage charges would be sufficient to cover: (a) the costs of operation and maintenance of such facilities, including depreciation based on a reasonable valuation of all headworks and equipment costs, (b) increases in working capital, and (c) the financing of minor expansion of the facilities.

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

WATER SUPPLY AND SEWERAGE FOR LORETO

PROJECTED INCOME STATEMENT (1978-1985)

<u>Fiscal Year Ending June 30</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>
				Thousands m ³				
<u>Water Usage</u>								
Tourism Consumption	35.5	39.0	42.6	81.6	263.7	441.0	639.4	848.9
Urban Consumption	292.0	416.1	584.0	642.4	854.1	1022.0	1233.7	1372.4
Unaccounted for Water	81.9	113.8	156.7	181.0	279.5	365.8	468.3	555.3
Total Water Usage	409.4	568.9	783.3	905.0	1397.3	1828.8	2341.4	2776.6
				US\$ '000 (Current Prices)				
<u>Revenues</u>								
Tourist Sales	15.8	18.6	21.8	44.8	148.6	263.1	378.6	499.1
Urban Sales	65.7	100.8	151.7	178.5	253.7	325.1	392.4	436.5
Miscellaneous Income	.6	2.5	1.7	30.8	19.4	61.1	66.3	68.9
Less Bad Debt	(3.3)	(5.0)	(7.6)	(8.9)	(12.7)	(16.3)	(19.6)	(21.8)
Net Total Revenue	78.8	116.9	167.6	245.2	439.0	633.0	817.7	982.7
<u>Operating Expenses</u>								
Personnel	19.7	101.5	116.9	203.2	221.1	245.7	271.2	290.3
Maintenance + Administrative	6.7	25.4	52.5	142.6	152.6	163.4	174.7	187.0
Electricity/Chemicals	3.3	4.8	7.1	8.8	14.6	20.4	27.9	35.5
Depreciation	12.4	44.3	92.3	129.1	138.3	147.9	158.2	169.3
Total Operating Expense	42.1	176.0	268.8	483.7	526.6	577.4	632.0	682.1
Net Income Before Interest	36.7	(59.1)	(101.2)	(238.5)	(87.6)	55.6	185.7	300.6
Interest on Long-Term Debt	--	--	--	--	--	--	--	73.2
Interest on Short-Term Debt	--	--	--	7.8	13.8	6.0	--	--
Net Income	36.7	(59.1)	(101.2)	(246.3)	(101.4)	49.6	185.7	227.4
Return on Net Fixed Assets	23.2	(9.7)	(7.1)	(12.1)	(4.4)	2.8	8.4	12.3

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

WATER SUPPLY AND SEWERAGE FOR LORETO

PROJECTED BALANCE SHEETS (1978-1985)

<u>Fiscal Year Ending June 30</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u> US\$ '000 (Current Prices)	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>
<u>Assets</u>								
<u>Fixed Assets</u>								
Plant in Service Adjusted for Revaluation	329.0	957.7	2115.5	2263.5	2422.1	2591.5	2773.0	2967.1
Less Depreciation	12.4	57.6	154.1	294.0	452.8	632.4	326.7	518.9
Net Plant in Service	316.6	900.1	1961.4	1969.5	1969.3	1959.1	2446.3	2448.2
<u>Current Assets</u>								
Cash	40.1	20.7	14.7	29.6	32.4	35.8	112.5	431.2
Network Replacement Reserve (Cash)	6.1	23.9	23.3	--	--	115.1	271.0	320.5
Accounts Receivable	7.9	11.7	16.8	24.5	43.9	63.3	80.4	111.9
Total Current Assets	54.1	56.3	54.8	54.1	76.3	214.2	463.9	863.6
Total Assets	370.7	956.4	2016.2	2023.6	2045.6	2173.3	2910.2	3311.8
<u>Liabilities</u>								
<u>Capital and Reserves</u>								
Paid-in-Capital	329.0	933.0	2039.0	2039.0	2039.0	2039.0	2039.0	2039.0
Retained Earnings	36.7	(22.4)	(123.6)	(369.9)	(471.3)	(421.7)	(236.0)	(8.6)
Reserve for Revalued Assets	--	23.8	71.4	208.6	346.7	484.4	621.7	792.9
Total Capital	365.7	934.4	1986.8	1877.7	1914.4	2101.7	2424.7	2823.3
<u>Long-Term Debt</u>								
--	--	--	--	--	--	--	403.0	398.8
<u>Current Liabilities</u>								
Accounts Payable	5.0	22.0	29.4	59.1	64.7	71.6	79.0	85.5
Current Portion--Long-Term Debt	--	--	--	--	--	--	3.5	4.2
Short-Term Borrowing	--	--	--	86.8	66.5	--	--	--
Total Current Liabilities	5.0	22.0	29.4	145.9	131.2	71.6	82.5	89.7
Total Liabilities and Capital	370.7	956.4	2016.2	2023.6	2045.6	2173.3	2910.2	3311.8

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

WATER SUPPLY AND SEWERAGE FOR LORETO

PROJECTED SOURCES AND APPLICATIONS OF FUNDS (1978-1985)

<u>Fiscal Year Ending June 30</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u> US\$ '000 (Current Prices)	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>
<u>Sources of Funds</u>								
<u>Internal Cash Generation</u>								
Net Income Before Interest	36.7	(59.1)	(101.2)	(238.5)	(87.6)	55.6	185.7	300.6
Depreciation	12.4	14.3	92.3	129.1	138.3	147.9	158.2	169.3
Total	49.1	(14.8)	(8.9)	(109.4)	50.7	203.5	343.9	469.9
<u>External Cash Generation</u>								
Long-Term Loan	--	--	--	--	--	--	--	--
Equity	329.0	604.0	1106.0	--	--	--	--	--
Short-Term Borrowing	--	--	--	86.8	--	--	406.5	--
<u>Total Sources</u>	<u>378.1</u>	<u>589.2</u>	<u>1097.1</u>	<u>(22.6)</u>	<u>50.7</u>	<u>203.5</u>	<u>750.4</u>	<u>469.9</u>
<u>Applications of Funds</u>								
<u>Capital Expenditure</u>								
Proposed Project	329.0	604.0	1106.0	--	--	--	508.1	--
<u>Debt Service</u>								
Interest--Long-Term Loan	--	--	--	--	--	--	--	73.2
Interest--Short-Term Loan	--	--	--	7.8	13.8	6.0	--	--
Amortization--Long-Term Loan	--	--	--	--	--	--	3.5	4.2
Amortization--Short-Term Loan	--	--	--	20.3	66.5	--	--	--
Total	--	--	--	7.8	34.1	72.5	3.5	77.4
<u>Working Capital Requirement</u>								
<u>Total Applications</u>	<u>49.1</u>	<u>(14.8)</u>	<u>(8.9)</u>	<u>(30.4)</u>	<u>16.6</u>	<u>131.0</u>	<u>238.8</u>	<u>392.5</u>
	<u>378.1</u>	<u>589.2</u>	<u>1097.1</u>	<u>(22.6)</u>	<u>50.7</u>	<u>203.5</u>	<u>750.4</u>	<u>469.9</u>

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

WATER SUPPLY AND SEWERAGE FOR SAN JOSE DEL CABO

PROJECTED INCOME STATEMENT (1978-1985)

<u>Fiscal Year Ending June 30</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>
				Thousands m ³				
<u>Water Usage</u>								
Tourism Consumption								
Urban Consumption	--	--	--	35.5	162.3	255.7	378.9	519.9
Unaccounted for Water	343.1	394.2	576.7	678.9	861.4	992.8	1182.6	1350.5
Total Water Usage	85.8	98.6	144.2	178.6	255.9	312.1	390.4	467.6
	<u>428.9</u>	<u>492.8</u>	<u>720.9</u>	<u>893.0</u>	<u>1279.6</u>	<u>1560.6</u>	<u>1951.9</u>	<u>2338.0</u>
<u>Revenues</u>								
Tourist Sales								
Urban Sales	--	--	--	19.5	91.7	152.1	239.4	325.9
Miscellaneous Income	77.2	95.5	149.8	188.7	255.8	315.8	402.3	459.4
Less Bad Debt	.8	.8	3.6	30.8	31.5	31.0	39.6	49.7
Net Total Revenue	(3.9)	(4.8)	(7.5)	(9.4)	(12.8)	(15.8)	(20.1)	(23.0)
	<u>74.1</u>	<u>91.5</u>	<u>145.9</u>	<u>229.6</u>	<u>366.2</u>	<u>483.1</u>	<u>661.2</u>	<u>812.0</u>
<u>Operating Expenses</u>								
Personnel								
Maintenance + Administrative	19.7	59.8	64.1	125.9	134.7	153.1	167.9	184.5
Electricity/Chemicals	6.7	18.8	45.3	90.0	96.3	103.1	110.2	118.0
SHH Fee-Current Items	3.8	4.3	5.7	6.8	9.0	11.1	14.1	17.2
SHH Fee-Depreciation and Reserves	6.9	7.9	11.6	14.4	20.6	59.7	79.7	102.2
Depreciation	26.5	30.5	44.6	55.2	79.1	96.5	120.6	144.5
Total Operating Expense	8.4	42.7	75.3	87.8	93.9	100.5	107.5	115.1
	<u>72.0</u>	<u>164.0</u>	<u>246.6</u>	<u>380.1</u>	<u>433.6</u>	<u>524.0</u>	<u>600.0</u>	<u>681.5</u>
<u>Net Income Before Interest</u>								
Interest on Long-Term Debt	2.1	(72.5)	(100.7)	(150.5)	(67.4)	(40.9)	61.2	130.5
Interest on Short-Term Borrowing	--	--	--	--	--	--	--	65.7
Net Income	--	1.8	6.6	16.6	21.3	22.0	14.1	4.6
Return on Net Fixed Assets	2.1	(74.3)	(107.3)	(167.1)	(91.7)	(62.9)	47.1	60.2
	<u>3.4</u>	<u>(20.3)</u>	<u>(15.7)</u>	<u>(22.5)</u>	<u>(10.8)</u>	<u>(7.2)</u>	<u>8.3</u>	<u>14.6</u>

ANNUAL STATEMENT

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

WATER SUPPLY AND SEWERAGE FOR SAN JOSE DEL CABO

PROJECTED BALANCE SHEETS (1978-1985)

<u>Fiscal Year Ending June 30</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>								
	US\$ '000 (Current Prices)															
<u>Assets</u>																
<u>Fixed Assets</u>																
Plant in Service Adjusted for Revaluation	131.0	642.9	819.6	876.9	938.4	1004.1	1074.3	1149.5								
Less Depreciation	8.4	51.8	130.8	227.7	337.6	461.8	140.6	297.8								
Net Plant in Service	122.6	591.1	688.8	649.2	600.8	542.3	933.7	851.7								
<u>Current Assets</u>																
Cash	8.5	10.1	14.3	24.4	28.3	35.3	41.0	47.2								
Network Replacement Reserve (Cash)	5.2	--	--	--	--	--	--	112.9								
Accounts Receivable	7.4	9.2	14.6	23.0	36.6	48.3	62.1	76.3								
Total Current Assets	21.1	19.3	28.9	47.4	64.9	83.6	103.1	236.4								
Total Assets	143.7	610.4	717.7	696.6	665.7	625.9	1036.8	1088.1								
<u>Liabilities</u>																
<u>Capital and Reserves</u>																
Paid-in-Capital	131.0	633.0	773.0	773.0	773.0	773.0	773.0	773.0								
Retained Earnings	2.1	(72.2)	(179.5)	(346.6)	(438.3)	(501.2)	(454.1)	(393.9)								
Reserve for Revalued Assets	--	9.2	42.2	90.4	135.9	177.9	215.8	248.9								
Total Capital	133.1	570.0	635.7	516.8	470.6	449.7	534.7	628.0								
<u>Long-Term Debt</u>																
Accounts Payable	10.6	20.2	28.6	48.7	56.6	70.6	82.1	94.4								
Current Portion Long-Term Loan	--	--	--	--	--	--	3.1	3.7								
Short-Term Borrowing	--	20.2	53.4	131.1	138.5	105.6	51.2	--								
Total Current Liabilities	10.6	40.4	82.0	179.8	195.1	176.2	136.4	98.1								
Total Liabilities and Capital	143.7	610.4	717.7	696.6	665.7	625.9	1036.8	1088.1								

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

WATER SUPPLY AND SEWERAGE FOR SAN JOSE DEL CABO

PROJECTED SOURCES AND APPLICATIONS OF FUNDS (1978-1985)

Fiscal Year Ending June 30

	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>								
	US\$ '000 (Current Prices)															
<u>Sources of Funds</u>																
<u>Internal Cash Generation</u>																
Net Income Before Interest	2.1	(72.5)	(100.7)	(150.5)	(67.4)	(40.9)	61.2	130.5								
Depreciation	8.4	42.7	75.3	87.8	93.9	100.5	107.5	115.1								
Total	10.5	(29.8)	(25.4)	(62.7)	26.5	59.6	168.7	245.6								
<u>External Cash Generation</u>																
Long-Term Loan	--	--	--	--	--	--	--	--								
Equity	131.0	502.0	140.0	--	--	--	--	--								
Short-Term Borrowing	--	20.2	33.2	77.7	7.4	--	368.8	--								
<u>Total Sources</u>	<u>141.5</u>	<u>492.4</u>	<u>147.8</u>	<u>15.0</u>	<u>33.9</u>	<u>59.6</u>	<u>537.5</u>	<u>245.6</u>								
<u>Applications of Funds</u>																
<u>Capital Expenditure</u>																
Proposed Project	131.0	502.0	140.0	--	--	--	461.0	--								
<u>Debt Service</u>																
Interest--Long-Term Loan	--	--	--	--	--	--	--	65.7								
Interest--Short-Term Loan	--	1.8	6.6	16.6	24.3	22.0	14.1	4.6								
Amortization--Long-Term Loan	--	--	--	--	--	--	3.1	3.7								
Amortization--Short-Term Loan	--	--	--	--	--	32.9	54.4	51.2								
Total	--	1.8	6.6	16.6	24.3	54.9	71.6	125.2								
<u>Working Capital Requirement</u>																
<u>Total Applications</u>	<u>10.5</u>	<u>(11.4)</u>	<u>1.2</u>	<u>(1.6)</u>	<u>9.6</u>	<u>4.7</u>	<u>4.9</u>	<u>120.4</u>								
	<u>141.5</u>	<u>492.4</u>	<u>147.8</u>	<u>15.0</u>	<u>33.9</u>	<u>59.6</u>	<u>537.5</u>	<u>245.6</u>								

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

THE TOURISM SECTOR

A. Tourism Assets

1. Mexico is one of the world's major and most richly endowed tourist destinations. Its varied attractions include the architectural remains of a series of major civilizations; entertainment ranges from the modern and fashionable, to superb traditional music and dance; a wealth of contemporary creative arts; a shopping paradise that includes handicrafts and haute couture; an agreeable climate; excellent beaches that abound along the Pacific and Caribbean sea costs; and street scenes that reflect the varied cultural background of Mexico's populace. In addition, Mexico is located next to the US and Canada, one of the world's richest tourist supplier markets.

B. Tourist Arrivals--Trends and Characteristics

2. The proximity to the US and Canada, and the 2,000-mile border shared with the US, has made Mexico the most accessible and truly foreign destination for North American tourists. In addition, close business ties, growing prosperity in the US and Canada, direct air access to various destinations in Mexico, and rapid expansion in accommodations and other facilities combined to make the growth of tourism to Mexico possible. Visitor numbers have increased to reach 3.2 million in 1975.^{1/} In addition, there is the Mexican-US border traffic (estimated at 70 million in 1975), which is not counted as tourism. Part of this border traffic is in fact tourism, especially weekend traffic and a large hotel capacity has been built to cater to their needs in border towns, such as Tijuana and Ensenada.

3. The average growth of number of visitors was 13.9% between 1961-1965, 10.1% between 1965-1970 and declined to 6.7% between 1971-1975. The recent slowdown in growth has been caused by a combination of factors: the economic recession in the US; a Jewish boycott, especially by Jewish travel agencies in the US; and a strongly overvalued peso (Mexico before the devaluation of September 1976 was more expensive than Hawaii for those who stay in "classic hotels" and travelled by air).

1/ Visitor numbers include Mexicans residing abroad.

4. Mexico is accessible by land, sea and air. Table 1 demonstrates the increasing popularity of air travel. In 1975 and 1976, about half of all visitors arrived by plane, a result of declining costs of air travel and the opening up of more direct flights from major US and Canadian cities to destinations such as Acapulco, Merida, Guadalajara, La Paz and Puerto Vallarta. Arrivals by car from the US are mainly from the border states which generate over 65% of the US tourism to Mexico (Arizona 10%, California 23%, Texas 29% - Table 2). Although 85 to 90% of the foreign visitors are from the US (Table 3), the number of Japanese, Europeans and Latin Americans (especially from Brazil and Venezuela) coming to Mexico is increasing steadily.

5. According to a study carried out by the National Bank of Mexico in 1973, the main reasons which visitors cited for coming to Mexico were:

<u>Reason</u>	<u>Number of Tourists (000)</u>	<u>Percentage</u>
-pleasure trip	2,505.6	77.6
-business	176.2	5.5
-study	18.8	0.6
-transit	29.3	0.9
-visit to family	401.4	12.4
-visit to friends	40.9	1.3
-other reasons	54.2	1.7

In fact many trips are made for more than one reason and almost all trips include more than one destination. About 22% of all visitors enter Mexico via the Mexico City airport, about 35% declare Mexico City as their final destination.

6. Beach tourism appears to have grown considerably in the last years. Arrivals to Acapulco jumped with the opening of the international airport from 7,000 to 35,000 in 1966 and has continued to grow thereafter. The number of tourists declaring Puerto Vallarta or Mazatlan as their final destinations, for instance, show the growth of popularity of these resorts (Table 4), with a large percentage of the foreign visitors arriving by air.

7. Studies carried out by the National Bank of Mexico show that air travellers are bigger spenders than those arriving by land: US\$368.80 per person-trip for air travellers vs. US\$152.21 per person travelling overland in 1975 (Table 5). A sample survey carried out during the summer of 1976 shows average daily expenditures of Mex\$600 in Cancun.

8. Seasonality is not a major problem for the Mexican tourist industry. The small peaks occur in December, June, July and August, with a low in September when it rains (Table 6). The popularity of Mexico for conventions,

and the skillful management of this convention capacity has aided Mexico in reducing seasonality. The total capacity for conventions in hotels is about 34,000, of which 14,500 is in Mexico City, and approximately 8,500 in Acapulco. The recently added convention center at Acapulco (8,000 capacity) and Cancun (550) and the centers planned for Ixtapa (2,500), Mazatlan (2,000) and Merida (2,000) will probably make convention tourism even more important for Mexico in the future.

9. FONATUR estimates that domestic tourism totalled 14.8 million visits in 1975 or 28.4 million visitor nights. One large government-owned hotel company (Nacional Hotelera) estimates that half of its guests are Mexicans and hotel statistics for Cancun and Ixtapa show more Mexican than foreign guests. The average length of stay of Mexicans, however, is much shorter than for foreigners. The popularity of buying condominiums or second homes on the coast is growing rapidly among the Mexican middle-income families. Besides the large middle class which can afford vacations away from home, a still largely untapped market exists among the lower-income families. Measures have been taken by the Mexican Government to promote and open up opportunities for vacation for this segment of the population. Discounts on bus and railroad travel for the labor union members and the provision of camping sites, lodges and famitels, have considerably increased the possibilities for "social tourism."

10. The number of Mexicans travelling abroad increased from 272,800 in 1970 to 526,252 in 1975. Since the September devaluation many foreign trips were cancelled (travel agencies estimate an 85% cancellation for Mexican group tours abroad) and the number of Mexicans travelling abroad has probably fallen in 1976.

C. Development of Tourism Facilities

11. In 1975, there were 6,269 lodging establishments with 190,513 rooms, which represent an annual increase of 7.5% since 1970. The fastest increase in rooms has been in the "A" category and the biggest in "B" category, which reflects the increased demand for reasonably priced accommodation. Tables 7 to 9 show the present situation, growth rates and distribution of accommodation by type and category. There is a definite trend towards building hotels with larger capacity.

12. Hotel occupancy statistics are not available for the country as a whole, only for certain destinations. As shown in the table below hotel occupancy is remarkably high and even throughout the year in Mexico City with a peak in the summer. Occupancy rates in the first class hotels are even higher and there is a definite demand in Mexico City for more rooms in this category (Table 10). Cancun and Ixtapa-Zihuatanjo are still too new to have established any trends. Table 10 shows relatively high occupancy rates for first-class hotels in established beach resorts.

1975 Hotel Occupancy

	<u>Mexico City</u>	<u>Acapulco</u>
January	65.4	74.6
February	72.6	80.3
March	72.5	75.6
April	64.3	58.8
May	60.4	54.5
June	73.5	37.6
July	84.4	50.6
August	82.1	74.3
September	66.0	43.3
October	71.7	51.4
November	68.3	65.7
December	69.7	72.5
Average	70.9	56.9

13. Room rates are fixed by the Government, in principle, for four-year periods. Hotels have to submit their proposed room rates to a committee in the Secretariat of Tourism. In practice, however, rates are reviewed more often, especially because of frequent wage increases. A 20% increase in prices was granted after the September 1976 devaluation. Even with this increase in rates, prices in dollar terms returned to their 1974 levels, as can be seen from the table below:

Mexico City
Weighted Average Hotel
Room Rate by Class of Hotel

<u>Class of Hotel</u>	<u>1974</u>		<u>1975</u>		<u>1974/1975 % Change</u>	<u>1976^{a/}</u>	
	<u>Mex\$</u>	<u>US\$</u>	<u>Mex\$</u>	<u>US\$</u>		<u>Mex\$</u>	<u>US\$</u>
AA	379.82	30.39	481.47	38.52	27	577.72	29.03
A	236.54	18.92	327.22	26.18	38	392.66	19.73
B	149.53	11.96	193.24	15.46	29	231.89	11.65
C	80.44	6.44	113.03	9.04	41	135.64	6.82
D	42.85	3.43	86.92	6.96	203	104.30	5.24

a/ Based on the 20% price increase granted after devaluation (Aug. '76) and converting it into US\$ at US\$1 = Mex\$19.9.

Prices of other goods and services typically bought by tourists, such as local transportation, souvenirs, and restaurants, are now similar to (or below) those prevailing in 1973-74. Since prices have increased substantially over the last few years in most competing destinations, Mexico is now in a competitive position in terms of prices, particularly compared with the Caribbean and Hawaii.

14. Tourist facilities, other than hotels, have also flourished with the continued expansion in tourism. The number of travel agencies increased from a total of 468 in 1972 to 758 in 1976, a 62% increase in less than four years. These agencies serve the foreign tourist, but cater also to Mexicans taking vacations in the country and abroad. Tourists frequently use the services of transport companies or rent-a-car agencies. The number of agencies catering to the transport needs of tourism has also grown fast: from 43 in 1973 to 320 in 1976 for specialized transport; from 159 to 205 in the same period for rent-a-car agencies. The number of restaurants and bars and other such facilities have increased by about 14% between 1972 and 1976.

Accessibility

15. Mexico has a well developed land, sea and air transport network. During the period 1971-74, about US\$2 billion were spent on road construction, increasing the network of paved roads from 71,250 km in 1971 to 175,540 km in 1974. A ferry network has been developed, largely to link Baja California with the Mexican mainland. Cruises are being organized along the Pacific Coast, tying US and Mexican cities. Air accessibility has also improved, with 44 commercial airports in operation at present. International airports were recently opened at Zihuatanejo and Cancun, and Mexico City's airport, which in 1974 handled about 50% of all flight arrivals from abroad is being modernized and expanded. Although Mexico City, Acapulco and some other cities have good air connections with the US, Canada, South America, and Europe, some air access problems have developed in the last few years. These relate to air policies rather than to infrastructure. Unfortunately some of the airports are not serviced with the frequency and variety that made Mexico City and Acapulco major tourist destinations. This is the result of the lack of a new bilateral civil aviation agreement between Mexico and the US for the 1970-1976 period. The main casualties of the lack of such agreement are the new resorts of Cancun and Ixtapa-Zihuatanejo. In particular the latter, which is not included in the 1970 bilateral agreement had to be serviced by domestic flights during its first two years of operations (1975-1976), which affected the flow of foreign tourists. A new bilateral agreement with the US is expected to be signed in 1977, and there is growing awareness of the need to strike a balance between the interests of the tourism sector (that would benefit from a liberal air policy) and that of Mexico's national airlines.

D. Land Ownership

16. Under Mexican law foreigners cannot own land within 100 km of the international borders or 50 km of the coast. However, the Decree of April 29, 1971, permits accredited Mexican banks to act as trustees for foreigners. The banks can purchase land on behalf of foreigners and hold the land in trust for a 10-year period, renewable to a maximum of 30 years. After 30 years, foreigners can seek a new trust with another bank or instruct the bank to sell the land.

17. Much of the land in Mexico, and therefore many sites with tourism potential, belong to the ejidos, a communal land tenure form which dates back to the time of the revolution. Under this system an ejidatario has the right to use communal land but he is prohibited from selling, leasing, dividing or mortgaging his share. Only one of his children can inherit his right to be an ejidatario. In Baja California, it is estimated that only 20% of the land is in private hands with 80% belonging to ejidos or the Government. Ejido land can be expropriated by presidential decree for purposes stated in the Federal Agrarian Reform Law, including tourism development purposes. Public agencies and ejidos themselves have the right to propose expropriation, but the Department of Agrarian Affairs has to judge if the proposed land use will yield a larger public utility than the existing utility. Ejido land can be expropriated in favor of only three government agencies: BANOBRAS, INDECO and CORETT. These agencies can then divide and sell the land to private or public organizations. The proceeds of the sale are handed over to the ejido assembly (which has a common fund) after deducting overhead and representation costs incurred. The ejidatario is entitled to indemnization for the expropriated land in the form of either 20% of the profits derived from the sale of land after it is developed or an amount equivalent to twice the estimated commercial value of the land before development, plus two urban lots provided the expropriated land is urbanized.

18. A strip along the coastline is in the hands of the Federal Government which can give concessions for the use of this and national land, provided the development does not restrict free entry to the beaches. The land which belongs to a municipality or city and is administered by these local authorities is called "fundo legal." The municipal authorities acquire this land by expropriation, although many "fundos" are administered as such without the appropriate legal transfer from and compensation to the ejidos that owned this land.

E. Institutional Aspects

19. There is no single entity at the federal level charged with the responsibility for developing tourism. This responsibility is in fact shared, among others, by the Secretariat of Tourism (Turismo), The National Council of Tourism and FONATUR. Each of these have some specific but many overlapping responsibilities and there is no effective coordination among them, although the law that created Turismo in 1974 entrusted it with a coordinating role of all aspects of sectoral development, including promotion and training. The new Government seems determined to strengthen Turismo so as to ensure more effective coordination. The National Council of Tourism was created in 1961 by Presidential Decree and is headed by the former president of Mexico, Miguel Aleman, and has as its principal task tourism promotion. Its budget is higher than that of Turismo (Mex\$330 million as compared to Mex\$290 million in 1976). It has a network of 15 foreign delegations and one in Acapulco, while Turismo has 19 delegations abroad and 126 in the country. The organization and tasks of FONATUR are discussed in detail in Annex VI.

