



Board of Executive Directors

For consideration

On or after 1 December 2010

PR-3643
12 November 2010
Original: Spanish

To: The Board of Executive Directors
From: The Secretary
Subject: Honduras. Proposal for a loan for the “Puerto Cortés Expansion and Modernization Program”

Basic Information: Loan type Specific Investment Operation (ESP)
Borrower *Empresa Nacional Portuaria*
Amount up to US\$94,500,000
Source Single Currency Facility of the Ordinary Capital
Amount up to US\$40,500,000
Source Fund for Special Operations

Inquiries to: Esteban Diez (extension 3890) or Néstor Roa (extension 1829)

Remarks: The loan amount for this operation exceeds the ceiling established for Group D countries; therefore, it does not qualify for approval by simplified procedure.

The financing for this operation corresponds to a parallel loan within the framework of the multilateral debt relief and concessional finance reform of the Bank.

Reference: GN-1838-1(7/94), DR-398-9(9/10)

HONDURAS

PUERTO CORTÉS EXPANSION AND MODERNIZATION PROGRAM

(HO-L1037)

LOAN PROPOSAL

This document was prepared by the project team consisting of: Esteban Diez (INE/TSP), Project Team Leader; Rafael Acevedo (INE/TSP); Néstor Roa (INE/TSP); Giovanna Mahfouz (INE/TSP); Trinidad Zamora (TSP/CHO); René Herrera (CID/CHO); Miguel Orellana (CID/CHO); Esteban Sarzosa (SCF/INF); María Cristina Landázuri (LEG/SGO); and Roberto Suárez (consultant).

CONTENTS

PROJECT SUMMARY

I.	DESCRIPTION AND MONITORING OF RESULTS	1
A.	Introduction.....	1
B.	Background, problem, and rationale	1
C.	Objective, components and costs.....	4
1.	Objective.....	4
2.	Components.....	4
3.	Costs.....	6
D.	Results Matrix and Principal Indicators (PPMR monitoring).....	8
II.	FINANCING STRUCTURE AND MAIN RISKS	8
A.	Financing instrument.....	8
B.	Environmental and social risks and mitigation measures.....	8
C.	Fiduciary risk.....	9
D.	Other issues and risks.....	10
III.	IMPLEMENTATION AND ADMINISTRATION PLAN	11

ANNEXES

Annex I	Development Effectiveness Matrix (DEM)
Annex II	Results Framework
Annex III	Procurement Plan Summary

ELECTRONIC LINKS

Required	
1.	Implementation plan http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=2033912
2.	Monitoring and evaluation procedure http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=2010688
3.	Procurement Plan http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=2010815
4.	Environmental and social management report (ESMR) http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=2009544
5.	Safeguard Policy Filter Report and Safeguard Screening Form http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=35387982
Optional	
1.	Economic viability http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=2030400
2.	Independent Financial & Market Review of Puerto Cortés http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=2030478
3.	Independent Financial & Market Review of Puerto Cortés (Addendum) http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=2030433
4.	Due diligence on the Puerto Cortés project http://idbdocs.iadb.org/WSDocs/getDocument.aspx?DOCNUM=2030568

ABBREVIATIONS

AWP	Annual work plan
CABEI	Central American Bank for Economic Integration
DSCR	Debt service coverage ratio
EIRR	Economic internal rate of return
ENP	Empresa Nacional Portuaria [Honduran Port Authority]
ENPV	Economic net present value
EPC	Engineering, procurement, and construction
GEF	Global Environment Facility
MARPOL	International Convention for the Prevention of Pollution from Ships
MCF	Management consulting firm
PCU	Project Coordination Unit of the ENP
PPMR	Project Performance Monitoring Report
SOPTRAVI	Ministry of Public Works, Transport, and Housing
Tb	Time at berth
TEU	20-foot equivalent unit (measure of container carrying capacity)
Tw	Waiting time

PROJECT SUMMARY

HONDURAS PUERTO CORTÉS EXPANSION AND MODERNIZATION PROGRAM (HO-L1037)