20. A recently created entity, FINRURAL,^{1/} can, under the new Agricultural Credit Law of April 1976, extend credit to communities in rural areas wishing to participate in tourism ventures. FINRURAL is expected to channel its funds to communities in FONATUR promoted projects or to projects being developed by local or regional tourism fideicomisos (trust funds). FINRURAL is expected to take over all ejidos' tourism projects, of which 135 with a total planned investment of Mex\$465 million were expected to be implemented in 1976-1977. Control over tourism enterprises will then not only rest in the private sector, or with public-private ventures as Nacional Hotelera, but also with social private enterprises at the local level.

Employment and Training

21. The tourism sector employs between 300 and 400 thousand persons or about 2% of Mexico's labor force, of which some 180,000 work in hotels. The Bank of Mexico estimates that 76% of the hotel work force is employed at the lower level, 18% in administration and food preparation, and 6% in supervisory and executive functions. Most labor in hotels and restaurants, particularly at the lower level, has not received any formal vocational training, but has been trained on the job. Some large AA and A category hotels have their own formal training programs before workers are brought on the job itself. Top management positions are often filled by Mexican or expatriate staff, trained in hotel schools abroad.

22. Although the most pressing need is for trained staff at the lower and intermediate level, existing training institutions concentrate on training people for higher management and supervisory levels. Only 16% of the students are being trained for lower level jobs, 55.8% for administration and food preparation, and 28.1% for management positions. This situation is considered both by Turismo and the National Hotel Association to be the reverse of the actual needs of the sector. Tourism training is carried out by different organizations, both in the public (Social Security Institute, Secretariat of Public Education, Secretariat of Tourism), and private sectors (labor unions and universities). The number of training institutions has grown from 42 in 1973 to 80 by the end of 1976. Most of these institutions prepare students for careers for which no demand exists, and have not contributed much to the improvement of tourism services. The organization most geared to the needs of the sector is the Mexican Institute for Social Security (IMSS). It has 11 schools training staff for the lower level.^{2/} They offer 16 weeks of basic training courses for jobs such as chambermaids, assistant bar attendants, restaurant or kitchen assistants, bellboys, telephone operators, receptionists, cashiers, and elevator operators. During the first semester of 1976, 974 students graduated. It is estimated that 50 to 85% of the graduates found work in the tourism sector.

^{1/} Financiera Nacional de Industria Rural

^{2/} These centers are located in: La Paz, Merida, Acapulco, Manzanillo, Mazatlan, Cancun, Zacatecas, Villahermosa, Morelia, Mexico City, Cuernavaca.

23. IMSS intends to continue to open up new centers at a rate of three to four a year; the next two centers will be in Tijuana and Toluca. The IMSS school in La Paz offers courses for only five occupations (chambermaid, bar, kitchen and restaurant assistants and receptionists). Ninety-one percent of the school's graduates are employed in tourism (in the first semester of 1976, 66 students graduated). A new hotel training school in La Paz, which opened in January 1977, has the capacity to train 1,000 students per year, initially only for lower-level jobs. This school has the best available physical facilities in the country; it is, however, uncertain who will operate it and how operating funds will be secured. Since 1971, the Secretariat of Public Education recognizes a career at the intermediate level ("tecnico"). This training (administration of tourism business) was given in 17 places in 1976. In addition, many private institutions offer training at the intermediate level which lead to degrees which are not officially recognized. In 1976, there were 21 such institutions, offering courses for stewardesses, guides, travel agents, etc.

24. At the advanced level, a degree ("licenciado") can be obtained after four years of study at a university. In August 1976, 17 universities offered this specialization; 3 of which specialize in the area of business administration in tourism, the others in tourism planning. Eight out of seventeen have degree programs which are recognized by the Secretariat of Public Education. Approximately 700 "licenciados" graduated in 1976 and most have had difficulties finding employment in the tourism sector. Common omissions in these careers are: (a) foreign languages; (b) human relations and communication skills; and (c) practical training. Postgraduate training for tourism planning can be obtained at CICATUR--The Inter-American Center for Tourism Training.

25. The lack of practical training is a common characteristic at all levels. It is in part caused by the existing labor laws and regulations which do not permit hotels and restaurants to serve as a training ground, unless a hotel has been designated to be a hotel training school. It is also caused, however, by the orientation of curricula planners, who do not correctly read the market needs.

26. Turismo estimates that for the period 1976-1982, with an assumed construction of 19,000 new rooms per year, the demand for trained staff will be approximately 15,000 people per year. The distribution of needs is as follows: 11,600 persons per year for lower-level jobs, 2,750 for medium-level jobs in administration and food preparation, and 900 for management jobs. Clearly the present training structure cannot fulfill these demands. The new administration recognizes the need to carry out market studies to determine the quantitative and qualitative demand for trained personnel, to improve curricula and to ensure more practical training.

G. Economic Importance of Tourism

27. The major roles played by tourism are its contribution to Mexico's balance of payments and the generation of employment. In relation to the first, tourism foreign exchange earnings amounted to some US\$800 million in 1975, after having reached over US\$840 million in the previous year. This represented some 13.9% of exports of goods and services in 1974 and 13.4% in 1975, as can be seen in the following table:

Balance of Payments Brief
(in US\$ million)

	1965	1970	1973	1974	1975	Rate of Growth (in %)	
						1965- 1975	1970- 1975
(a) Exports of Goods and non-factor services	1,902	2,745	4,603	6,064	5,966	12.1	16.8
(b) of which Tourism	275	415	724	842	801	11.3	14.0
(c) Imports of Goods and non-factor services	2,192	3,417	5,237	7,764	8,518	14.5	20.0
(d) b:a (in %)	14.5	15.1	15.7	13.9	13.4		

28. Tourism is the second most important single export item after border trade, which includes revenues which could be rightly counted as tourism as shown below:

Export Detail
(in 1967-69 US\$ million)

<u>Items</u>	<u>1970</u>	<u>1975</u>
Cotton	124	174
Coffee	86	184
Cattle, Meat	122	35
Petroleum, Oil Lubricants	38	460
Tourism	415	801
Border Transactions	879	1,542
Assembly Industry	81	403
All other Goods and Non-Factor Services	<u>1,123</u>	<u>2,530</u>
Total	<u>2,868</u>	<u>6,129</u>

29. A survey undertaken in Acapulco in the early seventies shows that income per employee in tourism activities was some 50% higher than the average income, with tips representing more than 40% of wages and benefits in hotels. Although Acapulco has other industries, it is still basically a tourism-dominated town. Mexico-wide, however, earnings in tourism are probably similar to those in other modern sector activities.

30. Handicrafts is an important component, particularly with respect to the distribution of benefits from tourism. In 1975 the total sales volume of handicrafts was estimated at Mex\$1.6 billion, affecting the lives and incomes of at least 5 million Mexicans (including producers and market intermediaries and their families) in the lower 40% income segment of the population. Mexican crafts are well known for their diversity, colorfulness and quality, and they are considered and advertised as a major tourist attraction. The craft products bought as souvenirs serve as lasting symbols of a vacation spent in Mexico and therefore partly represent "Mexico" in the experience of the tourists. Understanding of the mechanisms involved in crafts production and marketing and its links to the tourism sector, merits special attention, and is further described below.

31. The producers of crafts can be divided into various categories: over half belong to Indian ethnic groups, another 30-40% are mestizos. A very small percentage can be considered craftsmen--artists, who make a living based on the fame acquired from their individual products. However, most artisans are nameless. The amount of family effort devoted to craft production depends upon the yields and income from agriculture. For most craft producers, living at the subsistence level, agricultural activities are the basic occupation. Since on the average, however, there are over 200 days per year during which a family is not working in agriculture, some communities or families have specialized in craft production. For instance, 1975 was a bad year in agriculture and 200 Huichol Indians were registered as artisans; in 1976, a better agricultural year, only 61 registered.

32. There are several institutions involved in the preservation, production and marketing of crafts at various points in the production cycle. The largest and most well-known is the National Fund for Craft Development (FONART), created in 1971. FONART's role is to rescue, conserve, diffuse and improve all expressions and objects of popular arts as well as support the producers of these arts. The Museo Nacional de Artes e Industrias Populares, a small private institution, is well known for its location and its collection of products in Mexico City, but less for its historical preservation work. Other institutions such as the National Directorate for Artisans, within the Secretariat of Industry and Commerce, INI (National Institute for Indigenous Groups), FONAFE (National Fund for Ejido Development), the Rural Credit Bank, and PIDER (Investment Program for Rural Economic Development), have craft-artisan and/or small industry development in their programs. Their activities in this field, however, do not compare to those

of FONART. FONART focuses on dissemination of information on popular arts through regular publications, a weekly T.V. program and exhibitions. Its major task, however, lies with the producers, of which 70% are Indian. The first step in its contact with producers is the organization of a "solidarity group." This group collects orders, organizes and distributes work and is eligible for credit, training and other support. Each group establishes minimum quality requirements and prices. The producers receive half of the price upon delivery of the products and the other half the next month. This payment system guarantees a certain minimum income per month; but it also gives FONART a strong grip on the artisans.

33. FONART, which is against formation of cooperatives or workshops, wanting to safeguard the individuality of each producer, provides technical assistance to the producers by teaching them to use new, better instruments, better quality primary products or new, useful forms for the same artistic expression (e.g., place mats instead of large tablecloths). Producers can also obtain credit from FONART, up to a maximum of Mex\$50,000. FONART also tries to maintain and upgrade quality of the products by the organization of contests among artisans.

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Visitor Arrivals by Means of Transportation 1960-1976
(in thousands)

	<u>1960</u>	<u>1965</u>	<u>1970</u>	<u>1971</u>	<u>1972</u>	<u>1973</u>	<u>1974*</u>	<u>1975*</u>	<u>1976*</u>
Car	339.8	654.9	1145.3	1252.5	1368.7	1311.7	1304.5	1242.1	1238.0
Plane	281.4	432.2	888.8	1009.0	1261.0	1486.6	1613.8	1560.7	1654.0
Bus	43.2	73.8	159.8	178.2	209.7	230.0	235.3	228.5	236.3
Railway	21.8	25.9	45.0	50.2	52.4	68.0	67.2	61.1	66.6
Boat	1.9	3.7	6.8	7.5	5.8	13.0	10.1	12.9	10.0
Other	2.4	8.7	4.5	12.6	14.6	129.6	131.1	112.6	123.1
Total	690.0	1200.0	2250.2	2510.0	2912.2	3238.8	3362.0	3217.9	3328.0

PERCENTAGE SHARE

	<u>1960-65</u>	<u>1965-70</u>	<u>1971</u>	<u>1972</u>	<u>1973</u>	<u>1974</u>	<u>1975</u>	<u>1976</u>
Car	52.5	49.3	49.9	47.0	40.5	38.8	38.6	37.2
Plane	36.9	41.5	40.2	43.3	45.9	48.0	48.5	49.7
Bus	5.9	6.1	7.1	7.2	7.1	7.0	7.1	7.1
Railway	2.6	2.1	2.0	1.8	2.1	2.0	1.9	2.0
Boat	1.3	0.5	0.3	0.2	0.4	0.3	0.4	0.3
Other	0.8	0.5	0.5	0.5	4.0	3.9	3.5	3.7
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

* : Preliminary figures

Note: Numbers may not add up due to rounding

Source: Dirección General de Población, SRIA. de Gobernación

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Visitors from Selected USA States to Mexico (Percentage of U.S. Visitor) 1960-76

	<u>1960</u>	<u>1965</u>	<u>1970*</u>	<u>1971*</u>	<u>1972*</u>	<u>1973*</u>	<u>1974*</u>	<u>1975*</u>	<u>1976**</u>	<u>Average Annual Growth</u>			
										<u>1960-65</u>	<u>1965-70</u>	<u>1970-75</u>	
Texas	1/	32.8	34.8	29.9	29.3	29.1	26.8	26.5	30.7	28.9	13.5	7.5	7.0
California	1/	22.6	27.3	24.9	24.7	23.7	22.3	21.3	24.0	23.3	16.5	8.7	5.6
Arizona	1/	7.6	11.8	11.2	11.0	10.0	9.0	10.0	10.3	10.4	22.5	9.5	4.7
Illinois		6.6	5.5	5.0	4.8	5.2	5.3	5.5	5.2	5.2	8.1	8.7	7.3
New York		7.6	6.8	5.0	5.0	4.8	4.9	4.7	5.2	4.9	9.8	4.2	7.1
Florida		-	-	2.2	2.4	2.5	2.8	2.9	2.2	2.4	-	-	6.0
Michigan		1.7	1.7	1.6	2.0	1.8	1.8	1.6	1.7	1.9	11.9	10.9	7.0
New Mexico	1/	1.7	1.6	1.6	1.5	1.4	1.5	1.5	1.6	1.3	10.4	10.6	6.9
Louisiana		2.0	1.9	1.3	1.3	1.4	1.2	1.3	1.3	1.5	10.9	3.2	6.0
Ohio		1.3	1.0	1.1	1.1	1.2	1.3	1.5	1.0	1.2	7.0	12.4	4.3
Other States		16.1	7.6	14.8	15.5	17.9	22.3	22.3	15.8	18.0	-	-	7.9
Officials		-	-	1.4	1.4	1.0	.8	.9	1.0	1.0	-	-	-
Total		100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	-	-	-
Total Number of U.S. Visitors (thousands)		669.0	1188.0	1981.00	2210.0	2543.0	2758.0	2861.0	2707.0	2869.0	-	-	6.4

1/ Border states

* Preliminary figures

** Estimated figures

Source: Dirección General de Estadística, S.I.C.

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Foreign Visitors to Mexico by Country of Origin
(in thousands)

	<u>1970</u>	<u>%</u>	<u>1971</u>	<u>%</u>	<u>1972</u>	<u>%</u>	<u>1973</u>	<u>%</u>	<u>1974*</u>	<u>%</u>	<u>1975*</u>	<u>%</u>	<u>1976^{1/}</u>	<u>%</u>
Africa	0.1	-	0.2	-	0.2	-	0.4	-	0.6	-	0.4	-	0.6	-
America	2192.4	97.4	2445.0	97.4	2819.4	96.8	3095.0	95.6	3214.0	95.6	3037.7	94.4	3214.3	96.6
Canada	65.9	2.9	80.1	3.2	101.2	3.5	122.1	3.8	131.1	3.9	115.8	3.6	126.5	3.8
U.S.A.	1980.9	88.0	2209.8	88.0	2543.0	87.3	2758.1	85.2	2861.0	85.1	2722.3	84.6	2868.8	86.2
Guatemala	43.3	1.9	49.8	2.0	56.6	1.9	65.4	2.0	67.2	2.0	57.9	1.8	69.9	2.1
Other Countries	102.4	4.6	105.3	4.2	118.6	4.1	149.3	4.6	154.7	4.6	141.6	4.4	149.2	4.5
Asia	6.2	0.3	6.9	0.3	11.8	0.4	16.6	0.5	13.4	0.4	12.9	0.4	20.0	0.6
Japan	4.6	0.2	5.0	0.2	9.3	0.3	13.9	0.4	10.1	0.3	9.7	0.3	16.6	0.5
Other Countries	1.6	0.1	1.8	0.1	2.6	0.1	2.7	0.1	3.4	0.1	3.2	0.1	3.3	0.1
Europe	47.2	2.1	53.0	2.1	74.8	2.6	91.7	2.7	94.1	2.8	80.4	2.5	89.9	2.7
Federal Republic of Germany	9.2	0.4	12.1	0.5	20.2	0.7	23.7	0.7	23.5	0.7	16.1	0.5	20.0	0.6
Spain	4.8	0.2	4.9	0.2	5.0	0.2	4.5	0.1	3.4	0.1	3.2	0.1	6.7	0.2
France	9.3	0.4	13.5	0.5	18.7	0.6	20.2	0.6	20.2	0.6	12.9	0.4	20.0	0.6
Holland	1.4	0.1	1.6	0.1	2.5	0.1	3.5	0.1	3.4	0.1	3.2	0.1	3.3	0.1
England	8.2	0.4	5.7	0.2	6.5	0.2	7.4	0.2	6.7	0.2	3.2	0.1	3.3	0.1
Other Countries	14.2	0.6	15.2	0.6	21.9	0.8	32.4	1.0	37.0	1.1	41.8	1.3	36.6	1.1
South Pacific	4.0	0.2	4.9	0.2	6.1	0.2	7.3	0.2	3.4	0.1	3.2	0.1	3.3	0.1
Australia	3.4	0.1	4.1	0.2	5.0	0.2	6.0	0.2	3.4	0.1	3.2	0.1	3.3	0.1
Other Countries	0.7	0.1	0.8	-	1.1	-	1.3	-	-	-	--	-	-	-
Unknown	0.3	-	0.0	-	0.0	-	30.9	1.0	36.4	1.1	83.3	2.6	-	-
TOTAL VISITORS:	2250.2	100.0	2510.0	100.0	2912.2	100.0	3241.5	100.0	3362.0	100.0	3217.9	100.0	3328.0	100.0

* : Preliminary figures

^{1/}: Estimated figures

Source: Direccion General de Estadistica, S.I.C.

ANNEX V
Table 4

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Parameters of Tourism Growth in Selected Destinations

<u>Year</u>	<u>Number of Tourists (thousands)</u>		
	<u>Puerto Vallarta (Jal.)</u>	<u>Mazatlan (Sin.)</u>	<u>Acapulco (Guer.)</u>
1968	72.2	126.7	955.2
1969	92.8	141.7	1,001.5
1970	129.4	162.0	1,061.5
1971	157.5	204.6	1,120.2
1972	196.6	247.0	1,341.3
1973	218.8	305.3	1,457.8
1974	240.9	326.1	1,551.8
- of which foreigners	102.0	164.0	737.5
- of which visitors arriving to destination on inter- national flights	46.1	96.4	387.7

Source: Documentos de la Gerencia de Planeación y Estudios Económicos,
FONATUR, Nos. 40, 41 and 44.

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Average Expenditures and Average Length of Stay of Tourists 1969-1975

(in US\$)

	<u>1969</u>	<u>1970</u>	<u>1971</u>	<u>1972</u>	<u>1973</u>	<u>1974</u>	<u>1975</u>
Total average expenditure person/trip	284.44	n.a.	n.a.	193.03	224.46	250.43	248.65
- arriving overland	215.73	n.a.	n.a.	128.76	153.49	171.38	152.21
- arriving by plane	358.83	n.a.	n.a.	287.78	313.36	343.39	368.88
Average daily expenditure	20.95	n.a.	n.a.	18.38	20.34	23.05	23.46
- arriving overland	14.48	9.80	9.94	11.95	13.10	15.38	14.34
- arriving by plane	30.97	25.10	25.87	28.75	30.70	32.61	34.71
Average length of stay (days)	13.60	n.a.	n.a.	n.a.	11.00	10.90	10.60
- arriving overland	16.10	13.30	12.80	10.80	11.70	11.10	10.60
- arriving by plane	11.60	10.60	10.50	10.00	10.20	10.50	10.60

1/ Source: Banco de Mexico, S.A. Special Survey

1972-76: Banco de Mexico, S.A. Gerencia de Investigacion Economica

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

	<u>Visitor Arrivals by Month</u> (in thousands)								
	<u>1960</u>	<u>1965</u>	<u>1970</u>	<u>1971</u>	<u>1972</u>	<u>1973*</u>	<u>1974*</u>	<u>1975*</u>	<u>1976*</u>
January	58.3	105.9	161.4	186.8	215.7	242.1	252.9	253.4	252.7
February	62.0	105.1	170.1	187.8	229.0	244.9	271.8	264.4	270.4
March	52.5	90.9	214.6	176.3	278.2	271.3	295.3	327.6	267.3
April	60.3	106.7	143.4	219.4	210.4	283.1	296.4	216.2	279.3
May	51.6	93.6	180.2	180.8	195.5	238.1	244.8	237.3	230.2
June	73.2	123.1	213.9	223.0	276.1	289.6	301.9	280.1	255.1
July	90.8	152.8	236.5	270.0	297.6	305.8	317.2	303.9	288.9
August	80.3	143.2	222.3	238.1	262.4	314.7	321.0	305.2	-
September	51.3	89.9	130.5	146.2	178.5	191.8	183.8	173.6	-
October	47.7	91.1	149.0	176.8	206.2	220.5	235.2	233.7	-
November	51.5	100.4	171.4	201.8	222.8	273.4	277.2	260.3	-
December	81.1	147.7	256.9	303.1	344.0	366.9	364.5	362.2	-
TOTAL	761.0	1350.0	2250.0	2510.0	2912.2	3242.0	3362.0	3218.0	-

* Preliminary figures

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Lodging Establishments by Type and Category

TYPE OF ACCOMMODATION

Year	Total		Hotels		Moteis		Guesthouses		Apartments		Spas	
	No. of Establishments	No. of Rooms										
1961	3,314	90,891	2,243	76,666	195	4,240	699	7,800	177	2,185	-	-
1965	3,452	96,653	1,987	75,909	371	8,205	866	10,203	228	2,336	-	-
1970	4,765	132,701	2,534	100,377	510	12,127	1,381	16,019	340	4,178	-	-
1972	5,892	163,016	3,567	128,507	653	15,228	1,239	13,053	417	5,659	16	569
1973	5,970	166,107	3,605	130,849	673	15,623	1,248	13,201	427	5,857	17	577
1974	6,159	171,551	3,759	135,581	695	16,136	1,254	13,241	434	6,016	17	577
1975	6,269	190,513	3,880	150,917	752	18,419	1,149	12,754	455	7,181	33	1,242

CATEGORY OF ACCOMMODATION

Year	Total		"AA"		A		B		C		D		E	
	No. of Establishments	No. of Rooms												
1961	3,314	90,891	121	6,267	354	14,713	419	13,278	382	10,564	942	26,541	1,096	19,528
1965	3,452	96,653	233	10,994	739	26,047	478	14,170	347	8,862	846	20,814	809	15,766
1970	4,765	132,701	398	21,008	711	23,069	714	22,392	846	23,526	1,218	27,118	878	15,588
1972	5,892	163,016	167	14,700	422	19,642	912	32,867	1,002	28,015	1,541	31,935	1,848	35,857
1973	5,970	166,107	176	15,699	437	20,489	935	33,535	1,015	28,194	1,556	32,256	1,851	35,934
1974	6,159	171,551	192	16,500	449	20,954	986	35,345	1,058	29,214	1,600	33,184	1,874	36,354
1975	6,269	190,513	169	24,484	295	18,100	977	41,245	1,203	35,626	1,474	32,840	2,151	38,218

Source: Secretaria de Turismo

December 15, 1976

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Distribution of Lodging Establishments by Type and Category
in Selected Years (Percentages)

<u>Type</u>	<u>Rooms</u>				<u>Establishments</u>			
	<u>1961</u>	<u>1965</u>	<u>1970</u>	<u>1975</u>	<u>1961</u>	<u>1965</u>	<u>1970</u>	<u>1975</u>
Hotels	84.3	78.5	75.6	79.2	67.7	57.6	53.2	61.8
Motels	4.7	8.5	9.1	9.7	5.9	10.7	10.7	11.9
Guesthouses	8.6	10.6	12.1	6.7	21.1	25.1	29.0	18.3
Apartments	2.4	2.4	3.2	3.8	5.3	6.6	7.1	7.3
Spas	-	-	-	0.7	-	-	-	0.5
<u>Category</u>								
"AA"	6.9	11.4	15.8	12.9	3.7	6.8	8.3	2.7
A	16.2	26.9	17.4	9.5	10.7	21.4	14.9	4.7
B	14.6	14.7	16.9	21.7	12.6	13.8	15.0	15.6
C	11.6	9.2	17.7	18.7	11.5	10.1	17.8	19.2
D	29.2	21.5	20.4	17.3	28.4	24.5	25.6	23.5
E	21.5	16.3	11.8	16.9	33.1	23.4	18.4	34.3

Source: Secretaria de Turismo

December 15, 1976

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Lodging Establishments per Category and Type, per Dec. 31, 1975

CATEGORY Type	<u>Establishment</u>	<u>Rooms</u>	A		B		C		D		E		TOTAL	
			E	R	E	R	E	R	E	R	E	R	E	R
Hotels	132	22,925	184	15,218	588	31,486	794	27,423	1,022	26,481	1,160	27,384	3,880	150,917
Motels	9	591	34	1,460	229	7,040	240	5,592	205	3,156	35	580	752	18,419
Guest houses	1	24	7	23	19	262	49	757	151	1,849	922	9,840	1,149	12,754
Apartments	26	857	68	1,001	130	2,000	113	1,662	92	1,308	26	353	455	7,181
Spas	1	87	2	398	11	457	7	192	4	47	8	61	33	1,242
Trailer parks	-	-	-	-	-	-	-	-	-	-	-	-	190	10,366 <u>1/</u>

1/ Refers to spaces

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

HOTEL OCCUPANCY RATES, SELECTED DESTINATIONS, BY CATEGORY

1970 - 1975

Year	<u>Mexico City</u>		<u>Acapulco</u>		<u>Puerto Vallarta</u>		<u>Mazatlan</u>		<u>La Paz</u>		<u>Tijuana</u>		<u>Ensenada</u>		1/
	<u>AA</u>	<u>A</u>	<u>I</u>	<u>II</u>	<u>I</u>	<u>II</u>	<u>I</u>	<u>II</u>	<u>I</u>	<u>II</u>	<u>I</u>	<u>II</u>	<u>I</u>	<u>II</u>	
1970	68.4	62.5	74	61	50	66	76.0	65.0	65		68.0	55.0	51.0	46.0	
1971	58.1	60.1	78	65	67	66	76.0	66.0	67		70.0	55.0	51.0	49.0	
1972	68.5	65.3	70	64	76	67	77.0	71.0	63		65.0	55.0	52.0	51.0	
1973	77.5	70.9	81	74	81	67	85.0	81.0	70		45.0	59.0	61.0	48.0	
1974	79.7	72.8	81	65	84	71	83.4	75.2	60		55.8	45.6	55.2	49.3	
1975	-	-	72	57	-	-	-	-	55		57.6	57.2	51.7	44.7	

1/ AA class is luxury hotels; A, international standard.

I combines luxury and international standard; II is good, reasonably priced hotels.

Source: Fonatur Studies

MEXICOAPPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECTFONDO NACIONAL DE FOMENTO AL TURISMO (FONATUR)A. Background and History

1. In 1969, the Federal Government authorized the Bank of Mexico to create an organization--Fondo de Promocion de Infraestructura Turistica (INFRATUR)--that would lend public sector support to the expanding tourist industry. Its purposes were: (a) the promotion and carrying out of infrastructure projects in the tourism sector; (b) encouragement of private investment to supplement the Government's infrastructure investment; (c) purchase, development, subdivision, sale and rental of real estate property; and (d) collaboration with other federal and state agencies, for the purpose of developing the tourism industry as a whole.

2. The sum of Mex\$30 million was provided initially by the Federal Government as INFRATUR's capital, which has since then increased several-fold. In support of the Government's policy to diversify geographically Mexico's tourism facilities, INFRATUR began concentrating its efforts in developing two new sites: Ixtapa-Zihuatanejo on the Pacific coast and Cancun on the Caribbean coast. In addition, INFRATUR has on a smaller scale been involved in developing an infrastructure project in Oaxaca. The status of the projects in Cancun and Ixtapa-Zihuatanejo are described in paras. 9-12.

3. In order to further support the development of the industry, the Mexican Government established FONATUR (Fondo Nacional de Fomento al Turismo) in January 1974 as a trust fund in Nacional Financiera (NAFINSA), by merging INFRATUR with the Fondo de Garantia y Fomento al Turismo (FOGATUR). FOGATUR was created as a trust fund of Nacional Financiera in 1956 to provide a flexible tourism financing instrument, especially for hotels. FOGATUR was involved in a broad range of activities, including: (a) guaranteeing credits and bonds issued by private institutions to finance tourism activities; (b) acquiring temporarily equity of enterprises engaged in tourism activities; (c) acquiring shares and bonds of private tourism enterprises; (d) rediscounting term loans of private credit institutions disbursed for tourism development; and (e) opening credit lines to private credit institutions for on-lending or granting credit directly for tourism projects. Although engaged in a wide range of activities, FOGATUR had not been very active since its inception. It was only after INFRATUR and FOGATUR were merged that the hotel credit activities increased dramatically.

4. With the merging of the two trust funds, a single government agency is now responsible for promoting and developing infrastructure and financing tourism superstructure facilities. In addition, FONATUR has acquired majority interest in a national hotel chain (Nacional Hotelera), which both owns and specializes in the management and operation of hotels in Mexico.

5. In recent months, FONATUR has been given additional and increased responsibilities in the field of tourism. Early in 1976, a new trust fund was created to tackle the problems of Acapulco and a director of FONATUR was appointed Director General of the fund. Similarly, a large tourism development project at Nueva Vallarta (near Puerto Vallarta) has been handed over to FONATUR.

B. FONATUR's Organization

6. As presently set up, FONATUR has two operating departments, the Development Department, which is responsible for infrastructure projects, and the Operations Department, which is responsible for hotel credit (Attachment 1). The present Director General and the heads of both Departments are able and highly qualified managers.

7. FONATUR's management reports to a nine-man Board comprising six government officials and three representatives of the private sector, the latter appointed by organizations representing industry, agriculture and labor (Attachment 2). The Board, which is chaired by the Secretary of Tourism, meets at least every two months and is responsible for determining FONATUR policies and approving infrastructure development projects. A Loan Committee, which meets monthly and is composed of four of the above Board members, is responsible for approving hotel and other financing.

8. FONATUR has about 195 persons directly on its payroll, and 76 persons employed on a temporary or consulting basis.

C. FONATUR's Tourism Infrastructure Operations

9. With a mandate to diversify tourism destinations in Mexico, FONATUR (then INFRATUR) selected two areas to develop after an elaborate exercise that took into account market, economic, touristic, social and other factors. These areas were Cancun, located on the coast of Yucatan and Ixtapa-Zihuatanjo on Mexico's Pacific coast. In January 1972, the Bank made a loan of US\$22 million equivalent to help finance the provision of infrastructure for Ixtapa-Zihuatanjo which had been costed at US\$44 million. Earlier, in August 1971, the Inter-American Development Bank made a loan of US\$21.5 million for similar facilities at Cancun in the Yucatan peninsula.

10. The project at Ixtapa-Zihuatanejo would in its first stage provide infrastructure that would support the development of 3,500 hotel rooms and 500 single-family houses. The project comprised three main elements. The first included the principal infrastructures: roads and streets, water and sewerage systems, electric power and telecommunications--needed to develop the resort at Ixtapa itself. The second consisted of infrastructure facilities for the town of Zihuatanejo which would develop as both a service center and a secondary tourist attraction. The third main component of the project was the construction of an international airport designed to cater for non-stop flights from major US cities. The project also made provisions for hotel training.

11. After encountering some delays due largely to land acquisition problems, the project is now nearing completion, with most of the Bank's loan expected to be disbursed by June 30, 1977. The airport has been open for over a year and is serving both Ixtapa-Zihuatanejo, as well as the rapidly expanding industrial town of Lazaro Cardenas which is an hour's drive from the airport. The physical facilities of the town of Zihuatanejo have greatly improved since the project got underway. The population has grown from 4,000 to over 10,000 and is expected to grow much faster than estimated at the time of appraisal. In the tourist zone of Ixtapa, two hotels are open for business (534 rooms) and several others are under construction. By June 1977, about 1,500 rooms are expected to be available and in 1978 FONATUR intends to begin implementation of the second stage of the project.

12. The project in Cancun was of similar proportions, with the first phase already implemented. As of September 1976, 2,300 hotel and condominium rooms were completed and several hundred more were under construction. A whole new city was developed nearby which now has a population of over 10,000. Early in 1976, IDB approved another loan of US\$20 million to finance the second stage expansion of the Cancun resort.

13. The urban development and social impact aspects of the projects are described in detail in Annex XI.

D. FONATUR's Operating Policy for Infrastructure Projects

14. With respect to FONATUR's infrastructure investments, its basic financial objective as an entity responsible for promotion and development of tourism estates is the recovery of its investments and the earning of a reasonable rate of return. This objective is being achieved by selling developed land to potential hotel and other investors. FONATUR's operating policy calls for all developed land for the sites of hotels and other superstructure to be sold, not leased, with the condition that no land be acquired for speculative purposes. A further stipulation is that the

land be used within a reasonable period of time. FONATUR's land sales arrangements are:

- (a) on a cash basis;
- (b) on a deferred payment basis; and
- (c) by providing the site as equity contribution to individual projects.

15. To attract the first investors, FONATUR is charging relatively low prices for the developed land compared to the cost of developed land at other destinations on the coast in Mexico. They range from Mex\$150 to Mex\$450 per ²m², with investors paying 15-20% down, and the rest in three to five years at 12% interest.

E. FONATUR's Hotel Credit Operations

16. Much of the hotel expansion in Mexico in recent years has been due largely to the active role played by FONATUR. Since its establishment in early 1973, FONATUR has been supplying the bulk of hotel credit by rediscounting hotel term loans of private and public financial institutions. FONATUR rediscounts 90% of the term loans and the remainder is financed by financial intermediaries. The interest spread for the intermediaries is 2-3% with the ultimate borrower paying an interest rate of 10-12% for a loan of 10-15 years and a grace period of two to three years.

17. Through its hotel development arm, FONATUR is in the unique position of being able to invest in superstructure to complement the investment in infrastructure, both through equity participation and loan financing. Although it has not developed any operating policy for its superstructure investments--as it has for its infrastructure projects, FONATUR realizes the importance of concentrating on hotel projects that are likely to provide the highest yields to the economy. It is for this reason that it is channelling some of its credits to the project areas of Cancun and Ixtapa-Zihuatanejo. As of September 30, 1976, FONATUR had financed 15 hotels (2,322 rooms) at Cancun and 4 hotels (1,069 rooms) at Ixtapa which required Mex\$540 million and Mex\$474 million, respectively, and represented 48% of the total hotel investment in Cancun and 86% in Ixtapa.

F. FONATUR's Financial Status

18. The overall financial position of FONATUR is sound with adequate net working capital generated from its operations. As FONATUR's operations have expanded since its establishment by the merger of INFRATUR and FOGATUR in 1973, the total assets increased from Mex\$0.8 billion to Mex\$5.1 billion in August 1976. The total capital employed by FONATUR amounted to Mex\$4.7 billion, of which FONATUR invested Mex\$1.8 billion in the development of infrastructure and Mex\$2.9 billion in its hotel credit operations.

19. With respect to the development of infrastructure, FONATUR investment has been confined to two selected areas, Mex\$1.1 billion in Cancun and Mex\$0.7 billion in Ixtapa-Zihuatanejo. Most of the investment funds were allocated as Government equity contribution, including government budget allocation (Mex\$1.25 billion) and loans from IBRD (Mex\$0.14 billion) and IDB (Mex\$0.17 billion). While the construction of infrastructure at each project site in the initial development stage is nearing completion, FONATUR has already been earning a significant amount of surplus in cash flow terms from sale of the land and other developed facilities, showing an increase in accumulated surplus from Mex\$37 million in 1973 to Mex\$240 million in August 1976.

20. The volume of FONATUR's hotel credit operations has expanded much faster than the volume of infrastructural development. As of August 31, 1976, FONATUR approved 378 credit applications for a total of Mex\$2.8 billion to finance about 19,000 rooms throughout the country. Of this total, Mex\$1.9 billion had been disbursed as of August 31, 1976. The source of funds for FONATUR's credit operations has been the federal budget, Banco de Mexico bond issues and retained earnings from its credit operations. As of August 31, 1976, FONATUR's resources amounted to Mex\$2.9 billion, including Mex\$1.7 billion raised by Banco de Mexico through bond issues at an interest rate of 8% for a term of 8 years, and Mex\$0.1 billion earned from its operations.

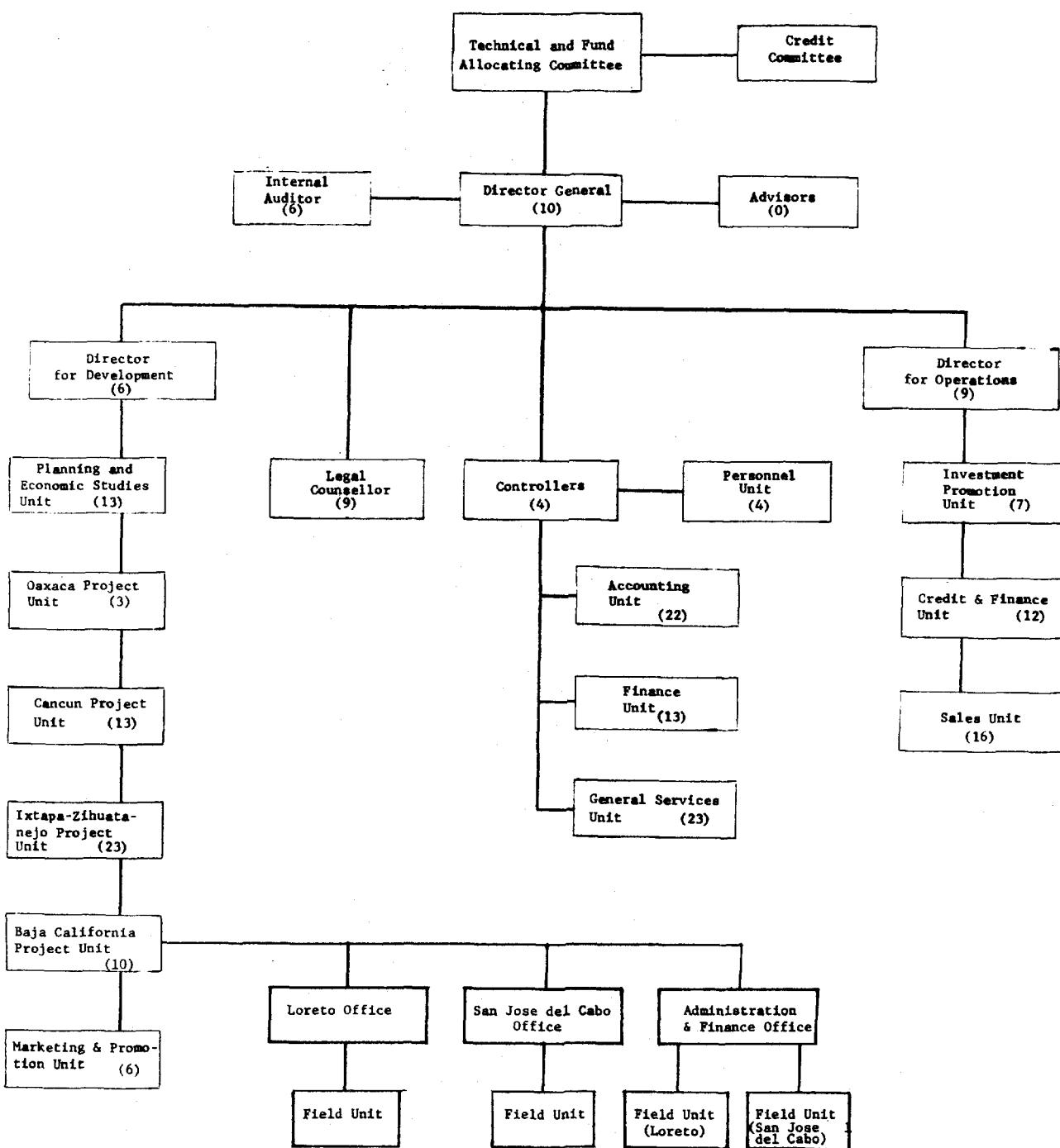
G. Prospects for the Future

21. While the Government has been providing FONATUR with full financial support for the development of infrastructure, including the payment of debt service for external funds financed by foreign institutions, e.g., IBRD and IDB, its financial support for FONATUR's hotel credit operations has been insufficient to cope with the rapid increase in the demand for hotel development in the country. FONATUR's resources appear to be too limited to support the further expansion of hotels. For 1977, FONATUR has proposed a total budget of Mex\$1.8 billion and is depending on the following sources to finance it: Government budget allocations (Mex\$500 million), bonds taken up by Banco de Mexico (Mex\$500 million) and retained earnings (Mex\$450 million). Of this total budget, Mex\$1.0 billion is allocated for the 1977 lending program and the remaining Mex\$0.8 billion to cover debt services to Banco de Mexico and operating costs. Since the lending program includes a total disbursement of Mex\$900 million for the loans already committed for in previous years, funds available for new hotels are very limited. FONATUR will also have to continue to depend upon the Federal Government for financial support if it has to continue providing tourism infrastructure, until the developments it has promoted become more mature.

22. The prospects for continued growth of tourism to Mexico are bright, particularly with the recent devaluations of the peso which is expected to accelerate an increase in vacation tourism to Mexico. Along

with the proposed project for opening up new resort areas at San Jose del Cabo and Nopol/Loreto in Baja California, FONATUR expects to continue financing hotels and other superstructure facilities. Although debt financing from other sources might be possible to finance hotel development, including foreign borrowings, suppliers' credit and domestic bond issues, it appears at least for the time being, that the Government will have to rely on FONATUR's discounting facility to encourage the interest of financial institutions and private groups in future hotel investment. In view of the current budgetary constraints and credit squeezes, however, it is not clear whether FONATUR can rely entirely on government budgetary allocations and bond issues from Banco de Mexico in order to enable it to continue to lend in any significant way.

FONATUR'S ORGANIZATION^{1/}



^{1/} Figures in parenthesis are the number of staff positions allocated to each unit.

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

MEMBERS OF THE TECHNICAL AND FUND ALLOCATING COMMITTEE
(FONATUR'S BOARD)

- (1) Secretariat of Tourism (*)
- (2) Secretariat of Programming and Budgeting
- (3) Secretariat of the Treasury and Public Credit (*)
- (4) Secretariat of National Patrimony and Industrial Development (*)
- (5) Banco de Mexico
- (6) Nacional Financiera, S.A. (*)
- (7) Confederation of the National Chambers of Commerce and Industry
- (8) Permanent National Agrarian Congress
- (9) Congress of Labor

(*) Members of the Credit Loan Committee

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

MARKET DEMAND

Present Visitor Traffic

1. Total foreign visitor arrivals to Mexico increased by an average of 10% per annum during the period of 1956-1976, reaching an estimated number of 3.33 million in 1976.^{1/} Foreign visitors'^{2/} growth has also been quite even. In no year since 1961, except 1974 and 1975, has the growth rate been less than 8.6%. Although visitor arrivals to Mexico declined by 4.3% from the 1974 peak of 3.36 million to 3.22 million in 1975, the number of foreign visitors continued to increase at a relatively fast pace during the early 1970's and showed some recovery in 1976. The decline in visitor traffic experienced in 1975 was the first since 1953 and was due to world-wide economic recession and to Mexico's uncompetitive position resulting from a strongly over valued peso.^{3/} The peso was allowed to float in September 1976.

2. Table 1 shows the growth in foreign visitor arrivals for the period 1970-1976.

Table 1. Foreign Visitor Arrivals ('000)

Country of Origin								Average Annual Growth Rate (%)	
	1970	1971	1972	1973	1974	1975	1976	70/74	70/76
US	1,980	2,210	2,540	2,760	2,860	2,720	2,870	9.7	6.4
Canada	70	80	100	120	130	120	130	16.7	10.9
Other	200	220	270	360	370	380	330	16.6	8.7
Total	2,250	2,510	2,910	3,240	3,360	3,220	3,330	10.5	6.8

1/ Mexico is a major international tourist destination, attracting in 1975 an estimated 1.4% of the total international trips and around 2.5% of the world revenues from tourism which were estimated at some US\$33 billion in 1975.

2/ Foreign visitors include Mexicans residing abroad.

3/ The visitor traffic in 1976 was also affected by the Jewish boycott and by some events that kept more tourists than normal in North America, such as the U.S. Bicentennial celebrations and the Montreal Olympics.

3. Air traffic to Mexico grew at a faster pace than the total visitor traffic, the average annual rate being 16% in 1970-74 and 11% in 1970-76. The number of foreign visitor arrivals by air accounted for 50% of the total arrivals in 1976, compared with 40% in 1970 (Table 2).

Table 2. Foreign Visitor Arrivals by Mode of Travel ('000)

	1970	(%)	1974	1975	1976	(%)	Average Annual Growth Rate (%)	
							1970/74	1970/76
By Air	889	(40)	1,610	1,561	1,655	(50)	16.1	10.9
Other	1,361	(60)	1,750	1,657	1,675	(50)	6.5	3.4
Total	2,250	(100)	3,362	3,218	3,330	(100)	10.5	6.8

4. Another important factor to assess the volume of overall tourism activities in Mexico is the average length of stay of tourists. Based on 1976 statistics, foreign visitors spent a total of 35 million nights in the country, which averaged out to a stay of 10.5 nights per visitor in that year. While statistics on the average length of stay of foreign visitors by tourist destinations in the country are not available, hotel statistics indicate that foreign visitors stay in the major tourist areas, e.g., Mexico City, Acapulco, Puerto Vallarta, etc., for some 4 nights, suggesting a typical multi-stop trip to Mexico.

5. The domestic market for tourism is also quite important in Mexico. With growing affluence of Mexico's middle class and the initiation of a five day week, this market rapidly developed to reach some 16.5 million visits to tourist destinations in 1975. Although no precise estimates were available on the size of the market in the past, its growth rate seems to have been similar to that of the number of visitors from abroad. However, since the length of stay in tourist destinations of locals is on the average some 1.9 days, the volume of local tourism represents only some 31 million guest nights. Nevertheless, local tourism represents a share of total tourism activities that is very high compared with similar countries. Mexicans make up an estimated 34-40% of guests in hotels of international class (i.e., AA and A and B) and the large majority in hotels of lower quality. Mexico's three largest cities, Mexico City, Guadalajara, and Monterrey, had 13.5 million inhabitants in 1975 which represents half of the country's urban and most of the high income population, and have been identified by FONATUR as generating most of Mexican visitors to domestic resorts. Among such inhabitants FONATUR estimates that 40 to 45% earn over Mex\$3,000 per month (US\$240) and that 7% earn over Mex\$7,000 per month (US\$560).

Future Visitor Traffic

6. Mexico benefits from its abundant touristic attractions and from its proximity to one of the largest tourist generating markets, the United States.

The number of US visitors going abroad, except to Canada, increased from 4.7 million in 1967 to 9.8 million in 1975 or at an average rate of 9.6% per year, although in 1974 and 1975 the number of such visitors declined as a result of the recession in the US (the rate of growth up to 1973 was 13.2%). Mexico's experience in the development of tourism in the past indicates that the overall size of Mexico's tourism and its growth depends heavily on the neighboring US travel market. Over 85% of all foreign visitors to Mexico come from the US and over 50% come from two states in the US--California and Texas. With the resumption of growth of the US economy, albeit at a slower rate than in the past, and with the steep devaluation of the peso in the fall of 1976^{1/}, the growth of foreign tourism to Mexico can be expected to resume although probably less dynamically than in the past.

7. FONATUR projects that foreign tourism to Mexico would grow at an annual average rate of 9% over the next 10 years. This implies that the number of foreign visitor arrivals would increase from the estimated figure of 3.3 million in 1976 to 4.7 million in 1980 and 7.2 million by 1985. While FONATUR's projections may be an attainable target based on past experience, the mission assumes an annual average rate of 6% over the same period, increasing from 3.3 million in 1976 to 4.2 million in 1980 and 5.6 million by 1985.

8. Based on the mission's assumptions on the likely growth of foreign visitors to Mexico and assuming the average length of stay of foreign visitors to remain at 10 nights, the volume of foreign tourism to Mexico would increase to 43 million tourist nights in 1980 and 56 million tourist nights by 1985. If domestic tourism in Mexico would grow at a similar rate of 6% per annum, it would add another 39 million nights in 1980 and 67 million nights in 1985. The projected traffic and volume of both foreign and domestic tourism in Mexico at 9% and 6% growth rates is summarized below:

Table 3. Visitor Projections to Mexico
(in millions)

	1976 (Estimated)	1980	1985	1990
<u>Number of Visitors</u>				
Foreigners (growth rate 9%)	3.3	4.7	7.2	11.1
Foreigners (growth rate 6%)	3.3	4.2	5.6	7.5
Mexicans (growth rate 9%)	16.5	23.3	35.8	55.1
Mexicans (growth rate 6%)	16.5	20.8	27.9	37.3
<u>Number of Visitor Nights</u>				
Foreigners (growth rate 9%)	35.0	49.4	76.0	117.0
Foreigners (growth rate 6%)	35.0	43.0	59.1	79.1
Mexicans (growth rate 9%)	31.0	43.8	67.3	103.6
Mexicans (growth rate 6%)	31.0	39.1	52.4	70.1

1/ The peso was devalued from 12.5 to around 20 to the US\$ in late August 1976 and has fluctuated in the low to mid-twenties ever since.

9. In order to further develop tourism in Mexico, the Mexican Government plans to further invest in both tourism infrastructure and touristic facilities. As part of this plan, FONATUR has been expanding existing, and opening up new destinations and is financing hotels all over the country. The expansion of touristic facilities, together with better utilization of existing capacity, are expected to be consistent with the market growth assumptions of the mission. In addition, the Government has been making determined efforts to increase direct flights from major tourist generating points in the US to Mexico that link up with various tourist destinations in the country. Given the current competitive price levels for foreign tourists resulting from the recent devaluation of the peso and Mexicans' strong interest in the development and promotion of international tourism, it is reasonable to assume that the number of foreign visitor arrivals and their staying nights projected by the mission is an attainable target. Similarly, the development of domestic tourism should continue to grow by at least 6%, since vacations abroad have become more expensive for Mexicans^{1/}, which should offset the likely slowdown in Mexicans' total tourist expenditures growth resulting from austerity measures being imposed by the Government.

10. Market targets for the Baja California project have been established on the basis of projected hotel, apartel, condominium and villa developments at Loreto and San Jose del Cabo and their likely utilization. Starting from 800 rooms to be built in 1980, the planned phasing calls for 6,150 hotel and apartel rooms and 2,330 condominium and villa rooms to be operational by 1990. Table 4 shows the buildup of accommodation capacity planned for the project areas. Roughly 70% of all visitors to the project areas are expected to be foreigners (78% in Loreto and 61% in San Jose del Cabo). Based on experience of other Mexican resorts, hotel and apartel room occupancies are projected to be 50% in the first year of operation increasing to 70% by the fifth year, with double occupancy factors of 1.8 guests per room and average lengths of stay of 4 days for foreigners and 3 for Mexicans. Condominia and villa room occupancies are projected at 50% in the first and later years, with double occupancy factors of 2.5 guests per room and average length of stay for foreigners of 6 days, and for Mexicans 10. On the basis of these estimates and assumptions, the market targets for the project areas would be 880,000 visitors (3.9 million visitor nights) in 1990. The number of visitors has been calculated under the assumption that they visit only one of the two project areas in the course of a trip to Baja California. Therefore, the target number of visitors will be less than stated above if some tourists (possibly up to a fourth, and mostly car travellers) visit both project areas. Some foreign visitors are expected to visit other parts of Mexico as well as the project areas, since multi-destination trips are typical of foreign visitors to Mexico. Table 5 shows the target visitor traffic and volume to the project areas.

1/ The expenditures of Mexican tourists abroad reached some US\$400 million in 1975 after having grown at 16.5% per year on average since 1960, and at 19% since 1970.

Table 4. Accommodation Buildup

	<u>1980</u>	<u>1985</u>	<u>1990</u>
<u>Loreto</u>			
Hotels and Apartels	400	2,600	3,000
Villas and Condominia	-	710	1,410
Total	<u>400</u>	<u>3,310</u>	<u>4,410</u>
<u>San Jose del Cabo</u>			
Hotels and Apartels	400	2,350	3,150
Villas and Condominia	-	405	920
Total	<u>400</u>	<u>2,755</u>	<u>4,070</u>

Table 5. Target Visitors and Guest Nights
in Loreto and San Jose del Cabo

<u>Visitors</u>	<u>1980/81^{1/}</u>		<u>1985/86</u>		<u>1990/91</u>	
	<u>Loreto</u> ('000)	<u>San Jose</u> ('000)	<u>Loreto</u> ('000)	<u>San Jose</u> ('000)	<u>Loreto</u> ('000)	<u>San Jose</u> ('000)
<u>Nationality:</u>						
Mexicans	6	12	69	106	100	(22.5)
Foreigners	<u>27</u>	<u>21</u>	<u>251</u>	<u>171</u>	<u>341</u>	<u>(77.5)</u>
Total	33	33	320	277	441	(100.0)
<u>Guest Nights</u>						
<u>Nationality:</u>						
Mexicans	19	37	319	410	526	(25.7)
Foreigners	108	86	1097	709	1523	<u>(74.3)</u>
Total	127	123	1416	1119	2049	(100.0)
1855	(100.0)					

1/ Since year 1 of operations begins on July 1, 1980, these periods run from mid-to-mid years rather than corresponding to calendar years.

11. The target figures for the project areas are in the range of 0.3 - 3.0% of the overall market projections for the number of guest nights spent in Mexico over the 1980-1990 period under the more conservative (6% growth) estimate made in para. 7 (the range is 0.5 - 4.0% in the case of foreign visitors and 0.2 - 2.0% in the case of Mexicans). These figures are reasonably attainable if adequate air access and promotion are provided.

12. FONATUR has undertaken market studies for the Baja California resorts that indicate that in the case of foreign tourists the project will mainly appeal to the market from the southwestern parts of the US and in particular from the state of California. They also show that these resorts will have to compete with Southern California and Hawaiian resorts in addition to other northwestern Mexican resorts. The studies further indicate that more than two-thirds of the tourists would come by air and that the majority would need first-class rather than luxury-type accommodation. In the case of Mexicans, FONATUR studies indicate that the project resorts will attract visitors from urban areas, mostly from Mexico City, Guadalajara and Monterrey, part of whom would normally travel to northwestern Mexico (in particular to Mazatlan and Puerto Vallarta) and to the southwestern parts of the US.