Financial Terms and Conditions					
Borrower: Empresa Nacional Portuaria (ENP) Guarantor: Republic of Honduras Executing agency: ENP				OC	FSO
			Amortization period:	30 years	40 years
			Grace period:	6 years	40 years
			Disbursement period:	4 years	4 years
Source	Amount (US\$)	%	Interest rate:	Fixed	0.25%
IDB (FSO)	40,500,000	17.97	Inspection and supervision fee:	*	N/A
IDB (OC)	94,500,000	41.92	Credit fee:	*	N/A
CABEI	90,000,000	39.93	Currency: (FSO) U.S. dollars and (CO) Single Currency Facility		U.S. dollars
Local	415,000	0.18			
Total	225,415,000	100			
Project at a glance					
Objective/description:					
<p>The general objective of the program is to enhance the capacity and efficiency of operations at Puerto Cortés, reducing costs for foreign trade and thereby contributing to the sustainable economic and social development of Honduras. To this end, the program will include civil works to expand the capacity of port infrastructure and equipment, and activities to strengthen the institutional performance of the ENP.</p>					
Special contractual conditions:					
<p>(a) <u>precedent to the first disbursement</u>: (i) selection and contracting of the management consulting firm to support the program (paragraph 3.3); (ii) establishment and startup of the Program Coordination Unit (paragraph 3.3); and (iii) signature and entry into force of the CABEI financing contract (paragraph 2.7); and (b) <u>during program execution</u>: (i) the commencement of any civil works would be conditional upon contracting the corresponding supervisory services (paragraph 2.6); (ii) prior to awarding a contract for: (1) expansion of the port terminal, presentation of the action plan for managing social, environmental and health and hygiene considerations (paragraph 2.5); (2) purchase of equipment for the container terminal, presentation of the preventive maintenance plan and evidence that funds had been budgeted for that plan (paragraph 2.12); and (3) dredging and land reclamation works, evidence that the firm in charge of performing the environmental and social audit has been selected and hired (paragraph 3.14); and (iii) maintain a debt service coverage ratio of at least 1.0 throughout the program execution period and present annual reports on compliance with this condition (paragraph 3.11).</p>					
Exceptions to Bank policies:					
<p>As indicated in paragraph 3.6, the project team recommends that member countries of CABEI that are not members of the Bank be allowed to participate in the procurement of goods, works, and consulting services to be financed by the Bank and by CABEI, recognizing the need to harmonize IDB and CABEI procurement policies in order to maintain the pari passu financing of procurement.</p>					
Project consistent with country strategy: Yes [X] No []					
Project qualifies as: SEQ [] PTI [] Sector [] Geographic [] Headcount []					

* The credit fee and inspection and supervision fee will be established periodically by the Board of Executive Directors as part of its review of the Bank's lending charges, in accordance with the applicable provisions of the Bank's policy on lending rate methodology for Ordinary Capital loans. In no case will the credit fee exceed 0.75% or the inspection and supervision fee exceed, in a given six-month period, the amount that would result from applying 1% to the loan amount divided by the number of six-month periods included in the original disbursement period.

I. DESCRIPTION AND MONITORING OF RESULTS

A. Introduction

- 1.1 Puerto Cortés is the main port of Honduras and handles almost 90% of maritime traffic. It is located on the northeast coast of the country, on the Caribbean Sea. It is the biggest and deepest port in Central America, with 1,000 meters of main piers and a depth of 12 meters, handling 8 million tons of cargo a year. It is classified as a “safe port.”¹ The port is connected to the principal cities of Honduras by Highway CA-5, which is part of the so-called Atlantic Corridor.² Once Puerto Cutuco in El Salvador is operational, the plan is to develop a 370-km interoceanic “dry canal” (Logistical Corridor) along the Atlantic Corridor, linking it to Puerto Cortés.
- 1.2 The efficiency of Puerto Cortés has a major impact on the economy of Honduras. In the first place, the port is the gateway for the import of inputs for, and the export of products from, the industrial zone around the city of San Pedro Sula, located 60 km from Puerto Cortés. Secondly, the State-owned port is the main point of entry for imports of grains and fertilizers,³ among other goods essential to the country’s economy.

B. Background, problem, and rationale

- 1.3 Apace with the expanding foreign trade of Honduras, Puerto Cortés has been handling growing volumes of cargo. The Empresa Nacional Portuaria (ENP), the government port authority that manages Puerto Cortés, has attempted to adapt to the growing volume of operations by making minor improvements to basic infrastructure⁴ and purchasing equipment, but without expanding berthing facilities or warehousing space.
- 1.4 Consequently, with only 1,000 meters of piers—essentially this offers berthing space for only four modern vessels—Puerto Cortés is today showing obvious signs of congestion, due to the shortage of berthing spaces and obsolete operating systems that keep productivity low. These constraints become especially obvious in the handling of containers (which represent the preponderance of cargo in a modern port) and bulk cargo. More specifically: (i) the port handles 300,000 containers a year (3.5 million tons per year) at semi-specialized and multipurpose piers (lack of space requires the use of off-site storage facilities), and has no specialized

¹ Since 2005, Puerto Cortés has been part of the “Container Security Initiative” (CSI), under a customs agreement with the U.S. Department of Homeland Security and the Megaports Initiative of the U.S. Energy Department.