13. The main market segments interested in Baja California are the following:

- (a) US visitors to southern California who travel by air;
- (b) US visitors to Hawaii;
- (c) Canadian visitors to the west coast of the US who travel by air;
- (d) Car travellers from California, Nevada, Utah, and Arizona who travel more than 2,000 miles roundtrip; and
- (e) Foreign and Mexican visitors to Mexico's northern Pacific resorts, mainly to Mazatlan and Puerto Vallarta.

14. Market segment (a), southern California, which comprises the San Francisco, Los Angeles, San Diego area, is one of the most important tourist destinations in America. In 1975, southern Californian resorts received around 8.5 million visitors of which some 70% were pleasure-motivated, over 50% arrived by air, and more than 5 million originated from the state of California itself. The revenues derived from such visitors reached almost US\$2,500 million in the same year, and the growth of visitor traffic has been 4% per year on average over the 1960-1975 period.

15. Market segment (b), Hawaii, is also one of the world's major tourism destinations. In 1975, Hawaii received some 2.8 million visitors, of which about 80% came from the mainland US. Of this total 70% were

pleasure motivated and they spent US\$1,100 million. The average length of stay of visitors is similar to that of foreign visitors to Mexico, i.e., around 10 days. The growth of visitor traffic has been 16.2% per year on average over the 1960-1975 period.

16. As regards segment (c), almost 10 million Canadians travelled to the US for a stay of more than one day in 1975, of which over a quarter had the west coast as the final destination. A similar fraction travelled to the US by air. Their average length of stay was around 9 days. This segment grew at 4.4% per year on average since 1960.

17. In relation to segment (d), the states of California, Utah, Nevada and Arizona generated about 18 million pleasure motivated person trips^{1/} by car in 1972 with California accounting for almost 16 million of such person-trips.^{2/} Some 9% of the trips entailed travel distances between 1,000 and 2,000 miles roundtrip, and 17% over 2,000 miles and/or travelling abroad. In comparison to these, the roundtrip distances from the Los Angeles area to Loreto and San Jose del Cabo are some 1,850 and 2,700 miles respectively, and from Phoenix 2,200 and 3,050 miles.

18. In relation to the last segment (e), Mazatlan and Puerto Vallarta are two of Mexico's important and fastest growing resorts on the Pacific coast. Mazatlan, located just across the Gulf of California (or Sea of Cortez) from southern Baja California, received some 360,000 visitors in 1975, of which just over half were foreigners. The number of visitors grew at 16.1% per year on average since 1968 (the number of Mexican visitors grew at 14.9%, and foreign visitors at 17.4%). Puerto Vallarta, located in the state of Jalisco some 400 km south of Mazatlan, received some 280,000 visitors in 1975, of which some 40% were foreigners. The number of visitors grew at 21% per year on average since 1968 (20% in the case of Mexicans and 23% in the case of foreigners).

19. Based on econometric studies^{3/}, FONATUR projects that segment (a) of the market can expect to grow at an average of 2.2% per year, segment (b) 8.3%, segment (c) 4.4%, segment (d) 1.2% and segment (e) 9.9%. Projecting the growth of each segment with these rates, the target number of visitors to the project areas by 1990 would represent only some 1% of the potential market attributed to the segments defined above which clearly do not exhaust the market.^{4/}

1/ Only those that travel more than 200 miles roundtrip are included.

2/ Source: U.S. Census of Transportation.

3/ Population growth and personal income have been used as the main explanatory variables.

4/ The potential market is composed of travel flow segments, rather than population segments. Accordingly the travel flow segment will be larger than the population segment, since some people are likely to travel more than once in a one-year period.

20. A question arises as to whether all visitor nights spent in the project areas will be incremental to Mexico, i.e., whether the projected visitors would have come to Mexico and stay in other resorts even without the project. Since the project clearly competes with other Mexican destinations, it has been conservatively assumed that 40% of foreign visitors coming to Loreto and 60% of those coming to San Jose del Cabo and 75% of Mexican visitors coming to both resorts are diverted from other Mexican destinations inasmuch as capacity to accommodate them is available there. This question, which seriously affects the project's economic evaluation, is examined further in Annex X.

21. Given that the project meets the major criteria that draw visitors to a given area: the natural attractiveness of the tourist destination, the cost of the vacation (including the cost of transportation to the destination and the convenience of getting there) and the level of income of the tourist generating countries, the target number of visitors to the project areas--both as a proportion to total projected volume of tourism to Mexico and as a proportion of the projected potential market--are reasonably conservative. In order to compete with destinations in southern California and Hawaii, however, comparable facilities need to be provided. Room tariffs in southern California and Hawaii averaged some US\$26 and US\$30 per night in 1975 respectively. The market strategy for Baja California calls for construction of facilities of good quality (at least as good as the average quality of those in these competing destinations) to be provided to visitors at prices similar or lower than in southern California and Hawaii. The projected average hotel room tariff in the two project areas in late 1976 prices is US\$25 per night (Annex VIII).

22. The proposed project, due to its location and design, is expected to be visited by foreign visitors who travel predominantly by air. Experience at other resorts, particularly in Acapulco, has demonstrated that to attract large numbers of foreign visitors by air to Mexico requires provision of direct flights.

Whereas the airport at San Jose del Cabo is already included in the bilateral air agreement with the US and can be served by both US and Mexican airlines from Los Angeles, the Loreto airport is not but will have to be included in a bilateral agreement before the project is completed, so that direct air services can be initiated by the time the first two hotels open for business (Annex III, paras. 19-20). The flying time from Los Angeles to Loreto, for example, would be just over 1½ hours, and to San Jose del Cabo 2 hours, as compared to more than 5 hours to Hawaii. On back-to-back air charter basis, travelling to Baja California from Los Angeles would therefore cost around US\$100, as compared to almost US\$200 to Hawaii. In addition to coming by air, it is expected that about one-third of the visitors will arrive by road, using the recently completed 1700 km paved highway that connects the US border with the tip of the Baja California peninsula, and touches on both Loreto and San Jose del Cabo. New ferry services are being operated, or will soon begin operating, connecting the project areas with Guyamas, Mazatlan and Puerto Vallarta. This will further increase accessibility of the project areas for those coming by car and will also make possible visits to other parts of Mexico in the course of one trip.

23. By mid-1976 foreign visitors to Mexico spent an average of US\$24 per day, with visitors arriving by air spending more than US\$38 per day (Annex V). At present, and due to the distance of Mexico's existing resorts to the border with the US few foreign car travellers visit such resorts; they normally stay close to the border (see Annex V for the distinction of border traffic) and have low daily expenditures. Average daily expenditures in the project areas in Baja California are expected to be as follows:

	Loreto			San Jose del Cabo		
	Mexicans (25.7%) ^{1/}	Foreigners (74.3%)	All Tourists (100%)	Mexicans (39.1%)	Foreigners (60.9%)	All Tourists (100%)
US\$	25.8	39.0	35.6	2.1	42.7	37.0

1/ Proportion of total guest nights spent.

The average figures for foreign visitors to the project areas are a little more than the average for foreign air travellers to Mexico as a whole (some of whom come to visit friends and relatives and, since they do not use paid accommodation and spend little per day, do not represent typical resort visitors), but less than for foreign tourists to Mexico who stay 10 days or less in the country and spent over US\$45 per day in 1975, for those who come on charter groups (US\$60 in 1976), and for those visiting destinations such as Cancun and Ixtapa (US\$48). As a reflection of the erosion of Mexican's purchasing power in dollar terms after devaluation, the projected expenditures of Mexican tourists are also lower than recent experience in Mexican resorts indicates (over US\$45 per day in Cancun in mid-1976). The projected level of expenditures takes into account the higher than normal expenditures (in dollar terms) in mid-1976 due to the overvalued peso. Overall, the expenditure projections are therefore reasonably conservative and consistent with the facilities offered.

24. Based on experience in Cancun, the breakdown of projected average expenditures of foreign visitors is calculated to be as follows:

<u>Items</u>	<u>Percentage</u>
Accommodation, food and beverages	58
Entertainment	14
Local transportation (including guides)	11
Shopping	12
Other (including tips)	5
Total	100

The expenditure breakdown of Mexican visitors is likely to be slightly different. Domestic visitors are expected to spend a higher proportion on accommodation and less on local transportation and shopping.

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

DEVELOPMENT OF ACCOMMODATION FACILITIES

1. The project calls for a gradual buildup of accommodation capacity at the two sites over the 1980-1987 period with 6,150 rooms to be completed by 1987: 3,150 rooms at San Jose del Cabo and 3,000 rooms at Loreto. Most accommodation at the two sites will be of two types, hotels and apartels (apartment hotel), and will be of three categories as described below:

HOTEL DEVELOPMENT
(Number of Rooms)

Year	San Jose del Cabo			Loreto		
	Hotel	Apartel	Total	Hotel	Apartel	Total
1980	250	150	400	250	150	400
1981	100	200	300	100	400	500
1982	100	200	300	100	300	400
1983	100	300	400	150	250	400
1984	150	300	450	100	500	600
1985	200	300	500	100	200	300
1986	100	300	400	100	100	200
1987	100	300	400	100	100	200
Total	1,100	2,050	3,150	1,000	2,000	3,000

Categories:

AA	165	310	475	150	300	450
A	770	1,430	2,200	700	1,400	2,100
B	165	310	475	150	300	450
	1,100	2,050	3,150	1,000	2,000	3,000

2. The major difference between hotel and apartel is characterized by the type of ownership and operation. While hotels are owned as a unit, normally by groups or companies, apartels generally are owned by numerous individuals who buy the units from developers. The operation of apartels is quite similar to that of hotels in terms of earnings from room rent and

other services, with the exception of the following concepts:

- (a) individual owners of apartels have the right to use the units (or rooms) once a year for a limited period of time (e.g., 25 days). During the rest of the year the units (or rooms) are to be made available for rental purposes;
- (b) profits generated from renting rooms and providing other services to tourists are to be shared by individual owners, in accordance with conditions stipulated in the agreements between the developers or managers of the units and individual owners; and
- (c) although apartel rooms are rented out in the same way as hotels and usually for similar prices, they generally have simple cooking facilities designed to serve "the self-catering" tourist. These tourists spend less on food and beverages than the typical hotel guest.

3. Past experience in Mexico has shown that there are two types of apartels; one which is developed along the lines of a pure hotel in terms of design and operation; and the other which is developed as a mixture of hotel and apartment complex (i.e., the hotel and apartment buildings are attached to each other in the same complex). It is projected that the development of apartels in project areas will be of the latter type, with the apartments managed the same way as hotel rooms.

Projections

4. In order to test the financial viability of hotels and apartels projected for the two areas, separate operating projections have been made for a typical 250-room hotel and a 250-room apartel. These models are of the "A category" type and projections are based on experience of comparable facilities in Mexico. (These projections are valid also for the proposed first hotels to be financed under the project.) A summary of these projections are shown in Tables 1 to 6 of this Annex, and show that the apartel is financially more attractive than the hotel, due largely to lower operating and capital costs. An added attractive financial feature for promotion of apartels is that they do not have to depend on one or two sources for equity, but can distribute the risk among several hundred individual owners. Furthermore, apartel developers are in a position to raise capital by selling the units to individual investors in advance. In view of the above, it is expected that the demand of potential promoters, developers and investors for such apartel development would increase in the future, and is therefore reflected in the proposed development plan for the project. The projections for the model hotel and apartel have been

based on the following assumptions:

Revenue Assumptions

5. The following assumptions on room sales have been used for both the hotel and apartel projections assuming that the apartel room rates will be the same as hotel room rates and that both would experience a similar level of occupancy. On the other hand, different assumptions on food and beverage sales have been used for the apartel projections assuming that many of the guests staying in these facilities will not use the restaurant and bar facilities as in the case of hotels.

6. Occupancy has been calculated on an annual per room basis, taking into account seasonality of operations. It is estimated that average occupancy rates would be at 50% in the first year of operation, increasing to 70% in the fifth year of operation. Since the hotels and apartels in the project area will be moderately priced and are geared more toward economy-class tourists, it would be reasonable to expect a 90% occupancy rate for the high season months (mid-November to mid-May) and 50% for the remaining months, averaging out to an annual occupancy rate of 70% in a typical year of operation. Double occupancy has been estimated at 1.8 guests per room.

7. The following assumptions on room rates are in late 1976 prices and based on the net receipts for hotels after deduction of the 4% sales tax on room rates and commissions to tour operators.

<u>Hotels/Apartels</u>	<u>Room Rates for Double Occupancy (in US\$)</u>		
	<u>Seasonal Room Rate</u>		<u>Annual Average</u>
	<u>High</u>	<u>Low</u>	
AA Category	33	24.50	30
A Category	28	19.50	25
B Category	23	14.50	20

The average high-season rates for A category hotels during the six-month period when occupancies are 90% would be US\$28 and the low-season rates for the remaining period when occupancies are 50% would be US\$19.50 for a weighted annual average room rate of US\$25.

8. Other sales, including food and beverage sales, have been calculated on the basis of room sales. For apartel food and beverage sales projections, it has been assumed that the 250-room apartels would consist of 125 rooms of the hotel type and that 125 rooms would be in apartments (comparable to some extent to suites in a hotel) and that only 20% of the guests staying in the apartments would use the restaurant and bar facilities in the complex. In other words, the apartels' revenues from food and beverage sales would amount to 60% of revenues of a typical hotel. The following table summarizes

departmental sales ratios used for the projections:

<u>Departmental Sales</u>	<u>Ratios to Total Sales</u>	
	<u>Hotel</u> (%)	<u>Apartel</u> (%)
Room	50	62
Food	34	25
Beverage	14	11
Other	<u>2</u>	<u>2</u>
Total	100	100

Operating Cost Assumptions

9. Cost of sales were based on ratios to departmental sales in the case of both the hotel and apartel operations. The cost ratios were estimated at 35% for food costs, 27% for beverage costs and 50% for other costs (gift shop, telephone, laundry, etc.).

10. Payroll and related benefit expenses were calculated from staffing tables for hotels based on average wages and related expenses experienced by comparable hotels in the country, adjusted to reflect the differences in the types of facilities. The monthly average wage was estimated at US\$150 per employee. In addition, fringe benefits were calculated at 30% of the average wage, for a total monthly average payroll of US\$195 per employee. The average number of employees was estimated at 1.2 per room for the hotel and 0.8 per room for apartel operations. The estimated payroll costs were assumed to be fixed for the operating projections.

11. Other departmental costs which include expenses for guest supplies, replacement of linen, china and glassware, etc., were also based on ratios to departmental sales: 8% on room sales and 15% on food and beverage sales.

12. Undistributed expenses include the costs of administration, promotion, utility and maintenance. These costs were calculated based on ratios to total sales experienced by comparable hotels in Mexico at an occupancy level of 60% and have been assumed to be fixed for the projections, with the exception of the utility costs which are assumed will vary with occupancy.

13. Management fees are assumed to be a combination of the basic and the incentive rates: the basic fee would be 3% of the total sales, and the incentive fee would be 10% of the gross operating profits after deducting basic management fees. When combined, the total management fee would be 7% of total sales. In the analysis of the profitability of the "model" or typical hotel and apartel operations, the projections have been made for two alternatives; the one with management fees, and the other without management fees, assuming that some of the hotels would be operated by owning companies as is increasingly becoming the trend in Mexico.

Capital Cost Assumptions

14. The investment cost of the 250-room hotel in 1976 prices, including the cost of land, interest during construction, and working capital, has been estimated at US\$6.73 million (or US\$26,950 per room). (Annex I) The investment cost of a typical 250-room apartel is estimated at US\$5.40 million (or US\$21,600 per room). The financing plan for hotels and apartels are assumed to be as follows:

	<u>Hotel</u>	<u>(%)</u>	<u>Apartel</u>	<u>(%)</u>
Equity	2.50	(37)	2.00	(37)
Long-term Loans	<u>4.09</u>	<u>(61)</u>	<u>3.30</u>	<u>(61)</u>
Subtotal	6.59	(98)	5.30	(98)
Working Capital	<u>.14</u>	<u>(2)</u>	<u>.10</u>	<u>(2)</u>
Total Capital	6.73	(100)	5.40	(100)

15. Long-term loans are assumed to carry an interest rate of 12% for 15 years, including a 3-year grace period. The working capital is assumed to be financed on a short-term basis with an interest rate of 16% for periods of less than one year. For the purpose of financial analysis, interest rates have been adjusted in real terms, with a 5% interest rate indexed for inflation on the long-term loans and 6% on the short-term loans. Based on a straight line depreciation, the building has been depreciated over 30 years and furnishing, fixtures and equipment over 10 years. Deferred expenses and interest during construction have been amortized for 5 years. Income tax has been calculated at 40% of taxable income from the first year of operation.

16. The results of operating projections for the hotel and apartel are presented in Tables 1 to 6 of this Annex, and include income statements, cash flow statements and balance sheets.

17. Based on the above assumptions, the financial projections indicate that the hotel would be financially viable and have a satisfactory financial rate of return. Despite low rates of return in the early years of operation, the hotel would be able to achieve a rate of return on initial equity capital investment of 12% in the sixth year of operation, increasing to 14% in the tenth year of operation. The projected sources and application of funds show that the hotel would be able to generate sufficient operating income to meet its financial obligations, including debt service, management fees and reserves to cover replacement costs. Debt service coverage is low in the first year of operation; however, it is compensated by the input of equity in this year. Thereafter, the hotel would be able to service debt satisfactorily. The projected balance sheet indicates that the hotel's

financial position would be sound. It is reasonable to expect that dividends can be paid from the sixth year of operation. Even with payments of dividends at 10% of the paid-in share capital from the sixth year of operation onward, its financial position would continue to remain satisfactory.

18. As to the operations of the apartels, experience shows that apartels are much more profitable than hotels due to the following factors: while the units (or rooms) of apartels can be rented out to tourists at similar room rates as hotels, and catering services provided in the complex at similar prices as hotels, the operating and capital costs are (comparatively) lower than the costs of hotels. The operating projections of an apartel show that it would generate a relatively high rate of return on initial equity capital investment of 11% in the fourth year of operation, increasing to 17% in the sixth year of operation. The profits generated will be shared by the individual owners, in accordance with conditions agreed upon between the developers and individual owners. Although such profit sharing is not projected in the financial forecasts, the financial analysis indicates that the apartel would be able to pay out dividends at 10% of the paid-in share capital from the fifth year of operation. After its financial obligations are met, including debt service, management fees, as well as reserves to cover replacement costs and payments of dividends, the apartel's financial position would continue to be sound.

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Pro-forma Income and Expense Statement
(For 250-Room Resort Hotel)

<u>Fiscal Year</u> <u>Operating Year</u>	<u>80/81</u> <u>1</u>	<u>81/82</u> <u>2</u>	<u>82/83</u> <u>3</u>	<u>83/84</u> <u>4</u>	<u>84/85</u> <u>5</u>	<u>85/86</u> <u>6</u>	<u>86/87</u> <u>7</u>	<u>87/88</u> <u>8</u>	<u>88/89</u> <u>9</u>	<u>89/90</u> <u>10</u>
Room Occupancy (%)	50	55	60	65	70	70	70	70	70	70
<u>Sales:</u>										
Room	1.14	1.25	1.37	1.48	1.59	1.59	1.59	1.59	1.59	1.59
Food	.78	.85	.93	1.01	1.09	1.09	1.09	1.09	1.09	1.09
Beverage	.32	.35	.38	.42	.45	.45	.45	.45	.45	.45
Other	.04	.06	.06	.06	.06	.06	.06	.06	.06	.06
Total Sales	2.28	2.51	2.74	2.97	3.19	3.19	3.19	3.19	3.19	3.19
<u>Cost Expenses:</u>										
Cost of Sales										
Food	.27	.30	.33	.35	.38	.38	.38	.38	.38	.38
Beverage	.09	.09	.10	.11	.12	.12	.12	.12	.12	.12
Other	.02	.03	.03	.03	.03	.03	.03	.03	.03	.03
Subtotal	.38	.42	.46	.49	.53	.53	.53	.53	.53	.53
Payroll	.70	.70	.70	.70	.70	.70	.70	.70	.70	.70
Other Departmental Expenses	.27	.30	.33	.36	.38	.38	.38	.38	.38	.38
Total cost and Expenses	1.35	1.42	1.49	1.55	1.61	1.61	1.61	1.61	1.61	1.61
<u>Gross Income :</u>	.93	1.09	1.25	1.42	1.58	1.58	1.58	1.58	1.58	1.58
Less										
<u>Undistributed Expenses :</u>										
Administration	.14	.14	.14	.14	.14	.14	.14	.14	.14	.14
Promotion	.08	.08	.08	.08	.08	.08	.08	.08	.08	.08
Heat, light, power	.09	.10	.11	.12	.13	.13	.13	.13	.13	.13
Maintenance	.02	.04	.08	.08	.08	.08	.08	.08	.08	.08
Total Expenses	.39	.36	.41	.42	.43	.43	.43	.43	.43	.43
<u>House Profit:</u>	.60	.73	.84	1.00	1.15	1.15	1.15	1.15	1.15	1.15
Less: Management Fees	(.13)	(.15)	(.16)	(.19)	(.21)	(.21)	(.21)	(.21)	(.21)	(.21)
<u>Gross Operating Profit:</u>	.47	.58	.68	.81	.94	.94	.94	.94	.94	.94
Less:										
<u>Capital Expenses</u>										
Depreciation	.28	.28	.28	.28	.28	.28	.28	.28	.28	.28
Amortization	.12	.12	.12	.12	.10	-	-	-	-	-
Interest	.21	.20	.19	.18	.16	.15	.13	.12	.10	.08
Subtotal	.61	.60	.59	.58	.54	.43	.41	.40	.38	.36
<u>Profit(or Loss) Before Tax:</u>	(.14)	(.02)	.09	.23	.40	.51	.53	.54	.56	.58
Income Tax	-	-	.04	.09	.16	.20	.21	.22	.22	.23
<u>Net Profit:</u>										
Cumulative Net Profit	(.14)	(.02)	.05	.14	.24	.31	.32	.32	.34	.35
Return on Net Fixed Assets	1.1	3.1	4.5	6.4	8.7	10.6	11.1	11.7	12.6	13.4
Return on Initial Equity	-	-	2.0	5.5	9.6	12.4	12.8	12.8	13.6	14.0

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Pro-Forma Balance Sheet
For 250-Room Resort Hotel

Fiscal Year Operating Year	78/79	79/80	80/81 1	81/82 2	82/83 3	83/84 4	84/85 5	85/86 6	86/87 7	87/88 8	88/89 9	89/90 10
Assets:												
Net working capital	-	-	.40	.38	.56	.82	1.14	1.42	1.69	1.95	2.21	2.46
Fixed Assets												
Land	.45	.45	.45	.45	.45	.45	.45	.45	.45	.45	.45	.45
in working-process	1.84	5.12	-	-	-	-	-	-	-	-	-	-
in operation	-	-	5.56	5.56	5.56	5.56	5.56	5.56	5.56	5.56	5.56	5.56
Less depreciation	-	-	(.28)	(.56)	(.84)	(1.12)	(1.40)	(1.68)	(1.96)	(2.24)	(2.52)	(2.80)
Net fixed assets	2.29	5.57	5.73	5.45	5.17	4.89	4.61	4.33	4.05	3.77	3.49	3.21
Other assets	.07	.24	.46	.34	.22	.10	-	-	-	-	-	-
Total net assets	2.36	5.81	6.59	6.17	5.95	5.81	5.75	5.75	5.74	5.72	5.70	5.67
Liabilities:												
Less: Short-term loans	-	-	.14	-	-	-	-	-	-	-	-	-
Long-term loans	1.39	3.55	4.09	3.83	3.56	3.28	2.98	2.67	2.34	2.00	1.64	1.26
Total liabilities	1.39	3.55	4.23	3.83	3.56	3.28	2.98	2.67	2.34	2.00	1.64	1.26
Equity:												
Paid in share capital	.97	2.26	2.36	2.34	2.39	2.53	2.77	3.08	3.40	3.72	4.06	4.41
Retained earnings	.97	2.26	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50	2.50
Debt/Equity Ratio	59:41	61:39	64:36	62:38	60:40	56:44	52:48	46:54	41:59	35:65	29:71	22:78

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Pro-forma Cash Flow Statement
For 250-Room Resort Hotel

<u>Fiscal Year</u> <u>Operating Year</u>	<u>78/79</u>	<u>79/80</u>	<u>80/81</u>	<u>81/82</u>	<u>82/83</u>	<u>83/84</u>	<u>84/85</u>	<u>85/86</u>	<u>86/87</u>	<u>87/88</u>	<u>88/89</u>	<u>89/90</u>
<u>Source of Funds</u>												
Net Operating income	-	-	(.14)	(.02)	.05	.14	.24	.31	.32	.32	.34	.35
Non-cash changes	-	-	.40	.40	.40	.38	.38	.28	.28	.28	.28	.28
Internal cash generation	-	-	.26	.38	.45	.54	.62	.59	.60	.60	.62	.63
Initial Equity Capital	.97	1.29	.24	-	-	-	-	-	-	-	-	-
Long-term loans	1.39	2.16	.54	-	-	-	-	-	-	-	-	-
Short-term Loans	-	-	.14	-	-	-	-	-	-	-	-	-
Subtotal	2.36	3.45	.92	-	-	-	-	-	-	-	-	-
Total Funds	2.36	3.45	1.18	.38	.45	.54	.62	.59	.60	.60	.62	.63
<u>Application of Funds</u>												
Land	.45	-	-	-	-	-	-	-	-	-	-	-
Project Cost	1.84	3.28	.68	-	-	-	-	-	-	-	-	-
Subtotal	2.29	3.28	.68	-	-	-	-	-	-	-	-	-
Interest during construction	.07	.17	.10	-	-	-	-	-	-	-	-	-
Loan Amortization	-	-	-	.40	.27	.28	.30	.31	.33	.34	.36	.38
Total Applications	2.36	3.45	.78	.40	.27	.28	.30	.31	.33	.34	.36	.38
Annual Surplus	-	-	.40	(.02)	.18	.26	.32	.28	.27	.26	.26	.25
Cumulative Surplus	-	-	.40	.38	.56	.82	1.14	1.42	1.69	1.95	2.21	2.46
Cash generation	-	-	.47	.58	.64	.72	.78	.74	.73	.72	.72	.71
Debt service	-	-	.61	.46	.46	.46	.46	.46	.46	.46	.46	.46
Debt service ratio	-	-	.7	1.3	1.4	1.6	1.7	1.6	1.6	1.6	1.6	1.6

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Pro-forma Income and Expense Statement
For 250-Room Apartment Hotel

Fiscal Year Operating Year	80/81 1	81/82 2	82/83 3	83/84 4	84/85 5	85/86 6	86/87 7	87/88 8	88/89 9	89/90 10
Room Occupancy (%)	50	55	60	65	70	70	70	70	70	70
(in Us Million Dollars)										
<u>Sales:</u>										
Room	1.14	1.25	1.37	1.48	1.59	1.59	1.59	1.59	1.59	1.59
Food	.47	.51	.56	.61	.65	.65	.65	.65	.65	.65
Beverage	.19	.21	.23	.25	.27	.27	.27	.27	.27	.27
Other	.04	.06	.06	.06	.06	.06	.06	.06	.06	.06
Total Sales	1.84	2.03	2.22	2.40	2.57	2.57	2.57	2.57	2.57	2.57
<u>Cost Expense:</u>										
Cost of Sales										
Food	.16	.18	.20	.21	.23	.23	.23	.23	.23	.23
Beverage	.05	.06	.06	.07	.07	.07	.07	.07	.07	.07
Other	.02	.03	.03	.03	.03	.03	.03	.03	.03	.03
Subtotal	.23	.27	.29	.31	.33	.33	.33	.33	.33	.33
Payroll	.47	.47	.47	.47	.47	.47	.47	.47	.47	.47
Other Departmental Expenses	.22	.24	.27	.29	.31	.31	.31	.31	.31	.31
Total Cost and Expenses	.92	.98	1.03	1.07	1.11	1.11	1.11	1.11	1.11	1.11
<u>GROSS INCOME</u>	.92	1.05	1.19	1.33	1.46	1.46	1.46	1.46	1.46	1.46
Less										
<u>Undistributed Expenses</u>										
Administration	.11	.11	.11	.11	.11	.11	.11	.11	.11	.11
Promotion	.07	.07	.07	.07	.07	.07	.07	.07	.07	.07
Heat, Light, Power	.07	.08	.09	.10	.10	.10	.10	.10	.10	.10
Maintenance	.02	.04	.07	.07	.07	.07	.07	.07	.07	.07
Total Expenses	.27	.30	.34	.35	.35	.35	.35	.35	.35	.35
<u>HOUSE PROFIT</u>	.65	.75	.85	.98	1.11	1.11	1.11	1.11	1.11	1.11
Less Management Fees	(.12)	(.14)	(.15)	(.17)	(.19)	(.19)	(.19)	(.19)	(.19)	(.19)
<u>GROSS OPERATING PROFIT</u>	.53	.61	.70	.81	.92	.92	.92	.92	.92	.92
Less										
<u>Capital Expenses</u>										
Depreciation	.24	.24	.24	.24	.24	.24	.24	.24	.24	.24
Amortization	.09	.09	.09	.09	.10	-	-	-	-	-
Interest	.17	.15	.14	.13	.12	.11	.09	.08	.07	.05
Subtotal	.50	.48	.47	.46	.46	.35	.33	.32	.31	.29
<u>PROFIT OR LOSS BEFORE TAX</u>	.03	.13	.23	.35	.46	.57	.59	.60	.61	.62
Income Tax	.01	.05	.09	.14	.18	.23	.24	.24	.24	.25
<u>NET PROFIT</u>	.02	.08	.14	.21	.28	.34	.35	.36	.37	.37
Cumulative Net Profit	.02	.10	.24	.45	.73	1.07	1.42	1.78	2.15	2.52
Return on Net Fixed Assets	4.1	5.3	6.8	8.8	11.0	13.2	13.9	15.1	16.4	17.2
Return on Initial Equity	1.0	4.0	7.0	10.5	14.0	17.0	17.5	18.0	18.5	18.5

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Pro-forma Balance Sheet
For 250-Room Apartment Hotel

<u>Fiscal Year</u> <u>Operating Year</u>	<u>78/79</u>	<u>79/80</u>	<u>80/81</u> <u>1</u>	<u>81/82</u> <u>2</u>	<u>82/83</u> <u>3</u>	<u>83/84</u> <u>4</u>	<u>84/85</u> <u>5</u>	<u>85/86</u> <u>6</u>	<u>86/87</u> <u>7</u>	<u>87/88</u> <u>8</u>	<u>88/89</u> <u>9</u>	<u>89/90</u> <u>10</u>
Assets:												
Net Working Capital	-	-	.45	.55	.80	1.11	1.49	1.82	2.15	2.47	2.79	3.10
Fixed Assets												
Land	.45	.45	.45	.45	.45	.45	.45	.45	.45	.45	.45	.45
In working Process	1.45	4.04	-	-	-	-	-	-	-	-	-	-
In Operation	-	-	4.39	4.39	4.39	4.39	4.39	4.39	4.39	4.39	4.39	4.39
Less Depreciation	-	-	(.24)	(.48)	(.72)	(.96)	(1.20)	(1.44)	(1.68)	(1.92)	(2.16)	(2.40)
Net fixed assets	1.90	4.49	4.60	4.36	4.12	3.88	3.64	3.40	3.16	2.92	2.68	2.44
Other Assets	.05	.19	.37	.28	.19	.10	-	-	-	-	-	-
Total Net Assets	1.95	4.68	5.42	5.19	5.11	5.09	5.13	5.22	5.31	5.39	5.47	5.54
Liabilities:												
Less Short-term Loans	-	-	.10	-	-	-	-	-	-	-	-	-
Long-term Loans	1.12	2.86	3.30	3.09	2.87	2.64	2.40	2.15	1.89	1.61	1.32	1.02
Total Liabilities	1.12	2.86	3.40	3.09	2.87	2.64	2.40	2.15	1.89	1.61	1.32	1.02
Equity:												
Paid-in share capital	-.83	1.82	2.02	2.10	2.24	2.45	2.73	3.07	3.42	3.78	4.15	4.52
Retained earnings	-.83	1.82	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
Debt/Equity Ratio:	57:43	61:39	62:38	60:40	56:44	52:48	47:53	41:59	36:64	30:70	24:76	18:82

MEXICO: BAJA CALIFORNIA TOURISM PROJECT

Pro-forma Cash Flow Statement
For 250-Room Apartment Hotel

<u>Fiscal Year</u> <u>Operating Year</u>	78/79	79/80	80/81 1	81/82 2	82/83 3	83/84 4	84/85 5	85/86 6	86/87 7	87/88 8	88/89 9	89/90 10
<u>Source of Funds</u>												
Net Operating Income	-	-	.02	.08	.14	.21	.28	.34	.35	.36	.37	.37
Non-Cash Charges	-	-	.33	.33	.33	.33	.34	.24	.24	.24	.24	.24
Internal Cash-Generation	-	-	.35	.41	.47	.54	.62	.58	.59	.60	.61	.61
Initial Equity Capital	.83	.99	.18	-	-	-	-	-	-	-	-	-
Long-term Loans	1.12	1.74	.44	-	-	-	-	-	-	-	-	-
Short-term Loans	-	-	.10	-	-	-	-	-	-	-	-	-
Subtotal	1.95	2.73	.72	-	-	-	-	-	-	-	-	-
Total Funds	1.95	2.73	1.07	.41	.47	.54	.62	.58	.59	.60	.61	.61
<u>Application of Funds</u>												
Land	.45	-	-	-	-	-	-	-	-	-	-	-
Project Cost	1.45	2.59	.54	-	-	-	-	-	-	-	-	-
Subtotal	1.90	2.59	.54	-	-	-	-	-	-	-	-	-
Interest during construction	.05	.14	.08	-	-	-	-	-	-	-	-	-
Loan Amortization	-	-	-	.31	.22	.23	.24	.25	.26	.28	.29	.30
Total Application	1.95	2.73	.62	.31	.22	.23	.24	.25	.26	.28	.29	.30
<u>Annual Surplus</u>												
Cumulative Surplus	-	-	.45	.10	.25	.31	.38	.33	.33	.32	.32	.31
Cash Generation	-	-	.52	.56	.61	.67	.74	.69	.68	.68	.68	.66
Debt Service	-	-	-	.48	.37	.37	.37	.37	.37	.37	.37	.37
Debt Service Ratio	-	-	-	1.2	1.6	1.8	2.0	1.9	1.8	1.8	1.8	1.8

MEXICOAPPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECTFINANCIAL FORECASTS ON ESTATE OPERATIONS

1. This annex deals with overall investments in the two project areas, except investments in the airports and the first hotels, which are dealt with in Annex III and VIII. These investments directly affect the land being developed for sale to hotel, apartel, commercial and other investors. FONATUR would administer the two tourism zones by maintaining the public areas and facilities within these areas (e.g., landscaping, buildings, environmental sanitation and stormwater drainage) and by selling the hotel and other commercial sites to private investors. FONATUR would also be responsible for development of the urban areas by providing required infrastructure and common facilities for redensifying existing commercial and residential sites in the towns and for selling lots to the local population.
2. Two new project units would be set up by FONATUR to be staffed with qualified and experienced staff that would deal with property management, planning, engineering, accounting and finance (Annex VI). The project units would have a small technical services unit, although FONATUR would rely on maintenance services being provided by other government and public agencies. The management services to be provided by FONATUR would primarily involve land sales and building management. The administrative services would primarily involve accounting, procurement and distribution.
3. The municipal government would provide maintenance services for roads, bridges, solid waste disposal, and stormwater drainage. A local junta would manage and maintain water supply and sewerage systems. Electrical installations would be maintained by CFE, while TELMEX would maintain the telecommunications installations. The technical services unit within the Project Unit of FONATUR would be responsible for assuring the overall quality of maintenance and repair services, and would plan their activities in close coordination with the government and public agencies involved in the project.
4. The total capital requirements for the development of the tourism estates are estimated to be US\$4.09 million in 1976 prices, including financial charges during construction. These costs exclude investments in the airports, the pilot hotels, the telecommunications system, and part of the investments in electric power, water supply and sewerage components (see Annexes III and VIII). The following table is a summary of costs and capital structure for the developments at Loreto and San Jose del Cabo (FONATUR's estate operations).

Requirements

(US\$ million)

	Loreto			San Jose del Cabo		
	<u>Resort</u>	<u>Town</u>	<u>Total</u>	<u>Resort</u>	<u>Town</u>	<u>Total</u>
Land	3.52	.85	4.37	2.01	6.38	(19)
Project Cost	6.56	6.50	13.06	8.16	21.22	(64)
Indirect Cost	2.27	1.16	3.43	2.30	5.73	(17)
Subtotal	12.35	8.51	20.86	12.47	33.33	(100)
Interest during Construction			.50	.26	.76	
Total			21.36	12.73	34.09	

Source of Funds

IBRD Loans	9.18	5.24	14.42	(42)
Government Equity	11.68	7.23	18.91	(55)
Operating Income	.50	.26	.76	(3)
Total	21.36	12.73	34.09	(100)

5. For purposes of financial analysis, it is assumed that the Bank loan would be on-lent to FONATUR at an interest rate of 9% per annum for 18 years, including a 3-year grace period. This interest rate has been adjusted to 2% interest indexed for inflation. Repayments of the IBRD loan are assumed to start in 1981. The financial charges on the IBRD loans during the grace period are assumed to be covered by operating income.

6. Forecasts of income and expense, cash flow and financial position for the first ten-year period of FONATUR's estate operations at Loreto and San Jose del Cabo are presented in Tables 1-6 of this annex. The basic assumptions used in these projections are summarized below.

7. FONATUR would generate revenues from the sale of hotel, commercial and residential sites in the tourism areas amounting to 66 ha at Loreto and 54 ha at San Jose del Cabo. In addition, FONATUR would generate revenues from the redensification and sale of commercial and residential sites in the towns of Loreto and San Jose del Cabo amounting to 77 has. It is expected that FONATUR would sell all the sites developed under the project to private investors over a ten-year period starting from 1978. The land sale prices for sites vary by type of development and the year the sales contract is signed. It is estimated that the average sale price would be in the range of US\$20-28 per m² for hotel sites, US\$25-35 per m² for villas and condominium sites and US\$30 per m² for other commercial sites. The average sales price for urban residential lots has been projected at US\$10-12 per m², and takes into account what the population can afford.

8. It is assumed that FONATUR would sell all land on a sale contract basis, which would require a down payment of 15% of the sales price at the time of signing the sales agreement. The balance of the sales price would

bear an interest rate of 13% per annum with principal and interest payable in equal installments over a 5-year period. These assumptions would mean that FONATUR would earn income from interest on the deferred cash receipts over a 5-year period. The interest rate on the deferred cash receipts has been adjusted to 6% interest indexed for inflation.

9. The operating costs include expenditures for community development, operating expenses for the project unit activities in the field, promotional and administrative activities for the tourism estate, and maintenance of the infrastructure within the resort complex. These costs, included in the project cost estimates as indirect costs (para. 4 above), have not been capitalized but treated as operating costs to be deducted from operating revenues from the initial year of project implementation. The operating costs, excluding maintenance costs are based on assumed work programs for the respective activities. The annual maintenance costs are estimated at an average of 1% of the depreciable total assets. On the basis of a straight line depreciation schedule, the civil work structures were depreciated over a 30-year period and equipment over a 10-year period. Only interest during construction has been treated as deferred expense which would be amortized over a 5-year period of operation.

10. On the basis of the above assumptions, the results of financial forecasts for FONATUR's estate operations at Loreto and San Jose del Cabo indicate that the financial position of the project would be sound with adequate income to cover financial costs and reserves for replacement costs and additional investment.

11. In the case of Loreto, however, if urban investments in the town of Loreto were separated from investments in tourism it would not be possible to recover the initial capital invested in the town because most of the land in the town will be sold at low prices to local residents for residential sites. This situation would not be true in the case of the town of San Jose del Cabo although urban lots would be sold at similar prices, because infrastructure investment costs are lower. When the financial projections of the estate operation for the tourist zone and the town of Loreto are consolidated, however, the financial position appears to be sound, with satisfactory debt service coverage, despite a net cash flow rate of return on equity which would be relatively low, reaching 10% in the fifth year of operation. In the case of the estate operation at San Jose del Cabo, it is assumed that a large portion of the land would be sold as sites for hotels and other commercial establishments with prices high enough to enable the project to recover the initial capital investment employed. The financial rate of return in San Jose del Cabo would be 24% (net cash flow on equity) by the fifth year of operation.

12. In addition to the financial returns to FONATUR on the estate operations at Loreto and San Jose del Cabo, the government is expected to receive substantial tax revenues from hotels and other commercial establishments in the project areas (Annex X).

13. To achieve the financial objectives of its estate operations, it is recommended that FONATUR establish a proper financial reporting system. The system would be based on specific financial formats and would include budgets for long-range operational programs, quarterly progress reports and project management accounting statements (income statements and balance sheets). These financial reports would be prepared and submitted by the Project Units to FONATUR management and the Bank. A comparison of actual operating results versus budgeted financial targets would be made and reported to FONATUR management and the Bank together with appropriate explanations as to cause of significant variations and proposals for action.

MEXICO: APPRAISAL OF LORETO TOURISM PROJECT

LORETO - FONATUR'S ESTATE OPERATION

Pro-forma Income and Expense Statement
(in US Million Dollars)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>	<u>1987</u>
		1	2	3	4	5	6	7	8	9	10
Revenue:											
Sales from Land											
Hotel Zone	-	1.00	1.26	1.10	1.15	1.92	.78	.54	.56	-	-
Villas Zone	-	-	-	.50	.52	.84	.87	.90	1.60	1.70	1.75
Commercial Zone	-	-	-	.15	.15	.15	.15	-	-	-	-
Urban Zone	-	1.15	1.23	1.69	2.50	.30	.15	.15	.30	-	-
Gross Sales	-	2.15	2.49	3.44	4.32	3.21	1.95	1.59	2.46	1.70	1.75
Less Cost of Land	-	(.04)	(.04)	(.05)	(.05)	(.05)	(.03)	(.02)	(.03)	(.02)	(.02)
Net Sales	-	2.11	2.45	3.39	4.27	3.16	1.92	1.57	2.43	1.68	1.73
Operating Cost:											
Community Development	.18	.53	.64	.76	.76	.76	.38	.38	.38	.19	.19
Operating Expense	-	-	-	.44	.44	.44	.22	.22	.22	.11	.11
Promotion	-	-	.20	.20	.20	.20	.10	.10	.10	.05	.05
Project Administration	.21	.43	.64	.64	.64	.64	.32	.32	.32	.16	.16
Maintenance	-	-	-	.19	.19	.19	.19	.19	.19	.19	.19
Total Cost	.39	.96	1.48	2.23	2.23	2.23	1.21	1.21	1.21	.70	.70
Gross Operating Income:	(.39)	1.15	.97	1.16	2.04	.93	.71	.36	1.22	.98	1.03
Other Income	-	.24	.48	.77	1.10	1.19	1.08	.92	.85	.73	.67
Gross Income	(.39)	1.39	1.45	1.93	3.14	2.12	1.79	1.28	2.07	1.71	1.70
Less											
Depreciation	-	-	-	-	.59	.59	.59	.59	.59	.59	.59
Amortization	-	-	-	-	.10	.10	.10	.10	.10	-	-
Interest	-	-	-	-	.19	.18	.16	.15	.13	.12	.10
Total	-	-	-	-	.88	.87	.85	.84	.82	.71	.69
Net Operating Income	(.39)	1.39	1.45	1.93	2.26	1.25	.94	.44	1.25	1.00	1.01
Cumulative Income	(.39)	1.00	2.45	4.38	6.64	7.89	8.83	9.27	10.52	11.52	12.53
Cash Flow Return on Government's Contribution to Equity	-	-	-	-	5.2	10.5	17.5	15.0	14.2	12.0	9.0

MEXICO: APPRAISAL OF LORETO TOURISM PROJECT

LORETO - FONATUR'S ESTATE OPERATION

Pro-forma Balance Sheet
(in US Million Dollars)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>	<u>1987</u>
		1	2	3	4	5	6	7	8	9	10
Assets											
Land	1.56	2.97 (.04)	4.38 (.08)	4.38 (.13)	4.38 (.18)	4.38 (.23)	4.38 (.26)	4.38 (.28)	4.38 (.31)	4.38 (.33)	4.38 (.35)
Less Transfer	-										
Subtotal	1.56	2.93	4.30	4.25	4.20	4.15	4.12	4.10	4.07	4.05	4.03
Other Fixed Assets											
in Working-Process	.39	3.92	8.10	11.89	-	13.06	13.06	13.06	13.06	13.06	13.06
in Operation	-	-	-	-	13.06	13.06	13.06	13.06	13.06	13.06	13.06
Less Depreciation	-	-	-	-	(.59)	(1.18)	(1.77)	(2.36)	(2.95)	(3.54)	(4.13)
Subtotal	.39	3.92	8.10	11.89	12.47	11.88	11.29	10.70	10.11	9.52	8.93
Current Assets											
Working Capital	(.15)	2.07	3.75	3.50	3.32	4.59	6.66	8.43	10.12	11.54	12.61
Receivables	-	1.55	3.03	4.77	6.55	6.70	5.70	4.48	4.14	3.70	3.60
Subtotal	(.15)	3.62	6.78	8.27	9.87	11.29	12.36	12.91	14.26	15.24	16.21
Other Assets	-	.08	.25	.50	.40	.30	.20	.10	-	-	-
Total Assets	1.80	10.55	19.43	24.91	26.94	27.62	27.97	27.81	28.44	28.81	29.17
Liabilities											
Less Long-term Loans	-	(3.27)	(6.61)	(9.18)	(8.62)	(8.05)	(7.46)	(6.86)	(6.24)	(5.61)	(4.96)
Equity											
Government Contribution	1.80	7.28	12.82	15.73	18.32	19.57	20.51	20.95	22.20	23.20	24.21
Retained Earnings	2.19	6.28	10.37	11.35	11.68	11.68	11.68	11.68	11.68	11.68	11.68
Debt/Equity Ratio	(.39)	1.00	2.45	4.38	6.64	7.89	8.83	9.27	10.52	11.52	12.53
	31:69	34:66	37:63	32:68	31:71	27:73	25:75	22:78	19:81	17:83	

MEXICO: APPRAISAL OF LORETO TOURISM PROJECT

LORETO - FONATUR'S ESTATE OPERATION

Pro-forma Cash Flow Statement
(in US Million Dollars)

	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
		1	2	3	4	5	6	7	8	9	10
<u>Source of Fund</u>											
Net Operating Income	(.39)	1.39	1.45	1.93	2.26	1.25	.94	.44	1.25	1.00	1.01
Non-cash Charges	-	-	-	-	.69	.69	.69	.69	.69	.59	.59
Subtotal	(.39)	1.39	1.45	1.93	2.95	1.94	1.63	1.13	1.94	1.59	1.60
Increase in Assets	-	(1.55)	(1.48)	(1.74)	(1.78)	(.15)	1.00	1.22	.34	.44	.10
Internal Cash Generation	(.39)	(.16)	(.03)	.19	1.17	1.79	2.63	2.35	2.28	2.03	1.70
Government Contribution	2.19	4.09	4.09	.98	.33	-	-	-	-	-	-
Long-term Loans	-	3.27	3.34	2.57	-	-	-	-	-	-	-
Subtotal	2.19	7.36	7.43	3.55	.33	-	-	-	-	-	-
Total Fund	1.80	7.20	7.40	3.74	1.50	1.79	2.63	2.35	2.28	2.03	1.70
<u>Application of Fund</u>											
Land	1.56	1.41	1.41	-	-	-	-	-	-	-	-
Civil Work	.32	2.87	3.40	3.08	.95	-	-	-	-	-	-
Equipment	.07	.66	.78	.71	.22	-	-	-	-	-	-
Project Costs	1.95	4.94	5.59	3.79	1.17	-	-	-	-	-	-
Decrease in Assets	-	(.04)	(.04)	(.05)	(.05)	(.05)	(.03)	(.02)	(.03)	(.02)	(.02)
Subtotal	1.95	4.90	5.55	3.74	1.12	(.05)	(.03)	(.02)	(.03)	(.02)	(.02)
Interest during construction	-	.08	.17	.25	-	-	-	-	-	-	-
Amortization	-	-	-	-	.56	.57	.59	.60	.62	.63	.65
Total Applications	1.95	4.98	5.72	3.99	1.68	.52	.56	.58	.59	.61	.63
Annual Surplus	(.15)	2.22	1.68	(.25)	(.18)	1.27	2.07	1.77	1.69	1.42	1.07
Cumulative Surplus	(.15)	2.07	3.75	3.50	3.32	4.59	6.66	8.43	10.12	11.54	12.61
Debt Service Ratio	-	-	-	-	1.8	2.6	3.7	3.3	3.2	2.9	2.4

MEXICO: APPRAISAL OF BAJA CALIFORNIA TOURISM PROJECT

SAN JOSE DEL CABO - FONATUR'S ESTATE OPERATION

Pro-forma Income and Expense Statement
(in US Million Dollars)

Fiscal Year Operating Year	1977	1978 1	1979 2	1980 3	1981 4	1982 5	1983 6	1984 7	1985 8	1986 9	1987 10
Revenue:											
Sales from Land											
Hotel zone	-	1.00	.74	.77	1.15	1.32	1.56	1.35	1.40	-	-
Villas Zone	-	-	-	.25	.26	.28	.58	.60	.64	1.02	1.05
Urban Zone	-	3.03	.28	.44	.72	.72	1.11	.78	1.19	1.13	1.20
Gross Sales	-	4.03	1.02	1.46	2.13	2.32	3.25	2.73	3.23	2.15	2.25
Less cost of land	-	(.12)	(.01)	(.02)	(.02)	(.02)	(.03)	(.02)	(.03)	(.02)	(.02)
Net sales	-	3.91	1.01	1.44	2.11	2.30	3.22	2.71	3.20	2.13	2.23
Operating Cost:											
Community Development	.02	.05	.06	.08	.08	.08	.04	.04	.04	.02	.02
Operating Expenses	-	-	-	.24	.24	.24	.12	.12	.12	.06	.06
Promotion	-	-	.20	.20	.20	.20	.10	.10	.10	.05	.05
Project Administration	.13	.26	.38	.38	.38	.38	.19	.19	.19	.10	.10
Maintenance	-	-	-	.10	.10	.10	.10	.10	.10	.10	.10
	.15	.31	.64	1.00	1.00	1.00	.55	.55	.55	.33	.33
Gross Operating Income	(.15)	3.60	.37	.44	1.11	1.30	2.67	2.16	2.65	1.80	1.90
Other Income	-	.45	.49	.56	.67	.75	.84	.92	1.03	.98	.92
Gross Income	(.15)	4.05	.86	1.00	1.78	2.05	3.51	3.08	3.68	2.78	2.82
Less											
Depreciation	-	-	-	-	.41	.41	.41	.41	.41	.41	.41
Amortization	-	-	-	-	.05	.05	.05	.05	.06	-	-
Interest	-	-	-	-	.10	.09	.08	.07	.07	.06	.05
Total	-	-	-	-	.56	.55	.54	.53	.54	.47	.46
Net Operating Income	(.15)	4.05	.86	1.00	1.22	1.50	2.97	2.55	3.14	2.31	2.36
Cumulative Income	(.15)	3.90	4.76	5.76	6.98	8.48	11.45	14.00	17.14	19.45	21.81
Cash Flow Return on Government's Contribution to Equity		30.7	11.8	8.9	13.3	23.8	26.6	32.1	39.0	39.8	39.9

MEXICO: APPRAISAL OF BAJA CALIFORNIA TOURISM PROJECT

SAN JOSE DEL CABO - FONATUR'S ESTATE OPERATION

Pro-forma Balance Sheet
(in US Million Dollars)

	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987
		1	2	3	4	5	6	7	8	9	10
Assets:											
Land	.71	1.36 (.12)	2.01 (.13)	2.01 (.15)	2.01 (.17)	2.01 (.19)	2.01 (.22)	2.01 (.24)	2.01 (.27)	2.01 (.29)	2.01 (.31)
Less Transfer	-										
Subtotal	.71	1.24	1.88	1.86	1.84	1.82	1.79	1.77	1.74	1.72	1.70
Other Fixed Assets											
in Working-Process	.32	2.44	5.30	7.42	-	8.16	8.16	8.16	8.16	8.16	8.16
in Operation	-	-	-	-	.41	(.82)	(1.23)	(1.64)	(2.05)	(2.46)	(2.87)
Less Depreciation	-	-	-	-	7.75	7.34	6.93	6.52	6.11	5.70	5.29
Subtotal	.32	2.44	5.30	7.42							
Current Assets											
Working Capital	(.02)	2.46	3.62	5.07	5.59	7.33	9.28	11.62	14.47	17.37	20.28
Receivables	-	2.93	3.09	3.34	3.76	3.69	4.88	5.24	5.70	5.20	4.73
Subtotal	(.02)	5.39	6.71	8.41	9.35	11.02	14.16	16.86	20.17	22.57	25.01
Other Assets	-	.04	.13	.26	.21	.16	.11	.06	-	-	-
Total Assets	1.01	9.11	14.02	17.95	19.15	20.34	22.99	25.21	28.02	29.99	32.00
Liabilities:											
Less Long-Term Loans	-	(1.70)	(3.40)	(5.24)	(4.94)	(4.63)	(4.31)	(3.98)	(3.65)	(3.31)	(2.96)
Equity:											
Government Contributions	1.01	7.41	10.62	12.71	14.21	15.71	18.68	21.23	24.37	26.68	29.04
Retained Earnings	1.16	3.51	5.86	6.95	7.23	7.23	7.23	7.23	7.23	7.23	7.23
(.15)	3.90	4.76	5.76	6.98	8.48	11.45	14.00	17.14	19.45	21.81	
Debt/Equity Ratio	-	19:81	24:76	29:71	26:74	23:77	19:81	16:84	13:87	11:89	9:91

MEXICO: APPRAISAL OF BAJA CALIFORNIA TOURISM PROJECT

SAN JOSE DEL CABO - FONATUR'S ESTATE OPERATION

Pro-forma Cash Flow Statement
(in US Million Dollars)

	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>1981</u>	<u>1982</u>	<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>	<u>1987</u>
	1	2	3	4	5	6	7	8	9	10	
<u>Source of Fund</u>											
Net Operating Income	(.15)	4.05	.86	1.00	1.22	1.50	2.97	2.55	3.14	2.31	2.36
Non-cash charges	-	-	-	-	.46	.46	.46	.46	.47	.41	.41
Subtotal	(.15)	4.05	.86	1.00	1.68	1.96	3.43	3.01	3.61	2.72	2.77
Increase in Assets	-	(2.93)	(.16)	(.25)	(.42)	.07	(1.19)	(.36)	(.46)	.50	.47
Internal Cash Generation	(.15)	1.12	.70	.75	1.26	2.03	2.24	2.65	3.15	3.22	3.24
Government Contribution	1.16	2.35	2.35	1.09	.28	-	-	-	-	-	-
Long-term Loans	-	1.70	1.70	1.84	-	-	-	-	-	-	-
Subtotal	1.16	4.05	4.05	2.93	.28	-	-	-	-	-	-
Total Fund	1.01	5.17	4.75	3.68	1.54	2.03	2.24	2.65	3.15	3.22	3.24
<u>Application of Fund</u>											
Land	.71	.65	.65	-	-	-	-	-	-	-	-
Civil Work	.24	1.61	2.17	1.61	.57	-	-	-	-	-	-
Equipment	.08	.51	.69	.51	.17	-	-	-	-	-	-
Project Cost	1.03	2.77	3.51	2.12	.74	-	-	-	-	-	-
Decrease in Assets	-	(.12)	(.01)	(.02)	(.02)	(.02)	(.03)	(.02)	(.03)	(.02)	(.02)
Subtotal	1.03	2.65	3.50	2.10	.72	(.02)	(.03)	(.02)	(.03)	(.02)	(.02)
Interest during Construction	-	.04	.09	.13	-	-	-	-	-	-	-
Amortization	-	-	-	-	.30	.31	.32	.33	.33	.34	.35
Total Application	1.03	2.69	3.59	2.23	1.02	.29	.29	.31	.30	.32	.33
Annual Surplus	(.02)	2.48	1.16	1.45	.52	1.74	1.95	2.34	2.85	2.90	2.91
Cumulative Surplus	(.02)	2.46	3.62	5.07	5.59	7.33	9.28	11.62	14.47	17.37	20.28
Debt Service Ratio	-	-	-	-	3.4	5.3	5.8	6.8	8.1	8.2	8.2

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

ECONOMIC JUSTIFICATION

A. Introduction

1. For purposes of economic evaluation, the investment program has been defined to include the following:

- (a) infrastructure for both the tourism and urban areas of Loreto and San Jose del Cabo, including the airports and the golf course and infrastructure that would benefit the poorest segments of the population;
- (b) superstructure facilities for the tourism and urban areas of Loreto and San Jose del Cabo, including the first pilot hotels financed by the project, health facilities, commercial and civic centers, market places, and schools;
- (c) expenditures on promotion, studies, technical assistance and community development activities; and
- (d) hotels, apartels, condominiums, villas, restaurants, shops, fishing boats and local transportation facilities which form a part of the program of investments but are not financed under the project.