² The Atlantic Corridor (1,745 km) is part of the International Mesoamerican Highway System (RICAM) under the Puebla-Panama Plan (PPP), linking Mexico, Belize, Guatemala, Honduras, and El Salvador.

³ Petroleum and petroleum products are imported primarily through Puerto Cortés, but the facilities are operated by Texaco.

⁴ The main piers were built between 1950 and 1978, with a subsequent 124-meter extension in 1992 completing the current berthing area.

- terminal;⁵ and (ii) dry bulk cargo (1.4 million tons per year) is transferred directly between vessel and truck at multipurpose piers, an inefficient procedure that can pollute the surroundings and interferes with urban transit. The current port area, hemmed in by the city, reduces the possibility of port zoning and impedes the development of specialized terminals at the existing piers, basically because of a chronic lack of space for arranging storage yards contiguous to the pier. All of these factors limit the efficiency of operations.
- 1.5 Symptoms of the problems described above manifest themselves, in particular, in the length of time that vessels must remain in port. The piers at Puerto Cortés are subject to intensive use (with an average occupancy rate of 70% or more), because of the shortage of berthing sites and inefficient transfer procedures. The inevitable consequence is that vessels wait a long time for a slip and then spend a long time at berth. This congestion is costly to the port's customers: the ENP has been able to avoid losing shipping customers only through a system of berthing priority that gives preference to container ships (liners) over bulk carriers (charter vessels that have more time flexibility, but bill for this), although the extra costs are also passed on to users.
- 1.6 This berthing priority system determines how waiting times are distributed. The average waiting time for Lo-Lo (lift on/lift off) container ships is 5.2 hours, or the equivalent of 35% of time in berth (15 hours), a high but still tolerable value.⁶ Bulk vessels must wait on average 42.1 hours,⁷ equivalent to 52% of average time in berth (81.3 hours), a very high value. The high cost of congestion affects all vessels, but is felt most intensely by the bulk vessels and thus by the users of their cargo.
- 1.7 **The ENP's investment plan and strategy.** With the project to expand and modernize Puerto Cortés, the ENP has established specific instruments for upgrading the port's infrastructure to meet current demand, with a view to increasing its capacity, improving its efficiency, and in the end enhancing the country's competitiveness and promoting domestic economic activity and regional integration. In particular, the ENP plans to expand infrastructure through new berthing slips, to incorporate modern equipment, and to expand landside storage spaces and other logistical facilities, in line with the worldwide trend to make better and more efficient use of resources at the new port. At the same time, it plans to maintain current infrastructure and to renew its equipment in due course.
- 1.8 **Stages of the ENP strategy.** To resolve its low capacity problems and make operations more efficient, the ENP has adopted a strategy for expanding and modernizing the port in three phases: (i) construction of a fully equipped container

⁵ The need to improve efficiency (operating costs and turn-around times) has led many ports to experiment successfully with specialized terminals for containers with lower transportation volumes.

⁶ In ports that face stiff competition for container traffic, waiting times for container vessels are reduced virtually to zero.

⁷ The average wait for bulk vessels is 42 hours (1.8 days), but some vessels are delayed less and others more (as much as three or four days, according to some observations).