2. Tourism net benefits of the project would consist of expenditures of visitors to the two areas less the costs to Mexico of undertaking this project, compared with a situation in which the project was not undertaken. The net benefits accruing from services provided in the urban areas, including those provided to the poorest segments of the population, are discussed elsewhere (para. 15). The size of the net benefits depends, of course, upon the definition of the "without the project case". An exact definition is difficult, given the size of the country and the dynamic nature of the sector. Several scenarios can be envisaged. For example, it might be concluded that in the absence of the project, the Mexicans would proceed with the construction of exactly the same amount of tourism capacity in some other region of Mexico. In this case, the benefit-cost analysis would consist of evaluating this alternative, both from the market and cost-effectiveness points of view. Another alternative would be to assume that all the capacity added by the project is incremental, so that

the project is responsible for a temporary increase in the rate of growth, and a long-term increase in the amount of tourism capacity, than would otherwise exist. A third alternative would be to assume something in between; namely, that the project induces temporarily more rapid expansion than would otherwise occur, and that a fraction of this incremental expansion persists, so that Mexican tourism capacity is larger due to the project, although probably not by the full amount of the project's accommodation capacity. The present analysis adopts the third hypothesis. The justification for assuming that the project would result in somewhat higher long-run capacity in Mexico is because it will in fact diversify the Mexican tourism product, and permit Mexico to penetrate market segments inaccessible to resorts developed elsewhere.

B. Nature of Benefits

3. The economic impact of the decision to go ahead with the project has been evaluated in terms of estimated costs and benefits, with the analysis focusing exclusively on visitors accommodated in Loreto and San Jose del Cabo, although not all of the benefits generated by visitors accommodated in the two areas are considered incremental to the project. Some of these tourists would have visited Mexico even without the project given the already numerous and varied selection of destinations in the country. Others, however, would belong to a market segment tapped by the project.^{1/} Visitors from the first segment would substitute for demand elsewhere in Mexico while they stay in the project resorts, provided hotel space is available. Usually, however, hotels are full during the high season.^{2/} Therefore, only visitors of this segment staying in the project areas in the low season are considered non-incremental to Mexico. Sixty percent of visitors coming from abroad to Loreto are estimated to be incremental to Mexico (40% in the case of San Jose del Cabo). Of the remaining 40% (60%), 27.6% would come during the off-season^{3/} (in substitution for visits to other Mexican destinations). The facilities from which demand is diverted will face not only lower revenues but

1/ The vicinity to the US and particularly to southern California, one of major tourist generating markets, and the uniqueness of Baja California as a tourist destination, renders substance to the notion that they would not have come to Mexico without the project.

2/ Full capacity should be understood as somewhere around 90% occupancy rate, since imperfect information results in problems to secure reservations at higher occupancies, a situation that turns potential visitors away. High season corresponds to the November 15 to May 15 period. The rest is off-season.

3/ The proportion of off-season traffic is expected to be higher for hotels (some 35%) and lower for villas and condominiums (some 10%). It should also be recognized that since occupancy during the high season is not uniform, some diversion might take place then. However, this is assumed to be compensated by periods in the low season (like weekends and holidays) when capacity is full.

also lower variable operating costs. Assuming that these diverted tourists would have spent as much elsewhere, the deduction from receipts due to diversion would come to 7.8% of total revenues in Loreto and 11.7% in San Jose del Cabo (operating costs of hotels and other tourist facilities represent on the average some 65% of revenues, and variable costs some 45% of operating costs).^{1/} This portion of revenues is therefore treated as not incremental and subtracted from the benefits stream for the economic rate of return (ERR) calculations. In view of the conjectural nature of some of the assumptions involved in calculating the effect of demand diversion, the sensitivity of results to other assumptions is tested later on.

4. With regard to Mexican tourists, the diversion effect estimate is even higher. Only 25% of Mexicans visiting the two project resorts is assumed to be incremental tourism. The proportion of revenues derived from Mexican visitors to be subtracted from benefits in both project areas is 14.6%.

5. Diversion of demand from other tourist resorts would reduce average occupancy rates, profitability and ultimately investments there. It has, therefore, been assumed that there will be lower investments in accommodation elsewhere as well (see para. 2), but that it would take some time before investors react. It is estimated that it would take investors about a year to perceive the changed situation, and another year or so to implement investment decisions. The diversion effect is therefore assumed to be felt fully during two years and felt at only 50% during the third year. After the third year demand diverted by the project from elsewhere in Mexico is assumed to be fully offset by increased demand for existing accommodation as compared to the "with the project" case resulting from the cancellation of some other accommodation construction projects. With investment decisions being taken on the basis of present and expected profitability, the situation could be described as having reverted to its "dynamic equilibrium".^{2/}

6. Although the diversion of demand is being taken into account in the calculation of ERR's, the "creation" of demand by the project to other

1/ For Loreto, the calculation is as follows:

$$\begin{array}{rcl} (0.40 \times 0.276) & (1 - 0.65 \times 0.45) & = 0.078 \\ (\text{diverted revenues}) & (\text{variable GOP}) & (\text{net benefits diverted as a proportion of total revenues}) \end{array}$$

2/ This "equilibrium" is always changing, being dependent, among other things, on relative prices of inputs/outputs, on loan financing availability and terms, and on the tax structure, which change over time. Nevertheless, based on present experience, it is estimated that hotels, for example, require occupancy rates of over 65% to attract investors' interest.

parts of Mexico and the effect of the capacity increase on prices are not incorporated into this analysis. Just as there is diverted demand, it can safely be said that the project would attract visitors to the project areas who would also visit other parts of Mexico or other parts of Baja California.^{1/} The creation of demand would occur as a result of improved air access and of the effect of the project-related promotion campaign in raising demand for Baja specifically, and Mexico more generally.^{2/} The omission of these positive effects in the ERR calculations is assumed will be compensated by the omission from the analysis of explicit consideration of "price softening" which could result from the more rapid expansion of accommodation capacity under the project.^{3/} This assumption is later tested in the sensitivity analysis.

7. The above analysis does not address itself to the question of whether the present set of taxes, credit arrangements and government promotional policies are such as to maximize tourism returns to Mexico. Changes in taxation and financing terms, for example, would in turn change the level of tourist prices and occupancy rates and affect the level of investment in the sector. By limiting the buildup of accommodation capacity, the Government could increase occupancy rates and presumably prices of existing hotels, but this would mean less tourists in the peak season as compared to the unrestricted growth case (off-season market growth could still be accommodated to a large extent). In order to enable the Government to tackle some of these questions, a market and economic study seeking to gather and analyze the necessary information has been included in the project.

8. The gross benefits resulting from the development of tourism facilities would then be the expenditures of visitors accommodated in the Loreto and San Jose del Cabo sites (duly corrected for demand diversion) and the receipts from sale of villas, condominiums and apartel units to foreigners plus the rental value to resident users of their own units. Those gross benefits relating to urban facilities would be the revenues from sale of urbanized lots to the local

1/ There are 500 international-class hotel rooms in the project areas' surroundings. These have low occupancy rates (they averaged below 50% in 1975 and around 50% in the early seventies) and the situation will not probably improve much without the air accessibility the project will provide.

2/ For example, some of those visitors from abroad belonging to market segments being tapped by the project might visit other parts of Mexico in the course of the trip. The average length of stay in the project areas is estimated will be four days, which is similar to the average for other resorts in Mexico. In contrast, the total average stay of foreign visitors in Mexico is ten days.

3/ Only reduction in prices in the case of foreign expenditures should be accounted for since in the case of Mexicans it is roughly compensated by an increase in their consumer surplus.

population,^{1/} and the rental values for the housing units built under the sites and services component of the project. Those relating to the electricity, telephone and water and sewerage facilities provided under the project would be the tariffs charged to incremental users of these facilities in the project areas.

9. The costs associated with these benefits would be the capital and operating costs of infrastructure (both tourism and urban) and the costs of hotels, apartels, restaurants and other superstructure. The revenue and cost assumptions are described in paras. 12 to 30 below. All revenues and costs are calculated at October 1, 1976 prices and expressed in US dollars. Any differential inflation rates between Mexico and the U S are assumed to be offset by movements in the floating Mexican peso.

10. Separate ERR have been calculated for Loreto and San Jose del Cabo, which are some 500 km apart. For each project area only one ERR has been calculated. Although it is possible arithmetically to run different calculations for the tourist and urban investments, the allocation of costs of components serving both tourism and the local population would be arbitrary. Despite the fact that some of the infrastructure investments might have been undertaken even in the absence of the project, albeit later, (e.g., the electricity transmission line from Villa Constitucion to Loreto which is part of CFE's interconnection plan, and the airport of San Jose del Cabo which is part of SAHOP's airport plan), it has been assumed that they would not, and therefore the full cost of these items (representing over 10% of infrastructure investment costs in Loreto and 20% in San Jose del Cabo respectively) has been incorporated in the ERR calculations. This imparts a conservative bias to the ERR calculations because the benefits that would have been generated by these investments "without" the project (external benefits as regards the project) have not been taken into account.

C. Revenue Assumptions

11. The expected average and breakdown of daily expenditures of Mexicans and foreign visitors are presented in Annex VII and range from US\$25.8 per day for a Mexican visitor to Loreto to US\$42.7 for a foreign visitor to San Jose del Cabo.

12. Revenue estimates for hotels and apartels are presented in Annex VIII. Revenues for villas and condominia have been calculated by assuming average daily rents of US\$20 per room (US\$40 per day for a two-bedroom apartment used on average by 5 people). Average occupancy is assumed to be 50%, or 42% if time spent by the owner is excluded. These revenues exclude sales taxes (4%) and commissions and are in line with market projections and marketing strategies to be adopted for the project.

^{1/} Since little is known about the sort of houses that buyers of these lots would build and about the incremental value of the land since urbanized lots are not normally rented, this rather than the theoretically superior rental values approach has been preferred. The bias that is introduced does not affect the ERR calculations much, however.

13. In addition to the revenues generated when rented to visitors, villas, condominiums, and apartel units generate gross benefits to the Mexican economy which will be different, depending on who owns these facilities. In the case of Mexicans, representing 30% of owners in Loreto and 40% in San Jose del Cabo, the benefits have been estimated by the use made of the units purchased (around one month a year) at a price equal to their room tariffs (or rental value). The actual purchase price of these units and the net financial returns they get from their commercial operation have been treated here as financial transfers and not entered into the economic evaluation. In the case of foreigners, on the other hand, the actual purchase price of the units has been considered as gross benefits (revenues) to the project,^{1/} the net financial returns they get have been treated as cost and no imputed rental value has been accounted for. It is assumed that the units would be sold a year after the opening, with about half the buyers paying in cash (the fact that they in turn might get loans from US banks is irrelevant) and the remainder paying in five years with a 20% down payment and a real interest rate of 5%. The projections for selling prices are: US\$30,000 for a typical 2-bedroom condominium apartment, US\$45,000 for a typical 3-bedroom villa, and US\$36,000 for a 2-bedroom apartel unit, all net of commissions and promotional costs. Although these prices are significantly lower than going prices (after devaluation) of actual sales in other parts of Mexico, such as Cancun and Acapulco, they are assumed to be so because of the large volume of sales involved.

14. Revenues generated by the water and sewerage services are shown in Annex IV. No consumer surplus has been assumed. Revenues from electricity have been estimated on the basis of an average selling price of US\$0.35 per KWH and consumption on the basis of experience typical of other resorts in Mexico. Since the costs of the telephone services were too difficult to estimate meaningfully, no revenues (nor operating costs) have been included in the ERR calculation.^{2/} The telephone company generates high returns on its investments, however, and the fact that investment costs of the telephone component of the project are included in the calculations imparts a conservative bias to the ERR's.

15. The gross benefits of the urban area are derived from sale prices of urbanized lots and are shown in Annex IX. In the case of the 500 houses built in each area under the sites and services program, gross benefits are assumed would be US\$30 per month per house which reflects the rental value of similar housing units in Baja California.

16. No gross benefits have been included on account of the airport, since experience in Mexico shows that their revenues barely cover operating costs (Annex III). All indirect taxes paid by foreigners and by Mexicans who

1/ This assumes that these investments are tied to the project (see footnote to para. 36).

2/ The implicit assumption being that revenues just cover operating costs. Being part of an integrated network, the telephone company would not provide estimates of the marginal operating costs nor of the marginal investments in their central facilities that the project would make necessary. The studies involved would be too costly compared to the cost of the telephone component of the project.

have travelled abroad without the project have been included in the gross benefits stream.^{1/} No direct taxes have been included.

D. Investment Cost Assumptions

17. Ninety-eight percent of the project investment costs have been taken into account in the cost stream for ERR calculations. The few components not included (like clinics, civic centers, and some community development expenditures during construction) have associated benefits but they are too difficult to estimate meaningfully. Since the area is a duty free zone, no import taxes have been subtracted from the costs. Although some locally procured items are subject to indirect taxes, these have not been taken into account and therefore the investment costs stream is slightly overestimated.

18. In addition to the components included in the project, other facilities such as hotels, apartels, villas, condominiums, shops, transport equipment, sporting and entertainment centers, restaurants, and nightclubs would be built or acquired by the private sector. The cost of materials for house construction in connection with the sites and services components of the project (estimated at US\$2,000 per house) is also included.^{2/} The investment costs of the hotels including physical contingencies, professional services and pre-opening expenses, have been estimated at an average of US\$24,000 per room; that of apartels at US\$18,000 and that of villas and condominiums at US\$11,000. All these estimates exclude the cost of land, price contingencies and interest during construction. The investment cost in other tourism enterprises, such as shops and restaurants, is estimated to total US\$7.35 million in Loreto and US\$10.25 million in San Jose del Cabo based on the cost of such facilities in other Mexican resorts.

19. The opportunity cost of land used for the project (about 260 hectares in Loreto and 250 in San Jose del Cabo) has been estimated at US\$560,000 in Loreto and at US\$450,000 in San Jose del Cabo.^{3/} These costs have been based on appraisals of the Ministerio del Patrimonio which duly

^{1/} Under the assumption that 75 percent of expenditures of Mexicans would have been incurred in other activities in Mexico without the project, the foregone indirect taxes with the project (assumed equal to the ones paid with the project) are deducted from the revenue stream.

^{2/} These houses would be built under a guided self-help program. The technical assistance cost is included in FONATUR's operating costs and the economic cost of the owner's work is assumed to be zero on grounds that the program is designed for those with no permanent jobs.

^{3/} FONATUR has purchased more land than needed for the implementation of the project.

take into account other alternatives to use the land.^{1/}

20. On the basis of the above assumptions, the investment costs, excluding replacement costs, relevant to the project evaluation are shown below:

	<u>Loreto</u> (in US\$ mil.)	<u>San Jose del Cabo</u> (in US\$ mil.)	
	(in %)	(in %)	
Superstructure	<u>83.95</u>	<u>74.7</u>	<u>84.75</u>
Hotel, apartels, villas and condominia	75.45	67.1	73.45
Other commercial facilities	7.35	6.6	10.25
Housing	1.15	1.0	1.05
Infrastructure	<u>28.50</u>	<u>25.3</u>	<u>15.79</u>
Land	0.56	0.5	0.45
Basic infrastructure	24.94	22.1	13.06
Project administration, promotion and pre- opening expenses	3.00	2.7	2.28
Total	<u>112.45</u>	<u>100.0</u>	<u>100.54</u>
			<u>100.0</u>

21. The infrastructure cost (including investments in the support towns to provide urbanized lots to the local population) represents about one-fourth of the total project cost in Loreto and less than one-fifth in San Jose del Cabo. This reflects the fact that some infrastructure already exists in these areas, especially in San Jose del Cabo.

22. Replacement costs will be incurred every five years, at the rate of 10% of investment costs for hotels and apartels, 7.5% for villas and condominia, 25% for other commercial facilities, and 5% for the infrastructure.

E. Operating Cost Assumptions

23. The projected operating costs for hotels and apartels have been derived from the financial forecasts described in Annex VIII. The operating costs of villas and condominia--representing on average some 55% of revenues--have been estimated on the basis of experience in other Mexican resorts. The full cost of utility services (which represent revenues of the agencies selling such services) is included. The operating costs of commercial activities other than those involving accommodation have been estimated on the basis of a FONATUR survey undertaken in Cancun and on experience elsewhere in Mexico. They represent on average some 65% of revenues. The operating costs of FONATUR's estate

1/ These costs are assumed to be roughly equivalent to the discounted stream of the land's annual rental value. (No discount rate nor horizon is given in the Ministerio del Patrimonio's calculations.) Any bias in the ERR's calculations that might be imparted by this assumption would be small, however.

operations and the water supply and sewerage are based on projections described in Annexes IV and VIII. In the case of electricity supply, they have been estimated at 80% of revenues in Loreto and 70% in San Jose del Cabo, which are based on information provided by CFE (Annex II).

24. Foreign buyers of apartels, villas, and condominium units are assumed to receive a 4% real annual return on their original investment, and the derived profits have been entered as a cost in the ERR calculations. This figure is consistent with the financial results these facilities are expected to achieve and with other real estate ventures in Mexico that offer fixed returns to buyers.

25. Although unemployment and under-employment of unskilled labor are widespread in Mexico, sparsely populated Baja California has low unemployment because there are few opportunities to subsist without modern sector employment. Experience in Mexico shows, however, that migration into areas where employment is created seems to be triggered almost immediately.^{1/} Wages for unskilled labor (representing around 50% of total wages) have therefore been shadowpriced at 75% of market wages. The case where shadow wages are assumed to be equal to market wages has been tested in the sensitivity analysis.

F. Internal Economic Rates of Return

26. The project's cost and benefit streams in Loreto and San Jose del Cabo resulting from the above assumptions and projections are presented below:

Year	Economic Cost and Revenue Streams (in US\$ million)				San Jose del Cabo			
	Loreto				San Jose del Cabo			
	Inv. Costs	Oper. Costs	Revenues	Net Benefits	Inv. Costs	Oper. Costs	Revenues	Net Benefits
1	5.8	-	-	(5.8)	3.2	-	-	(3.2)
2	11.4	0.2	0.2	(11.4)	7.7	-	0.3	(7.7)
3	23.5	0.2	0.6	(23.2)	16.6	0.2	0.6	(16.2)
4	11.3	5.1	6.5	(9.9)	8.0	4.5	5.6	(6.9)
5	10.6	10.8	15.8	(5.6)	8.4	8.0	11.4	(5.0)
6	11.5	16.0	24.6	(2.9)	10.2	11.8	18.5	(3.4)
7	15.0	22.0	36.9	(0.1)	12.4	17.2	26.3	(3.3)
8	8.6	29.6	49.2	11.3	12.2	22.1	36.6	2.3
9	7.5	35.7	58.4	15.3	10.1	28.3	46.7	8.3
10	13.3	40.0	67.6	14.3	14.1	33.5	55.9	8.3
11	3.3	45.0	74.5	26.2	2.4	38.7	64.9	23.8
12	1.5	47.5	79.2	30.2	2.5	40.4	70.0	27.2
13	2.1	48.0	81.5	31.4	2.1	41.8	73.6	29.8
14	2.1	48.3	79.0	28.6	2.1	43.0	75.1	30.0
15	2.1	48.4	79.3	28.8	2.1	43.1	75.7	30.5
16 - 30	2.1	48.4	79.4	28.9	2.1	43.1	75.8	30.6
<u>Present Values</u>								
(10% Discount rate)								
	<u>88.3</u>	<u>255.7</u>	<u>418.9</u>	<u>74.9</u>	<u>73.8</u>	<u>217.4</u>	<u>369.9</u>	<u>78.8</u>

^{1/} The development of Cancun is a relevant example of Mexico's population mobility, even when it involves moving to remote areas.

27. Based on these streams and an estimated economic life of 30 years, the internal economic rate of return is 19% in Loreto and 21% in San Jose del Cabo. Since facilities are built over a period of 12 years, the economic life of the facilities implicit in these calculations varies from 27 years for the first hotels (hotels may have an even longer life if properly maintained) and 18 years for some villas and condominiums. Facilities or equipment with shorter economic lives are replaced several times (para. 22). No residual value is taken into account.

G. Sensitivity Analysis

28. The sensitivity of the project's economic rate of return to changes in costs and revenues is presented below:

Internal Economic Rate of Return: Sensitivity Analysis

		<u>Loreto</u>	<u>San Jose del Cabo</u>
<u>Best Estimate</u>		18.7	20.6
<u>Changes</u>			
Investment Cost	+ 10%	17.3	19.0
	+ 20%	15.9	17.6
Operating Cost	- 10%	21.3	23.1
	+ 10%	16.1	17.9
	+ 20%	13.1	15.1
No Shadow Wages		17.2	18.9
Gross Operating Profit	+ 10%	21.4	23.3
	- 10%	16.3	17.9
	- 20%	13.1	15.1
Prices a/	+ 10%	21.9	25.1
	- 10%	14.2	16.0
One Year's Delay b/in Project Implementation		16.1	17.0
Only 75% of Superstructure Developed c/		16.2	17.8

a/ Change of all prices used in estimating revenues in tourist facilities.

b/ Some investments in the initial years are stretched out, so that operations commence in Year 5.

c/ Development stops when it reaches 75% of best estimate total capacity.

29. Assuming, in contrast to the base case, that the price "dilution" effect is not compensated by the project's demand "creation" effect, i.e., that the project's promotion, accessibility and added diversity in the offer will not affect demand for Mexican destinations as a whole, including the project area (para. 7), and that the price elasticity of demand for Mexico is -5 (or -3), the internal economic rate of return would be 16.6%

(13.1%) in Loreto and 17.5% (14.0%) in San Jose del Cabo.^{1/}

30. If the proportion of foreign visitors that would not have come to Mexico "without" the project were only 40% instead of 60% in the case of Loreto and 20% instead of 40% in the case of San Jose del Cabo (implying a stronger substitution of demand elsewhere in the country (para. 6), then the internal economic rate of return would be 17.1% in Loreto and 18.4% in San Jose del Cabo.

H. Project's Main Risks

31. While the ERR of the project is not very sensitive to changes in investment cost, it is quite sensitive to changes in operating costs. However, the risk of operating costs increasing by as much as 20% with no parallel increases in revenues is considered small, since prices of tourist goods and services have always followed the inflation trend quite closely, and in the future the assumed corrections of the exchange rate will prevent Mexico's tourism from becoming uncompetitive. Moreover, in relation to operating efficiency, hotel management skills in the country are already developed and it is not difficult to "absorb" what amounts to a modest expansion of capacity by Mexico's standards.

32. Possible lack of investors' interest to build hotels because of unattractive profit prospects is perhaps the greatest risk facing the project. Nevertheless, even with only 75% of superstructure development (and a similar fall in visitors' arrivals in the later years) the project is still economically feasible. In fact, the sensitivity of the rates of return to a shortfall in such development is small. This is due to the rather low proportion of the infrastructure investments (or the fixed costs), particularly in San Jose del Cabo. In addition, FONATUR's active role in lending and even in direct investment in hotels make the hotel construction projections quite firm, in particular during the early years of hotel development as experience in Cancun and Ixtapa has shown, making a shortfall in the earlier years less likely.

33. Even if hotel investors are forthcoming, however, there is always the risk of a softening of the market for Mexico as a whole (as well as for the resorts in Baja California) and of hotels achieving lower occupancy rates. It is, however, unlikely that a significant drop in occupancy rates will be permanent since relative softness in the market for a long period would soon slow down expansion in overall accommodation capacity in Mexico (the project is expected to represent only some 9% of total international-class accommodation development in Mexico during the 80s assuming a 6% per year average growth rate), thus helping to restore profitable occupancy levels and prices in these and other resorts. Nevertheless, should occupancy rates of all accommodation facilities fall by 20% (from 58% on average to 46%) from the

1/ Since lower prices will have a similar effect as lower occupancy rates on profitability and investments in new accommodation elsewhere, the same arguments and assumptions regarding the period and extent of such effect described in para. 5 are applied here.

time the capacity is fully developed (around the eighth year of operation of the resorts) onwards, the internal economic rates of return on investments in Loreto would be 13% and in San Jose del Cabo, 14.3%.