- terminal; (ii) construction of an organic bulk freight terminal; and (iii) expansion and renovation of the machinery at the existing piers. This program would finance the first construction phase, and preparation of studies and designs for the second phase.
- 1.9 **Country strategy.** The program is consistent with the Bank's strategy with Honduras. That strategy defines four areas of action: (i) to improve the investment climate; (ii) to improve competitiveness, by reducing logistics and production costs among other aspects; (iii) to promote human capital formation; and (iv) to strengthen the institutional framework and risk prevention management. The program is consistent with the activities proposed in the strategy in support of the second point.
- 1.10 The proposed program is consistent with the strategy in that: (i) it will assist in the development of a more efficient national transport system based on a higher-capacity modern port infrastructure, which will facilitate and guarantee the transport of merchandise and products to and from the centers of consumption, production, and export; (ii) it will reduce costs along the logistics chains in which the port participates, and thereby boost national competitiveness; and (iii) it will allow the integration of new international transport chains that have development potential in the context of the Atlantic Corridor.
- 1.11 **Rationale for Bank participation.** The Bank is supporting the expansion and modernization of transport infrastructure in Honduras. It has been supporting institutional strengthening for the sector and financing works, including some that are related to this program. Specific projects are under way that relate to improving the CA-5 logistics corridor, through the Puebla-Panama Plan's Atlantic Corridor Improvement Program (sections of the CA-5 Norte Highway) (1565/SF-HO approved in July 2004, for US\$50 million), and supplementary financing for the same program (1910/BL-HO, approved in October 2007, for US\$30 million), as well as financing of the San Pedro Sula Logistics Corridor Infrastructure Program (2017/BL-HO, approved on 17 September 2008, for US\$20 million). These projects have been executed under a coordination agreement with other multilateral agencies that are financing complementary investment programs to improve this important corridor. The Bank is currently processing a US\$10 million project for modernization of customs at Puerto Cortés (HO-L1055), the goal of which is to improve the efficiency and quality of customs services at the port. This project complements the proposed program by improving the movement of cargo through the port and contributing to the development of the port as a regional logistical hub.
- 1.12 This operation was originally conceived as a non-sovereign guaranteed (NSG) loan, for which the project concept document (PCD) was approved on 3 April 2008. As a result of the analysis conducted during preparation of the operation, and bearing in mind the requirements for financing operations of this type, especially as they relate to the interest rate, level of contingencies, reserve accounts, and debt service coverage indicators, it was decided that if the project were to be viable it would

have to be carried out through a conventional public-sector investment operation, using concessional resources with the country's guarantee.

C. Objective, components and costs

1. Objective

- 1.13 The general objective of the program is to improve the capacity and efficiency of operations at Puerto Cortés, by promoting better international physical integration and thereby contributing to the sustainable economic and social development of Honduras. In particular, it seeks to: (i) reduce operating costs and delays in vessel and cargo handling, and enable the development of logistics operations typical of specialized terminals (containers); and (ii) avoid the risks of pollution from port operations and prevent interference with urban transit, through the use of specialized equipment and in-port storage yards. The program is expected to benefit users of the port (operators, shippers, consignors, etc.) and to boost economic activities within the port's area of influence, which will lead to lower costs for importing inputs and exporting products, and better access to suppliers, customers, and markets.

2. Components

- 1.14 **Program components.** The principal components of the program are: (i) dredging of the port basin and slips, and land reclamation (for the container terminal, the adjacent yard and the expansion zone), through a conventional works contract; (ii) construction of the infrastructure and superstructure works for the container terminal, through an EPC (engineering, procurement and construction) contract; (iii) procurement of complete equipment and systems for the container terminal; and (iv) a business strengthening and technical assistance component for the ENP.
- 1.15 **Component 1. Engineering and administration** (US\$4.7 million, IDB: US\$2.95 million)
- 1.16 **Subcomponent 1.1. Program administration.** The program will finance the hiring of a "consulting firm" to support the ENP in program management. This approach is similar to the "management firm" used in various Bank projects.⁸ The consulting firm will provide technical assistance to the ENP by performing the following basic functions: (i) providing specialized consulting services for defining equipment specifications for the container terminal, completing the design of the organic bulk terminal, and defining its equipment, as well as support for defining the equipment for the existing piers and the procurement of marine equipment; and (ii) assisting with administration of program execution, including monitoring the social and environmental aspects, carrying out the programming and monitoring tasks, cost control, quality control, loan contract administration, and technical administrative

⁸ The use of "management firms" in Honduras finds precedents in Bank projects executed by SOPTRAVI. This practice has ensured proper execution of those projects. It allows for flexibility and responsiveness in resolving specialized technical aspects of execution that fall outside the normal activity of the ENP, and also makes it possible to follow up on relations with the Bank.