34. As can be observed from the Sensitivity Analysis table, a fall in prices (costs remaining unchanged) would cause a severe drop in the rates of return. A fall in prices of, say, 10% over the life of the project is considered unlikely, however, since the base case prices and resulting expenditures per day are lower than those estimated in other Mexican resorts in mid-1976 (Annex VI), and quite low for the standards of competing destinations abroad.

I. Balance of Payments Effect

35. Based on the projected expenditures of foreign tourists and on estimates of foreign exchange component (direct and indirect) of 50% of investment costs and 20% of operating costs,^{1/} the projected foreign exchange component of revenues and costs and net foreign exchange earnings generated by the project are shown in the table on page 13.

36. Mexico's net foreign expenditures would total some US\$35 million in foreign exchange in the two resorts by year 4. Thereafter, accumulated net foreign exchange earnings would grow, becoming positive by year 7 and reaching some US\$180 million by year 10. Over the life of the project, net foreign exchange earnings generated in Loreto would be US\$1,100 million, and US\$850 million in San Jose del Cabo.^{2/} The project will therefore make a significant contribution to Mexico's balance of payments.

J. Employment Effect

37. The direct employment effect of the project by the time it reaches full development is estimated at some 5,900 additional jobs in Loreto and 6,000 in San Jose del Cabo. (See table on page 16.) Around 55% of these would be in accommodation facilities (mostly in hotels and apartels), around 34% in commercial facilities outside hotels such as shops, restaurants, and .

^{1/} This percentage is much higher than normal in Mexico because Baja California is a duty free area with easy access to the United States. It also includes dividends to foreign villa and condominium owners.

^{2/} It is assumed that the only investments financed by foreigners and tied to the project correspond to purchase of villas and condominiums and that whatever they invest in hotels (and tied to the project) is compensated by a proportion of the first being untied investments. The Bank loan is considered to be untied.

Net Foreign Exchange Earnings
(in US\$ million)

Year	Loreto					San Jose del Cabo				
	Inv. Costs	Oper. Costs	Foreign Exchange Revenues	Net F. Exch. Earnings	Accum.	Inv. Costs	Oper. Costs	Foreign Exchange Revenues	Net F. Exch. Earnings	Accum.
1	2.9	-	-	(2.9)	(2.9)	1.6	-	-	(1.6)	(1.6)
2	5.7	-	-	(5.7)	(8.6)	3.6	-	-	(3.6)	(5.3)
3	11.8	-	-	(11.8)	(20.4)	8.3	-	-	(8.3)	(13.6)
4	5.7	1.0	5.2	(1.5)	(21.8)	4.0	3.9	-	(1.0)	(14.6)
5	5.3	2.2	12.4	4.9	(16.9)	4.2	1.6	7.6	1.8	(12.7)
6	5.8	3.2	20.7	11.7	(5.2)	5.1	2.4	13.1	5.6	(7.1)
7	7.3	4.4	29.8	18.1	12.9	6.2	3.3	18.9	9.3	2.3
8	4.3	6.0	44.7	34.4	47.3	6.1	4.5	25.3	14.8	17.0
9	3.8	7.3	46.3	35.3	82.6	5.1	5.7	32.7	21.9	38.9
10	6.7	8.1	53.5	38.7	121.3	7.0	6.8	38.8	25.0	63.9
11	1.7	9.2	58.3	47.5	168.8	1.2	7.9	45.0	36.0	99.8
12	0.8	9.7	61.3	50.9	219.7	1.2	8.2	47.5	38.1	137.9
13	1.1	9.8	62.4	51.6	271.3	0.6	8.5	49.4	40.3	178.3
14	1.1	9.8	59.4	48.5	319.8	1.1	8.7	49.2	39.4	217.6
15-30	1.1	9.9	59.6	48.7	1,098.4	1.1	8.8	49.7	39.8	855.0

sports clubs, the rest in construction^{1/} and the infrastructure services (mostly utilities and airports). Over the life of the project, some 158,000 man-years would be generated in each Loreto and San Jose del Cabo (50% of which in accommodation facilities, 30% in commercial facilities outside hotels, 15% in construction, and the rest in infrastructure services).^{2/}

38. Indirect employment can be estimated roughly at 10-15,000.^{3/} This would be concentrated in handicrafts, agriculture, food processing, production of furniture and hotel equipment, transportation, etc. Only some 1,000 of these would be generated in each project area. Most of the rest would probably be generated out-of-state.

39. Unskilled labor would represent more than 60% of the labor force (although less than 50% of the wage bill). Employment opportunities for women would be created both directly and indirectly by the project. It is estimated from experience elsewhere in Mexico's hotel industry, that some 30-40% of direct employment created could be filled by women.

K. Effect on Government Finances

40. The Government would benefit both directly and indirectly from its investments in the project area. In addition to the Government revenue-earning agencies involved in the project, such as FONATUR and utility companies, the Government would capture revenues from the 4% sales taxes and direct taxes paid by commercial enterprises (direct taxes paid by workers on income generated by the project are not included). On the other hand, the Government would invest in land, in tourist and urban infrastructure, in one hotel and in several other superstructure facilities in each area. It would incur increased expenses related to project administration and promotion (no incremental tax collection costs are considered).

41. The estimated incremental costs and revenues that would accrue to the Government with the project in the two areas (excluding the effect of the Bank loan, which is considered untied to the project, and FONATUR's hotel lending operations) are presented on page 16.

1/ Estimates of employment in construction were derived from investment costs based on the assumption that labor cost per man-year is US\$2,200.

2/ Defining one permanent job as 15 man-years and discounting investments at 10%, the project generates one "job" for every US\$7,673 invested. If both investment costs and man-years are discounted at 10%, the investment cost per man-year comes to some US\$1,800, and compares favorably with the urban poverty lending benchmark for Mexico on employment generation grounds.

3/ According to data from Mexico's 1960 input-output table, the relationship between direct and indirect employment in tourism is around 1:1.3, and almost 70% of indirect employment is generated in agriculture.

DIRECT EMPLOYMENT PROJECTIONS

<u>Year</u>	<u>Construction</u>	<u>Hotels</u>	<u>Apartments</u>	<u>Villas & Condominia</u>	<u>Infra-structure</u>	<u>Other facilities</u>	<u>Total</u>
<u>Loreto</u>							
1	960						960
2	1800				220		2020
3	3800				280		4080
4	1811	300	120		350	300	2880
5	1690	420	440	36	360	700	3650
6	1846	540	680	75	370	900	4410
7	2392	720	880	124	380	1150	5650
8	1378	840	1280	184	390	1400	5470
9	1200	960	1440	241	400	1600	5840
10	2120	1080	1520	309	400	1700	7130
11	212	1200	1600	388	400	1800	5600
12	212	1200	1600	479	400	1900	5790
13	212	1200	1600	479	400	2000	5890
14-30	212	1200	1600	479	400	2000	5890

	<u>San Jose del Cabo</u>						
1	540						540
2	1200				200		1200
3	2600				280		2880
4	1270	240	160		350	300	2320
5	1330	360	320	20	360	700	3090
6	1620	480	480	46	370	800	3796
7	1990	660	680	77	380	1000	4787
8	1950	840	920	107	390	1200	5407
9	1614	1080	1160	138	400	1400	5792
10	2248	1200	1400	168	400	1700	7116
11	376	1320	1640	200	400	2000	5936
12	392	1320	1640	240	400	2100	5852
13	210	1320	1640	275	400	2100	5945
14-30	210	1320	1640	313	400	2100	5943

Government Finances
(in US\$ Million)

<u>Year</u>	<u>Investment Costs</u>	<u>Operating Costs</u>	<u>Revenues</u>	<u>Cash Flow</u>	<u>Accum. Cash Flow</u>
1	9.4	--	--	(9.4)	(9.4)
2	18.2	.4	5.0	(13.6)	(22.9)
3	27.9	.6	3.4	(25.1)	(48.0)
4	--	1.0	6.2	5.2	(42.9)
5	--	1.4	10.1	8.7	(34.2)
6	.4	1.6	10.4	8.5	(25.8)
7	.4	2.4	13.0	10.2	(15.6)
8	.4	3.0	15.3	11.9	(3.7)
9	.4	3.4	21.2	17.4	13.7
10	.4	3.8	21.5	17.2	30.9
11	.4	4.1	24.2	19.7	50.6
12	.4	4.2	21.9	17.3	67.9
13	.4	4.3	22.8	18.1	86.0
14	.4	4.3	23.6	18.9	104.9
15	.4	4.3	24.0	19.3	124.2
16	.4	4.3	24.4	19.7	144.0
17-30	.4	4.3	25.6	19.8	163.8
					to 421.9

42. The internal rate of return on the Government's cash flow is over 20%. Most of the revenues would be collected in the form of taxes.

L. Distribution of Project Benefits

43. The following table shows the distribution of project financial benefits: 1/

Present Value (at 10% discount rate) of Project Net Financial Benefits, by Recipients

	<u>Loreto</u> (in US\$ m.)	<u>San Jose del Cabo</u> (in US\$ m.)	
	<u>(%)</u>	<u>(%)</u>	
(a) Hotels, apartels, villas and condominia	5.5	7.2	5.8
(b) Shops, restaurants, street vendors, guides, local transp., etc.	26.5	34.9	18.5
(c) Unskilled workers <u>2/</u>	22.9	30.2	19.3
(d) Government <u>3/</u>	21.0	27.7	35.1
Total	<u>75.9</u>	<u>100.0</u>	<u>78.7</u>
			<u>100.0</u>

1/ Since the financial projections have been corrected here by reducing gross benefits to account for demand diversion, this table underestimates the amount of the project's net financial benefits, but the distribution is not altered much.

For Footnotes 2/ and 3/ see page 17.

- 2/ The difference between wages and benefits paid to unskilled labor with the project and shadow wages has been entered here as a financial benefit, the assumption being that unskilled labor would have been paid on average shadow wages in alternative occupations. This would likely overestimate the benefits of unskilled workers. In addition, one half of tips has been entered as a benefit, on grounds that unskilled labor receive tips on top of a minimum salary that normally would have been sufficient to attract them to employment in tourism. Some semi-skilled and skilled labor, on the other hand, receive basic salaries that are normally lower than in alternative occupations in which case the tips become essential to attract them to tourism employment.
- 3/ Includes the profits of Government agencies, such as FONATUR, and utilities, in addition to taxes.

Since no consumer surpluses were calculated in the urban development components of the project, the benefits accruing to the poorest segments of society have not been fully accounted for. A more detailed discussion of the benefits to the local population is presented in Annex XI.

MEXICO

APPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECT

SOCIAL ASPECTS

I. Introduction

1. The social impact of tourism development in Mexico has to be evaluated in the light of present tourism sector policies. A first factor affecting the nature, extent and value of the impact is the presence or absence of planning. Development of the tourism sector in Mexico in the past, as well as other sectors, was characterized by a lack of effective government controls and regulations. An example of this is Acapulco, a beautiful but polluted bay, whose surrounding hills are eroded and lined with squatter settlements without community services, water, sewerage, or electricity. In the late 60s the Government decided to become more active in the planning of the tourism sector, so that Mexico could, among other things, avoid repeating costly economic and social mistakes of the past. Current tourism sector policies emphasize:

- (a) the need for development of the sector in those regions where tourism can be a major source of income and employment and can curb migration to urban areas;
- (b) the need to provide necessary social amenities to the local population (housing, education, health, training, etc.) while developing facilities for tourists;
- (c) the need to encourage local ownership and participation in tourism development; and
- (d) the importance of providing holidays for Mexicans of all income groups.

In implementing some aspects of these policies the Government has through FONATUR, obtained remarkable results in effectively coordinating and executing the development of two new resort areas: Ixtapa and Cancun.

II. Developments in Cancun and Ixtapa-Zihuatanjo

Cancun

2. With the implementation of this first integrated resort on a deserted tip of the Yucatan peninsula, Cancun's population grew from 117

people in 1970 to 15,000 in September 1974 at the height of its construction phase, leveling off to a population of 10,050 in September 1975. Many of its inhabitants come from the two neighboring states, Yucatan and Quintana Roo.

3. In spite of careful planning, experience in Cancun has shown that:

- (a) living conditions in camps for construction workers were often subhuman;
- (b) urban development proceeded faster than planned;
- (c) rapid urban growth led to a keenly felt lack of social-infrastructure;
- (d) rapid development created a housing shortage for middle and lower income families;
- (e) in addition to physical facilities, there is need for community development efforts to tackle day-to-day problems of the population;
- (f) training programs are essential;
- (g) unless provision is made for linkages to agricultural and other sectors, shortages will occur affecting adversely the cost of living (this is being rectified under Phase II of the Pider Program); and
- (h) it is essential to have periodic surveys of the population to monitor social and other developments.

Ixtapa-Zihuatanejo

4. FONATUR's second resort project, Ixtapa-Zihuatanejo, is located on the Pacific coast in the state of Guerrero, about 240 km north of Acapulco. It is in an extremely poor region of the country with high unemployment rates and social unrest. FONATUR's plans called for the development of the small fishing village of Zihuatanejo, which was to be developed both as a secondary resort and a service center for the main tourism zone at Ixtapa. Approximately one-third of the funds assigned to the project were used for urban development purposes. Land had to be acquired for the development from three different ejidos.^{1/} The ejidatarios consented to and requested expropriation of their land for tourism and urban development. It took over two years, however, to finally acquire the land and agree on the amount and type of compensation.

^{1/} A communal land ownership system dating back to pre-Colombian times and re-instituted at the time of the revolution (para. 22).

5. Work in the tourism zone at Ixtapa, however, proceeded according to the original schedule and an influx of construction workers resulted in a housing shortage and an increase in consumption and prices. At the height of construction activities, some 5,000 workers lived in camps with primitive facilities. Most workers came from the surrounding hill areas, going back to farming when this activity required their attention. About 20% stayed in Zihuatanejo, largely those at the semi-skilled or skilled level. All inhabitants are now receiving clear titles to their land lots, a first for Mexico and benefiting from water, sewerage, electric and telecommunications services. People have built new houses. The winding streets have been preserved, public laundry areas installed and low cost housing projects started. Community centers and schools now operate, a training institute run by the Mexican Institute for Social Security (IMSS) turns out skilled construction and maintenance workers, small industries are being fostered and a consumer cooperative operates ten stores.

6. FONATUR is also making an effort to create a "host mentality" by organizing a "tourism week" contests for the best local dish, open-house dinner invitations for tourists, instruction in guiding and town clean-up for young boys, training for taxi drivers and boatmen, tourism courses and English language classes at school.

7. The population of Zihuatanejo has more than doubled; it is becoming a city of high physical quality, with increasing social and economic opportunities. It has been an experience in participatory planning for FONATUR and the residents involved. Without FONATUR's community development efforts the land problems would not have been solved as peacefully nor would the construction work have proceeded as rapidly as it did. The local government had neither the financial resources nor the management capacity required to obtain and promote a project of this nature.

III. Plans for Baja California

A. Background

8. The state of Baja California is a sparsely populated state (167,666 people in 1975) which since 1960 has experienced a net increase in population due mainly to immigration from the mainland. Agriculture is the most important activity, although it is beginning to employ less and less people (Table 1, page 4). The state of Baja California fares well when compared to conditions elsewhere in the country. It has a low illiteracy rate (3%), low indices of mortality and morbidity, high indices of health and education facilities per capita; all favorable preconditions for development. These figures, however, do not show the distribution of services among the population, a large proportion of which is concentrated in the capital city of La Paz. It is probable that many small rural communities have far fewer services. Also the distribution of these services among different income groups is not even. Lower income classes, especially in rural areas, are part of a complex socio-economic situation characterized by bad hygiene, insufficient nutrition, and inadequate

housing, water and sewerage facilities.

Table 1. Baja California Labor Force Composition

<u>Sector</u>	<u>Number</u>	<u>% of State Labor Force (1970)</u>	<u>% Change from 1960</u>
Agriculture	12,035	34.5	- 17.2
Manufacturing	2,726	7.8	+ 77.9
Services	6,488	18.6 ^{a/}	+ 56.7
Construction	2,059	5.9	+122.6
Commerce	3,642	10.5	+141.7
Other Activities	7,914	22.7	+ 2.2
Total	34,864	100.0	

a/ Which puts Baja California among the states with a higher than average service sector labor force (in percentages), mostly employed in the tourism sector.

Source: Mexico, Census 1960, 1970.

B. Existing Conditions in the Project Areas

San Jose del Cabo

9. The town of San Jose del Cabo is the center of a group of seven small settlements. The total population of the area including the settlements was estimated at 8,330 in January 1976, of which about half reside in the town of San Jose del Cabo itself. Although the local inhabitants in this area are relatively young (35% are under 13 and 78% are under 28 years of age) and the level of education high (only 0.2% of the adults are illiterate), only 20% of the population is economically active. Sources of income include among others construction, trade and agriculture (Table 2, page 5). The average monthly income per family is Mex\$4,613; approximately 20% of the families earn incomes below the legal minimum wage, with higher percentages for the surrounding settlements.

10. Although a sizeable portion of the family budget is spent on basic necessities, the nutrition of the population of San Jose is not adequate in quality; only 15% of the population gets a complete diet. FONATUR's community development activities could do much to decrease the deficiency in the nutrition and lower the child mortality rate which now results from this situation.

11. Most of the families own their houses (85% of the population) with the remainder paying an average of Mex\$980 per month for rented facilities. Most houses in the town itself are hooked up to the municipal utility systems, i.e., 90% to the water system, 40% to the sewerage system

(which does not work) and 88% to the electricity network. The average cost for water and sewerage services is Mex\$26 monthly. The settlements outside the town do not have adequate utility services.

Table 2. San Jose del Cabo and Loreto
Percentage Breakdown of Persons Employed in Each Sector

	<u>San Jose del Cabo</u> (%)	<u>Loreto</u> (%)
Hotels	3.5	12.6
Commercial activities	10.6	12.6
Construction	16.9	11.3
Domestic servants	3.5	2.8
Agriculture, fishing, animal husbandry	10.6	29.6
Public services	8.4	11.3
Government employment	14.1	11.3
Other	32.4	7.0
Craftsmen	--	1.5
Total	100.0	100.0

Source: FONATUR Survey, January 1976.

12. San Jose del Cabo has several schools and shops which classify it as a small urban center. The health facilities include a health center with 18 beds, and a consulting room run by the Mexican Institute for Social Security. San Jose del Cabo has many labor unions and professional associations, several banks and a local Chamber of Commerce. Social organizations include PTA's, INPI women's club and committees for material improvement of the town. The family unit, nucleus of all social organizations, is rather unstable at the lower-income level.

13. Tourism is fairly well developed along the coast between Cabo San Lucas and San Jose del Cabo. In San Jose del Cabo itself only 3.5% of the people work in hotels and restaurants, but tourism activities are increasing with the opening up of souvenir shops, boat rental facilities, and a black coral jewelry workshop. Also, people from the communities close to Los Cabos migrate during the tourist season to work in hotels (e.g., in La Ribera, Santiago and Miraflores 26%, 4.4% and 5.6% respectively of the economically active population are engaged in the tourism sector).

Loreto

14. Loreto, a fishing community of 3,176 inhabitants (January 1976) or about 590 families, is poorer and much less developed than San Jose del Cabo. Half of the population (49.6%) is under 13 and two-thirds is under 28 (66.8%). Twenty-three percent of the population is economically active.

Many of the young people migrate to La Paz in order to earn a living; the remaining population works mainly in agriculture and fishing (30%). Construction, hotels, shops and public services provide other sources of employment (Table 2). The average monthly income per family is Mex\$ 3,480. About 35% of the income earners earn less than the legal minimum wage, and about half of those work in the agricultural sector. Ninety percent of the population owns their own house and the other 10% pays an average of Mex\$510 per month for rent.

15. Loreto has a municipal water supply system serving 89% of the houses. The water is chlorinated and free of disease-spreading organisms. There is no sewerage system, but 45% of the houses have an individual septic tank and 52% have a latrine. Electricity reaches 95% of the houses. Garbage collection is frequent and garbage is burnt outside the village.

16. Loreto has two kindergartens and nursery schools, two primary schools, one secondary school and a preparatory school. There is a boarding school for the children of farmers living outside the village. The villagers themselves participate actively in the construction and maintenance of the schools. Basic necessities are sold in 16 little shops. Loreto has two hotels (100 rooms). The town has a health center, which is adequate to serve the local population. The Catholic church represents a very strong factor in the social life of Loreto. Several associations of taxi drivers, truck drivers, cattle raisers and a cooperative of fishermen complete the social picture of Loreto. It is a community which is still very cohesive with strong multiple social ties between its members. The community is very alert to the opportunities which arise from present day tourism, particularly to the creation of local employment opportunities.

C. Project Design and Impact

17. The proposed project is designed in such a way that the local populations of San Jose del Cabo and Loreto should reap the benefits of tourism development as much as possible, while adverse effects as far as they can be foreseen, will be limited. The proposed projects are basically well conceived integrated tourism-urban development, but have been planned from the top down. Experience in Zihuatanejo has shown the need to involve the population at an early stage; this need has been partially met by keeping the population of Loreto and San Jose del Cabo informed about the proposed investment activities at a much earlier stage than in other projects, by starting community development activities before initiation of project implementation. Doing more than this is not feasible in Baja California. The local governments are not in a position to be "partners" to FONATUR. Instead, FONATUR's answer has been to create community development teams, staffed by capable and sensitive people who are bound to lessen the adverse impacts of rapid urban development.

Increase in Population

18. With the implementation of the project, the populations of San Jose del Cabo and Loreto are expected to grow to 50,000. Baja California should have no problem finding workers; it presently has few service sector workers but can draw people into the service sector from its own hinterlands. The investments would cause expansion in construction employment and could effectively increase the labor force in the service sector without stimulating immigration. However, migrants would still be attracted and most migrants would originate in the states of Michoacan, Oaxaca, Jalisco (states with a low per capita income and a large agricultural population) or come from Sonora and Sinaloa (also states with a large population which are connected by ferries to the peninsula).

19. Experience in Cancun and Zihuatanejo show that three distinctive phases in the growth of population can be expected. During the construction phase, a large number of temporary migrant workers (without their families) would come to the development areas, creating demand for housing and other services. Many of the construction workers would be housed in labor camps or other temporary quarters; others would require more permanent housing. Generally, a core of skilled or semi-skilled workers travel from job to job with the construction companies. Some of the unskilled labor, however, will be recruited in the area. This construction activity would increase employment opportunities for the existing population. FONATUR has prepared a construction schedule which estimates the requirements for manpower of various skill levels for each month. It intends to require contractors to hire as many local workers as possible, particularly since it will alleviate some of the suffering caused by the recent earthquake. FONATUR also intends to enforce strict adherence to the labor law regulations prescribing adequate labor camp conditions.

20. The second growth phase would commence with the operation of the hotels and other facilities. Again, the higher management levels would come from other places in Mexico, but middle and lower skilled staff could be hired from the region, especially if the hotel training school in La Paz operates satisfactorily. Indirect employment will begin to be generated as demand for products and services increase, particularly from the agricultural sector. In this phase it is expected that families, rather than individuals, would settle in both towns.

21. A third phase of immigration would start when the resort is established. A distinctive group, with higher income levels (for example, retired people) would either settle in the two areas or use the facilities during weekends or vacation periods.

Ejidos

22. Much of the land in Baja California belongs to ejidatarios. The role of the ejidos is a very special one in tourism development in Mexico. For historic reasons ejidatarios legally have the power to decide whether or not a tourism project will be allowed to develop on their land. This

gives them an important role and place in their own community, singling them out as a group which, temporarily, influences the direction of development for the whole community and gives them more power than other members of the population and municipal authorities. Receiving monetary payments and free developed urban lots as part of the compensation package, also singles them out as the first group which will benefit economically from the new tourism developments. All these factors lead to change in socio-economic structure in the community. A new class emerges for the relatively short time when the community still has its original size and structure. Later, the ejidatarios become less important, especially if they continue to be farmers and fishermen, and do not become investors or operators in the tourism sector. Some may, because training of ejidatarios will take place as part of the compensation measures.

23. Ejido members form a relatively small part of the population in Loreto and live apart in one part of town. They earn their living from fishing rather than agriculture; in San Jose del Cabo, they are less centralized and earn their living from agriculture and fishing. The 350 ejidatarios in San Jose del Cabo would receive a sum of Mex\$31.2 million in compensation which will make them a relatively rich group in the community. The same situation occurs in Loreto; a group of 60 ejidatarios will receive Mex\$13.1 million in compensation. Not all of the compensation will be in cash. Ejidatarios in Loreto will receive Mex\$4 million and those in San Jose del Cabo, Mex\$6.2 million at the time the presidential decrees are executed and the trust funds formed. The other part of the compensation will be paid over a period of three years, and will consist of 2 developed urban lots per family, and the starting of enterprises which will be run by and for the profit of ejidatarios. The decisions of the ejido assemblies to vote in favor of expropriation reflect, in part, FONATUR's effort to involve and inform the ejidatarios about the planned developments from the early stages on. Also some trips to Zihuatanejo helped to prepare the ejidatarios better to understand what was meant by tourism development.

Project Plans

24. In order to cope with the impact of the projects on the existing communities and plan for the orderly growth in population, several measures will be taken.

(1) Housing: A deficit of houses, both in terms of quantity and quality, is prevalent in the whole country and especially in rural areas. Several Government programs have been developed to assist the development of housing. Beneficiaries of housing loans in public programs have to fulfill the following conditions: (1) not be the owner of a housing unit in the same city; (2) be head of a family; and (3) meet credit requirements. This last condition varies per program but in most cases it means that the incomes have to be over or at the level of the legal minimum salary. INFONAVIT is the only exception; 10% of the credits of INFONAVIT are destined to families earning less than the legal minimum salary.

Approximately 65% of the population who are not formally employed or do not receive regular incomes, do not qualify for current housing programs. The rural sector is almost completely excluded from these programs, partly because in the urban areas unions are in a much stronger position to obtain housing assistance. Attitude studies have shown that people in the "popular" sector consider a house in itself to be less important than the availability of basic services (water, sewerage, electricity) and the security of tenure of the lot on which their house is built.

Table 3. Expected Distribution of Family Income Levels in Baja California by 1983

Income Mex \$	% Population	Estimated Monthly Income to be Spent on Housing		Housing Program	
		%	Mex\$	Sites and Services	
		0 - 600	12.0	0 - 72	INFO-
600 - 1,200	9.0	12.5	73 - 150	NAVIT	Private
1,200 - 2,000	27.0	15.0	151 - 300		Banks
2,000 - 4,000	38.0	15.0	301 - 600		
4,000 - 6,000	12.0	17.0	601 - 1,020		
6,000 - 10,000	8.0	19.0	1,021 - 1,900	FOVI	
10,000 - 15,000	2.5	20.0	1,901 - 3,000		
Over - 15,000	1.5	20.0	Over 3,001		

25. The Baja California tourism project calls for the provision of housing or other facilities for population of all income levels. FONATUR will sell urbanized lots with a 5 year repayment period and 12% interest, with private banks acting as intermediaries providing purchase, construction or mortgage loans. In addition, FONATUR plans to promote construction of houses by the public and private sector. For the private sector this would consist of private contractors putting up uni-family and multi-family units and making them available for sale or rent. Public organizations would participate by extending loans to those who are eligible under their programs or by directly building the houses. FOVI is expected (as in Cancun) to construct houses which will sell for Mex\$120,000 (US\$6,000), which with 15 or 20 years repayment period at 10% will require monthly payments of respectively Mex\$1,280 or Mex\$1,150 per month. FONATUR also plans to follow the same procedure as followed in Zihuatanejo, i.e., construct houses and turn them over to INFONAVIT to select the families who are eligible for them.