- support (information system, monitoring etc.). Also included is the hiring of external consultants specializing in ports, to make up the committees that will be evaluating the bids and the international open calls for proposals.
- 1.17 **Subcomponent 1.2. Financial, accounting, and environmental audits of the program.** Financing will be provided for the semiannual and annual audits, in accordance with Bank policies and the requirements of the Environmental and Social Management Plan.
- 1.18 **Component 2. Civil works and supervision** (US\$144,725,000, IDB: US\$93.42 million)
- 1.19 **Subcomponent 2.1. Dredging and land reclamation works.** This subcomponent will finance the works needed to: (i) create new shipping space by dredging to a depth of -14 meters over an area of approximately 40.2 hectares, in order to complete the internal channel, and 105.9 hectares to form the turning basin in front of the new port facilities; and (ii) generate new landside spaces in the southeast portion of the current port, as the location for the new port facilities, using hydraulic fill with material extracted from the dredging, for a total of 45.3 hectares of new, stabilized land, with appropriate coastal protection. The new space reclaimed from the sea will accommodate the container terminal, a future expansion area, and an area for the future organic bulk terminal. This subcomponent will include environmental studies complementary to the existing ones, and environmental monitoring.
- 1.20 **Subcomponent 2.2. Construction of the container terminal.** This subcomponent will finance the plan and construction of physical infrastructure for the container terminal through an EPC contract, using the newly reclaimed land. The works include: (i) a 485-meter linear pier (two berths) designed to operate at a maximum depth of -15.5 meters; (ii) an operations area of about 27.6 hectares, including a container storage yard of about 15.6 hectares; (iii) a logistics warehouse (consolidation/deconsolidation), an office building, a transfer zone, a maintenance workshop, internal access and control points; (iv) an area for handling special and hazardous cargoes; (v) auxiliary facilities (power supply, storm and wastewater drains, etc.); and (vi) external access points and roads linking them to the port's main street.
- 1.21 The pier will be long enough to berth two Panamax-type vessels (220 m) or one post-Panamax vessel (260 m) and one pre-Panamax "feeder" vessel (180 m). With these investments, the practical transfer capacity for the container terminal will be around 400,000 containers per year (760,000 TEU/year), with a ceiling of 480,000 containers per year (910,000 TEU/year) with more productive equipment.
- 1.22 **Subcomponent 2.3. Works supervision.** The technical, environmental and administrative aspects of the program works will be supervised by specialized firms hired for this purpose. Their responsibilities will include: (i) supervising the works, ensuring compliance with technical and environmental control specifications contained in the existing designs and environmental assessments; (ii) verifying the

quality of the contractors' work; (iii) maintaining laboratories and other equipment for the necessary technical tests and controls and environmental monitoring; (iv) measuring the services performed by the contractors; (v) advising ENP on matters relating to works management; (vi) advising on any needed contract amendments, suspension of service, expansion of activities, changes to unit prices, and pricing of new activities; and (vii) preparing monthly progress reports, covering the works as well as implementation of the environmental control measures, and the final works report.

1.23 **Component 3. Procurement of equipment.** (US\$67.5 million, IDB: US\$33.75 million). This component will finance the complete equipping of the container terminal, which will comprise: (i) 4 post-Panamax 45-ton gantry cranes, including their installation on the pier; (ii) 20 "straddle carriers" that can load containers in stacks of three; (iii) 4 front loaders for handling empty containers; (iv) terminal management software; (v) security and communications equipment; and (vi) work vehicles.

1.24 **Component 4. Institutional strengthening.** (US\$2.4 million, IDB: US\$1.2 million). This component will finance institutional strengthening activities to be determined by means of an institutional analysis, and support for the operations, planning, marketing, and security sectors of the ENP, through: (i) design of the organizational structure, personnel requirements, training etc. for the container terminal administration unit, including the equipment maintenance and social environmental units; (ii) design, organizational structure, and training to create the port planning unit and the marketing unit; (iii) preparation of an industrial and environmental safety program for Puerto Cortés and a hazardous materials management plan; (iv) introduction of an environmental, social, and industrial health, safety, and hygiene management system; and (v) a study of user charges and capacity to pay.

3. Costs

1.25 The total cost of the program will be US\$225,415,000. The country financing parameters will be used for the Bank's financing. A breakdown of this amount, by source and component, is shown below (in US\$000).

Components	Total	IDB	CABEI	Local
Component 1. Engineering and administration	4,700	2,950	1,750	
1.1 Administration	4,200	2,700	1,500	
1.2 Financial audit	500	250	250	-----
Component 2. Civil works and supervision	144,725	93,425	51,300	
2.1. Dredging and filling	35,000	20,000	15,000	
2.2. Container terminal construction	105,725	71,425	34,300	-
2.3. Works supervision	4,000	2,000	2,000	-----
Component 3. Equipment	67,500	33,750	33,750	-----
3.1. Container terminal equipment	67,500	33,750	33,750	-----
Component 4. Institutional strengthening	2,400	1,200	1,200	
4.1. Assistance in structuring the maintenance and environmental units	1,000	500	500	
4.2. Assistance in structuring the port planning and marketing units	500	250	250	-----
4.3. Preparation of safety programs and plans	250	125	125	-----
4.4. Implementation of an environmental, social, and industrial health and hygiene management system	400	200	200	
4.5. User charge study	250	125	125	-----
5.0. Contingencies	3,800	1,800	2,000	-----
6.0. Financial expenses	2,290	1,875	-----	
6.1. Credit fee	415	-----	-----	415
6.2. Interest	1,875	1,875	-----	
TOTAL	225,415	135,000	90,000	415