26. (2) Sites and Services: Provision has been made under the project to care for approximately 30-35% of the population which will not be eligible for any housing program, public or private (see Table 3). In order to avoid the development of shanty town settlements, the project will make available 500 lots of 150m² each in both Loreto and San Jose del Cabo. The lots will be distributed among several blocks in town, to avoid clustering of low income groups and social stigmatization. The lots will be provided with water taps (one for ten lots), roads and electricity. Each lot will also be provided with a simple toilet system. The cost of these facilities will be Mex\$10,000 (US\$500) per lot. FONATUR, which is not expected to

recover the full investment costs of the sites and services plots, would design a payment system that would not be a burden and under which rent payments would count toward the purchase price. The project will provide for technical assistance through the community development organization to help these families construct their own houses with materials made available at cost. A plan for provision of credits for construction materials (in a rotating credit fund) will be drawn up. Flexibility in housing design to meet the needs of the families will be one of the criteria for the auto-construction program. All services including treated water, sewerage, electricity and garbage collection will be provided under the project. The rates would be set at a level which most families can afford; for the sites and services, the rates would be subsidized by FONATUR.

27. (3) Temporary Accommodation: In order to avoid a shortage of housing and the resulting exorbitant prices charges for services, FONATUR plans to make provision for proper temporary facilities to be financed under the community services program. The final arrangements for leasing or operating this facility are being drawn up.

28. (4) Training: Measures have been taken under the project to construct a training center in each town. These centers would be operated by the Mexican Institute of Social Security (IMSS) and would train people such as carpenters, masons, electricians, and air-conditioning and refrigerator mechanics. The promotion of these centers partly compensates for the expropriated ejido land and is meant especially to give children of ejidatarios a new profession. The ejidatarios will also (as part of their compensation) become owners of small industries (e.g., cement and ice factories). Training in management of these small enterprises would be provided as part of the pre-opening costs of the project.

29. (5) Social Services: The project would create several social amenities for the growing population. New schools and health centers are integrated in the urban plans. A nursery for pre-school children will be built in both towns to give mothers an opportunity to earn a living; these nurseries will be operated by the state. Other schools would be built and operated by state and federal governments, while health centers would have to be operated by the state health authorities.

30. Under the project a community development team would be set up by FONATUR. Based on experiences in other projects, this organization would be responsible for ensuring a smooth transition and growth of primarily rural communities to modern urbanized service towns for tourism, with maximum benefits and participation of the local population in this process. This entails the following activities:

- (a) during the first phase of the tourism development the community development team will participate in the land expropriation procedures, advise people on how to reinvest compensation money, advise on construction of new houses, and promote training and control conditions in the labor camps;

- (b) during the second phase, it will promote and participate in the formation of many community services, e.g., consumer and producer cooperatives and associations, environmental hygiene; and
- (c) in the third phase, its role diminishes to a tourist community development organization and its activities will be to educate tourists and the host population about each other, train the local inhabitants in tourism activities and organize activities for tourists and population.

31. FONATUR plans to create a team for each town; approximately one professional for every 350 families. The project would finance housing and transport for this team. Experience has shown that early introduction of community development efforts is important. These activities started in Baja California in 1976.

32. (6) Linkages to the Agricultural Sector: FONATUR will, as part of project activities, estimate needed quantities of agricultural produce. These estimates have been made for FONATUR's other projects and will be based on consumption habits of tourists and the urban population. FONATUR will present a plan for the use of recycled sewerage water for irrigation purposes to the Bank. The estuary area in San Jose del Cabo is in a semi-arid countryside, an ideal place for agricultural production, especially for perishable crops like fresh vegetables. FONATUR would cooperate with other government organizations which already foresee investments and training in hydroponic vegetable production for the development of date orchards in Loreto and citrus, papaya and avocado orchards in San Jose del Cabo.

D. Conclusions

33. If tourism development is well planned, the level of available services to the local population is much higher than would have been the case without proper planning. Concomitant urban development leads to better houses, availability of infrastructure, hospitals, schools and other urban services. The non-incorporated segments of the population (rural and informal urban sectors), however, do not benefit from these services unless special arrangements are made (e.g., health clinics, sites and services), as done under the project. Unplanned industrial and urban development leads to higher land prices and speculation, attracts migration for which no proper provisions are made in housing, physical and social infrastructure, leads to resentment on the part of the original population toward newcomers if the original population tends to become submerged, and leads to the development of a new social structure, new classes and problems. All these foreseeable adverse effects of "boom-towns" have been forestalled as much as possible in the Baja California tourism project by proper advance planning.

34. The social impact of the project can be valued in several ways. The immediate impact on the communities will be the short-lived emergence of the ejidatarios as an important social group. The second and positive impact will be caused more directly by the changes in the urban environment brought about by the project, i.e., a better, safer and healthier environment (water, sewerage, well-constructed houses for each income group, electricity, etc.), more opportunities to learn a profession and earn a living in the two towns themselves, instead of having to migrate to other towns or the mainland and relatively high incomes for those working in the tourism sector.

35. The negative impact for the existing towns will be caused by rapid urban development. This rapid urban development in basically rural communities will bring about many changes for the present local population: the social structure of the village will undergo changes, new classes will develop, new economic and social power relationships will emerge, and new social organizations, formal and informal, will be formed. Experience elsewhere suggests that communities which are cohesive and have multiple overlapping social networks are better able to cope with changes in their environment and lifestyle. In that sense, Loreto, a more cohesive, more rural community, is probably better equipped to cope and adapt to the new environment and take advantage of the opportunities than San Jose del Cabo, which is already partially urbanized.

36. The impact of tourism, however, will not be known immediately. Both communities now attach a positive value in their attitudes towards tourists and tourism as a means for development of their community and as a means of earning or increasing their incomes. Community development activities would have to further this positive feeling and guide the population toward realistic expectations of the benefits and develop pride in the population in being a host and support community for tourism. Generally speaking, the impact of foreign visitors to the project areas (largely from the US) is not likely to affect changes in value systems in scope or direction, other than those already occurring in the present day Mexican society. In fact the influx of international tourists could bring about, as in the rest of Mexico, a much stronger and deeper appreciation of the national cultural heritage.

37. Careful monitoring by the community development teams will be crucial in detecting and solving potential problems. Two forms of monitoring of the developments in the communities and in the project areas have been foreseen in the project. FONATUR would continue to hold annual or semi-annual surveys of the socio-economic situation of the population. These data would support the day-to-day monitoring activities of the community development team. Secondly, the community development team will be represented in the board of the trust funds that will manage investment activities in the areas. Part of the costs of the monitoring activities are included in the project.

MEXICOAPPRAISAL OF THE
BAJA CALIFORNIA TOURISM PROJECTENVIRONMENTAL ASPECTS

1. The peninsula of Baja California is a fascinating and intriguing predominantly desert biome which seems dead and sterile, but which is, in fact, abundant with webs of life in complex and little understood eco-systems. Baja California's attractions include a dry warm climate, clear blue waters, beautiful beaches, towering mountain ranges (including ancient rock paintings in caves), deserts with innumerable cacti (110 known succulent species, about 60 of them endemic), flowers and trees such as the elephant tree and the bizarre Bojuum or Cirios tree, and some of the world's richest maritime fauna (more than 1,000 species, including marlin, whales, dolphins, sailfish, sharks, yellowtails, giant squids, and octopi). The environmental adaptation of fauna and flora is especially remarkable due to eco-isolation resulting in numerous endemic, indigeneous species. Because of its inaccessibility and its desert climate (only 61 mm of average annual rainfall), human development efforts have been limited. The soil conditions have further hampered development and where permanent water sources are available (the Colorado River), salinization is affecting the agricultural potential.
2. The delicate environment described above could be upset for a variety of reasons, including indiscriminate, unplanned human interference. The already constructed transpeninsular highway could result in erosion, pollution and environmental impoverishment particularly when traffic volumes increase. There is also the potential danger of indiscriminate development having a detrimental impact on fish and bird life in the Sea of Cortez.
3. Another danger is posed by the scarcity of water in the peninsula. All developments should be reviewed in light of their future water needs since underground water reservoirs limit the peninsula's capacity for development. Too much depletion of the water resources has already led to salinization of the fertile valley of St. Domingo, and several areas in the north of the peninsula.
4. The Mexican Government realizes the importance of environmental protection. A sub-secretariat for these matters has been created. The governments of Mexico and the US plan a joint study on the impact of the recently completed highway on the environment. Several federal agencies are involved in different aspects of environmental policies on the peninsula. Certain plants have been put on a "protected list" and only limited exploitation is allowed. Hunting of wild sheep is being regulated and is allowed

only during certain seasons. National parks have been established on the peninsula by the Secretariat of Human Settlements and Public Works in nine zones^{1/} and by the Secretariat of Agriculture and Hydraulic Resources in two additional places (Constitucion de 1857 and San Pedro Martin). The lagoon of San Jose del Cabo and the extreme point of Cabo San Lucas are among them, as well as several bays where the gray whales mate. The state government, conservation institutes, and the Secretariat of National Patrimony collaborate on research and funding of conservation activities. An integrated environmental policy for the whole peninsula however has not been formulated, nor is enforcement of the existing decrees and regulations very effective.

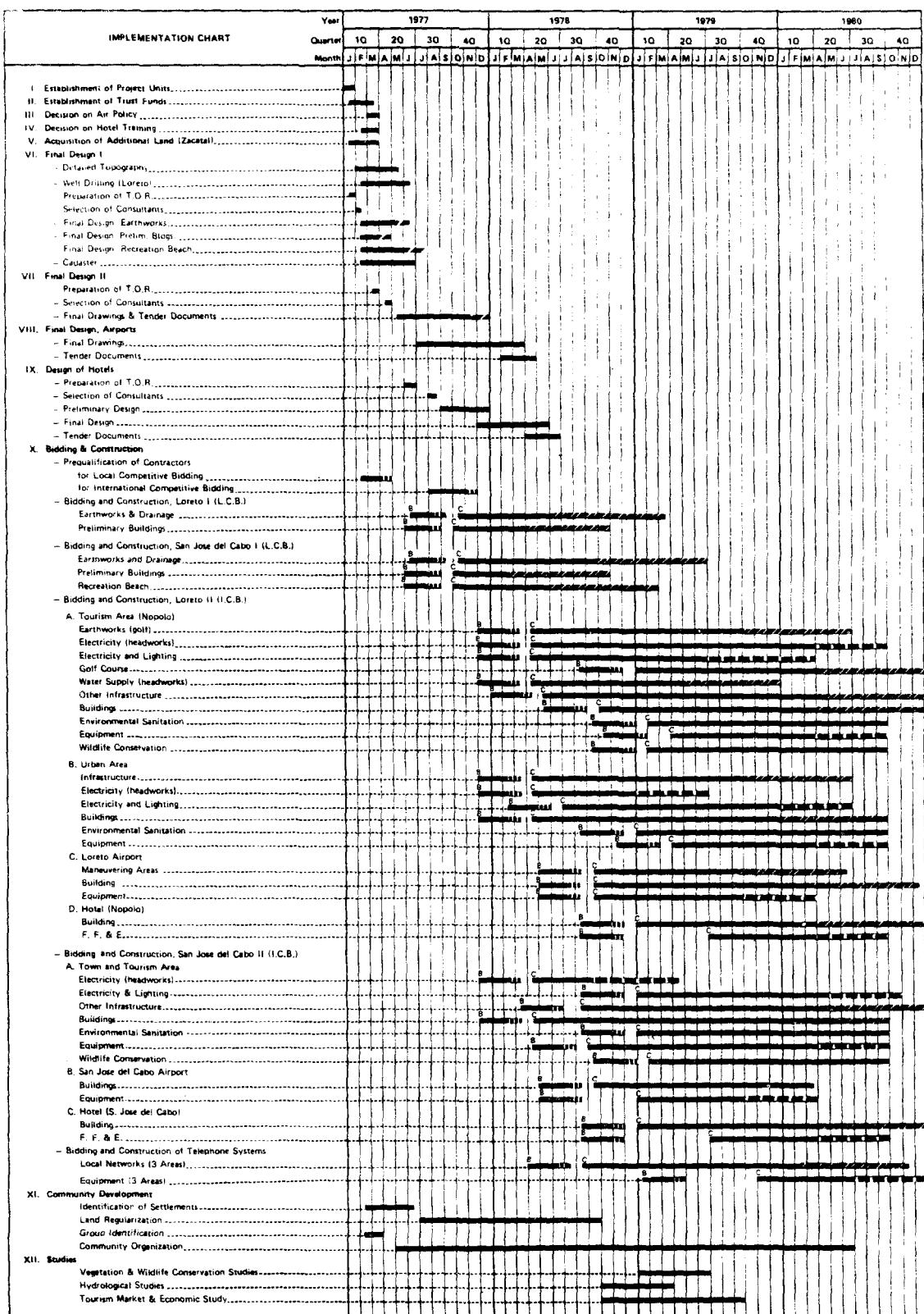
5. In the design of the project, great care has been exercised to preserve natural environment as much as possible (Annex I): there will be minimum disturbance of existing vegetation and green zones; natural ground cover will be planted where needed; no construction will be allowed on primary, secondary and tertiary dunes which can easily shift during bad weather; the oasis near Nopoló will be preserved; the sweet-water lagoon in San Jose del Cabo will be cleaned and dredged; a water management study will be undertaken that will recommend ways to protect the lagoon in San Jose del Cabo and help recharge the aquifer; other studies, financed under the project, will aim at classifying all fauna and flora material in the project areas and make recommendations on the conservation; and lastly, all waste-water will be recycled and be used for irrigation purposes.

6. In summary, the proposed project, as planned, is a fine example of resources management for the benefit of the population, and will not result in undue harm to the environment. It is in keeping with the objectives of local authorities, who favor a balance between development needs and the need to conserve the environment. There are environmental risks to the project. The local climate can be harsh and difficult to cope with. For more than four centuries people have attempted to subdue the peninsula. The peninsula is adjacent to the San Andreas fault line and thus geologically active. Cyclones, locally referred to as "chubascos" often reach full hurricane strength and although most dissipate their energies elsewhere to the south and west in the Pacific, some hit the peninsula. FONATUR, however, is well aware of the environmental issues and all existing records on hurricanes, seismic activity, climatic and geohydrologic conditions have been considered in choosing the project locations and designing the project components.

1/ Cabo San Lucas, the extreme point; Lagoon of San Jose del Cabo; Sierra de la Laguna; Isla de Espíritu Santo; Zone of Punta Chinato; Lagoon of St. Ignacio; Lagoon of Ojo de Liebre, Sierra de S. Francisco and the paleontological zone of La Custre de S. Francisco.

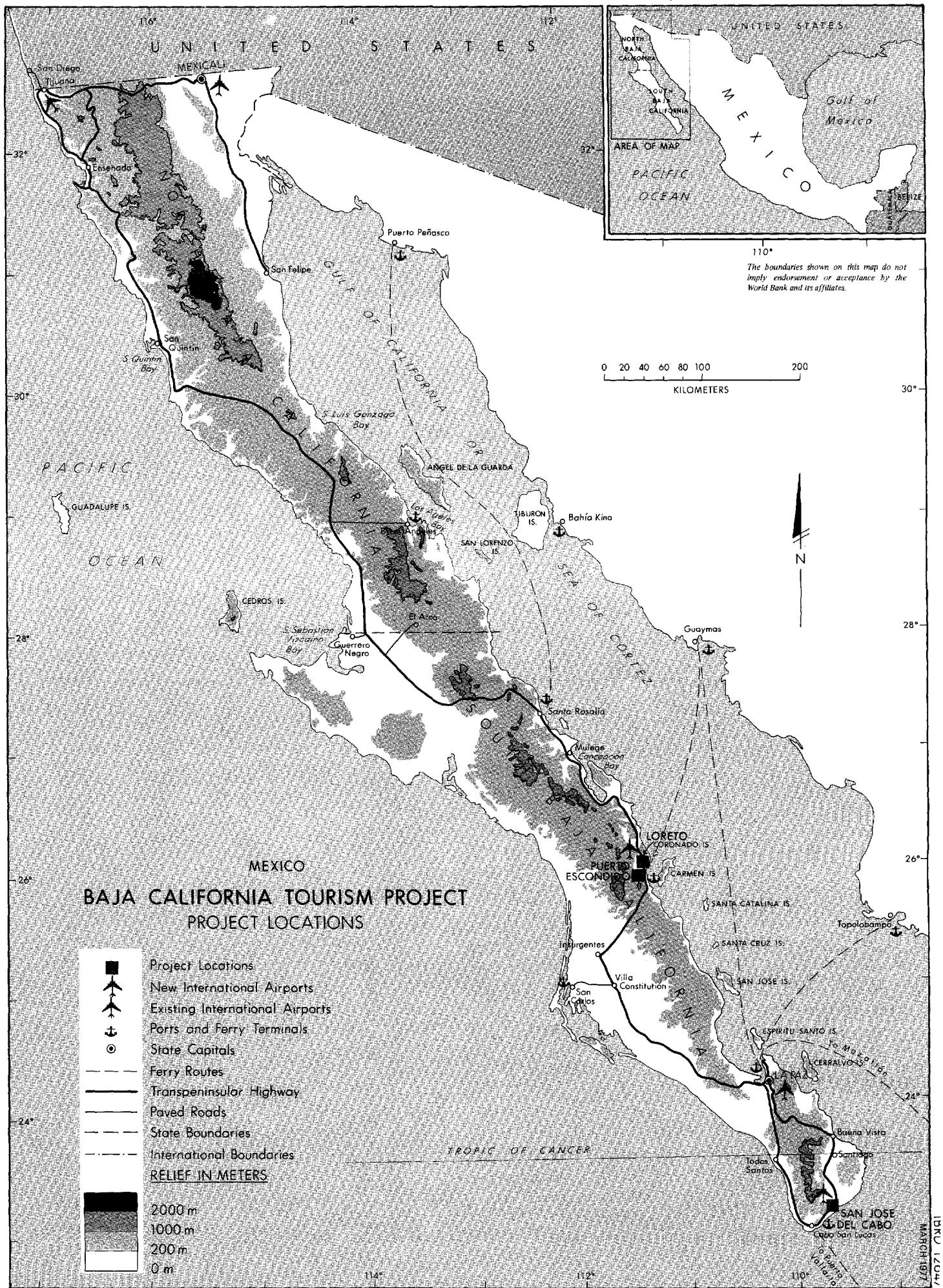
MEXICO: BAJA CALIFORNIA TOURISM PROJECT

SCHEDULE OF IMPLEMENTATION

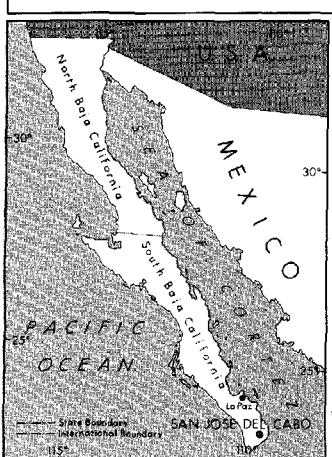
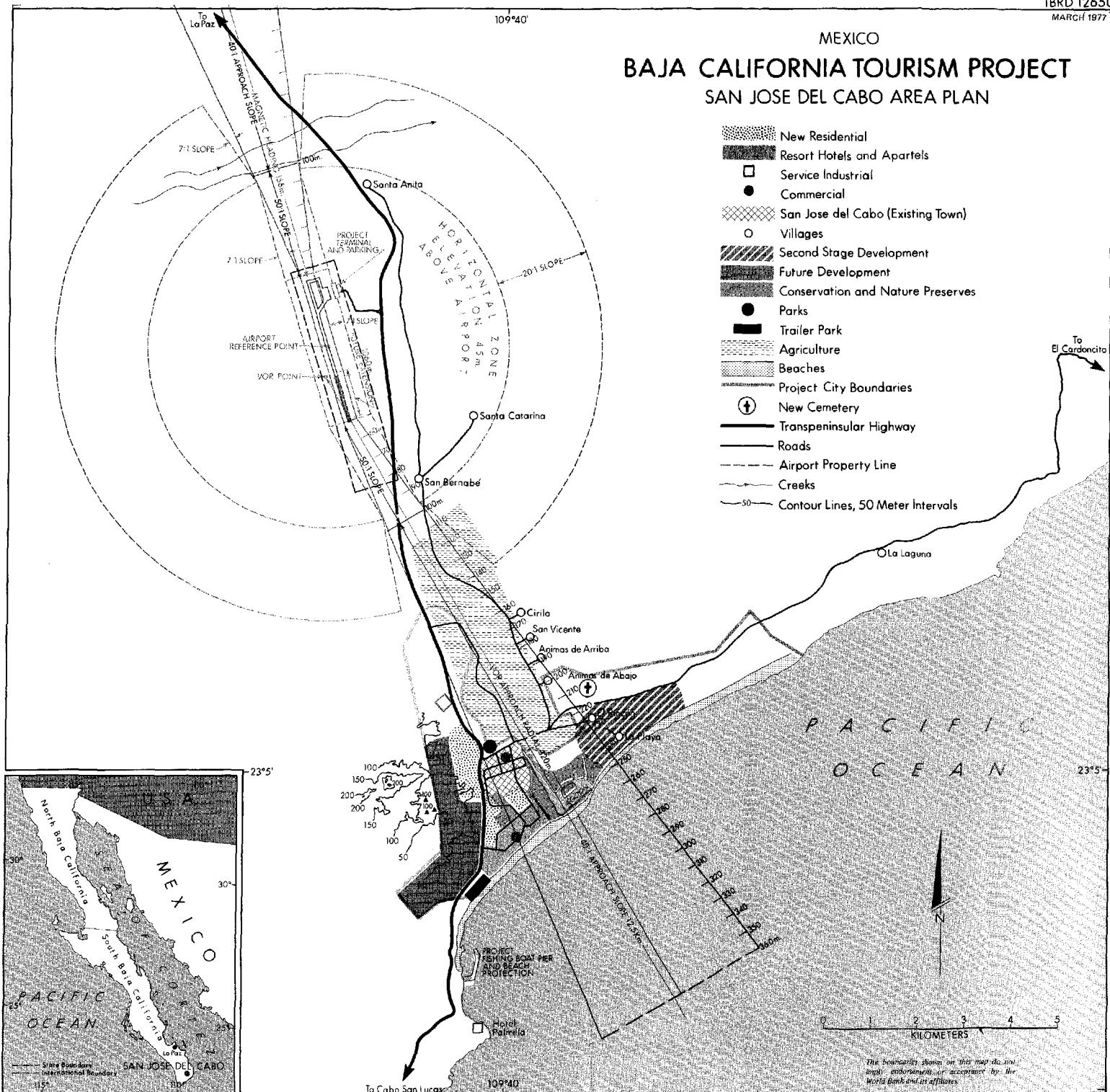


Date of Loan Agreement

ESTIMATED QUARTERLY EXPENDITURES & DISBURSEMENT (in '000 US Dollars)	1977				1978				1979				1980				TOTAL
	-20	-10	10	20	30	40	50	60	70	80	90	100	110	120	130	140	
QUARTERLY TOTALS	Expenditure	1,835	1,854	4,044	4,048	3,293	3,295	7,069	7,073	7,073	7,075	7,775	7,787	7,779	3,390	2,771	83,946
	Disbursement	1,266	1,905	1,937	1,360	3,707	3,710	3,849	3,912	4,105	4,373	4,339	4,				



MEXICO
BAJA CALIFORNIA TOURISM PROJECT
SAN JOSE DEL CABO AREA PLAN



MEXICO
BAJA CALIFORNIA TOURISM PROJECT
SAN JOSE DEL CABO LAND USE PLAN

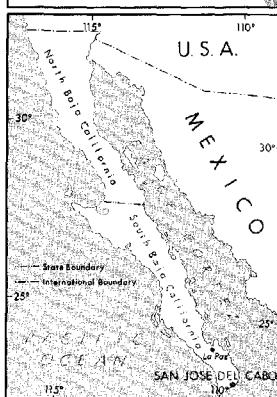
A horizontal scale bar labeled "METERS" with numerical markings at 0, 100, 200, 400, 600, and 800.

2

This figure is a map of the Andean region, specifically the central Andes from approximately 10°S to 23°S. It shows the distribution of two genera: Chusquea (stippled areas) and Puya (hatched areas). Contour lines indicate elevations of 50, 100, and 23°S. Key locations labeled include La Paz at the top right, Chuquicamata near the center, and Cerro de Pasco at the bottom right. The map also shows the outlines of several countries: Chile, Argentina, Bolivia, and Peru.

A detailed black and white map of a coastal or riverine landscape. The map shows a large body of water on the right, a river flowing from the center-left towards the bottom, and several smaller streams and inlets. A prominent, dark, irregularly shaped area in the center-right is labeled 'LOOK OUT POINTS' with an arrow pointing to it. In the bottom-left corner, there is a small rectangular icon representing a signpost, with the words 'OLD BATTERY' written on it. The map uses various hatching patterns to distinguish different land types or ownership. A coordinate reading '23°51' is visible in the top right corner.

The boundaries shown on this map do not imply endorsement or acceptance by the World Bank and its affiliates.



This detailed map of Cabo San Lucas illustrates various urban planning and geographical features. The map includes labels for the Pacific Ocean, Cabo San Lucas, and Trailer Park. A legend on the right side provides a key to symbols and features:

- Limit of First Stage Development**: Represented by a dashed line.
- Second Stage Development**: Represented by a dotted line.
- Future Development**: Represented by a diagonal hatched pattern.
- Resort Hotels**: Indicated by diamond symbols.
- Condominium Apartments and Villas**: Indicated by small dots.
- Single Family Villas**: Indicated by a cross-hatch pattern.
- Apartels**: Indicated by a vertical hatched pattern.
- Urban Renewal Area**: Indicated by a light gray shaded area.
- Parks**: Indicated by a dark gray shaded area.
- Recreation Centers**: Indicated by a diagonal hatched pattern.
- Sites and Services**: Indicated by a horizontal hatched pattern.
- Ejido Resettlement**: Indicated by a light gray shaded area.
- Beach Protection Zone**: Indicated by a diagonal hatched pattern.
- Commercial**: Indicated by a solid black circle.
- Project City Boundaries**: Indicated by a thick dashed line.
- Existing Town Boundaries**: Indicated by a thin dashed line.
- Transpeninsular Highway**: Indicated by a thick solid line.
- Main Avenue**: Indicated by a thick solid line.
- Secondary Roads**: Indicated by a medium solid line.
- Pedestrian Walkways**: Indicated by a thin solid line.
- Contour Lines in Meters**: Indicated by a thin line with numerical labels (e.g., 50).
- Highest Points in Meters**: Indicated by a triangle symbol with a numerical label (e.g., ▲75).

MEXICO

BAJA CALIFORNIA TOURISM PROJECT
LORETO AREA PLAN