1.26 The disbursement period will be four years, in accordance with the following schedule (values in US\$000).

	2011	2012	2013	2014	TOTAL
IDB	30,000	56,000	36,000	13,000	135,000
CABEI	20,000	40,000	22,000	8,000	90,000
TOTAL	50,000	96,000	58,000	21,000	225,000

D. Results Matrix and Principal Indicators (PPMR monitoring)

1.27 The principal results expected from the program are summarized below, and are presented in greater detail in the Results Matrix (Annex 1).

Expected results	Indicator
Increased productivity in pierside transfer of containers.	<ul style="list-style-type: none"> • Movements per vessel and hour at berth (mov/ship/hour): 30 to 50
Reduced waiting times for vessels in port.	Waiting time/berthing time (Tw/Tb): <ul style="list-style-type: none"> • for Lo-Lo container ships: 0.35 to 0.01 • for bulk vessels and other ships: 0.52 to 0.07
Improved port management capacity.	<ul style="list-style-type: none"> • Personnel hired and trained for key posts. • Preventive maintenance system in place. • Safety programs and plans in place.

II. FINANCING STRUCTURE AND MAIN RISKS

A. Financing instrument

2.1 The proposed program is an investment loan. The program has a total cost of US\$225.4 million, which will be financed as shown in paragraph 1.27. The financial structure of the operation includes US\$135 million (59.9%) from parallel funds (FSO/OC) from 2010. Honduras is eligible for a 30%/70% FSO/OC financing blend. Another US\$90 million (39.93%) will be financed by CABEL (Central American Bank for Economic Integration), and the remaining US\$415,000 (0.18%) will be the counterpart contribution.

B. Environmental and social risks and mitigation measures

2.2 As this project involves the expansion of an existing port, the most significant environmental impacts have already occurred, and those caused by the expansion will be of minor significance. The Bank joined the project at an early stage, and was able to build the environmental aspect into the specifications for the project's design and supervision, working in parallel with the preparation of an environmental impact study commissioned by the ENP.

2.3 As a result of previous studies and monitoring reports, the expansion works are not expected to generate any significant adverse impacts, as the physical works will be of medium magnitude and fairly conventional from the engineering viewpoint. Moreover, because they will be carried out within the port precinct they will have no repercussions on properties not owned by the ENP or that are environmentally sensitive. Dredging work generally has the most serious impacts, because excess

materials are dumped at sea. In this project, however, the material specifications were revised, and there will be no disposal at sea. All the excavated material will be used as fill and in land reclamation in amounts sufficient to accommodate construction of the new piers.

- 2.4 Halcrow Ltd. was originally contracted to perform an environmental and social due-diligence study. The results of that study, and those of the environmental impact assessment (EIA), are discussed in further detail in the Environmental and Social Management Report. To ensure compliance with Bank policies, arrangements were made to have the EIA published and put to consultation, and in fact it contains the requests from the affected communities, which are reflected in the environmental management plan for construction and operation of the port. The strategy for handling operation-related environmental and social issues calls for: (i) strengthening the ENP's environmental management unit responsible for environmental and social monitoring of the project; (ii) resolving the environmental liabilities related to the port's current operation; (iii) including environmental specialists in the works supervision teams; (iv) implementing environmental and social management systems and occupational and industrial health and safety management systems, in order to improve existing practices and ensure that port operations achieve international quality standards; and (v) updating and supplementing contingency plans.⁹ The Environmental and Social Management Report (ESMR) attached to this document provides further information confirming the project's B classification, as defined in ESR Minute 40-08 of 10 October 2008.
- 2.5 Given the importance of bringing the port up to international management standards, it has been agreed that, as a condition precedent to award of the port terminal expansion contract, the ENP will deliver to the Bank a Social, Environmental, and Health and Safety Action Plan for the new terminal defining: (i) the schedule for implementing an environmental and social management plan based on ISO 14001; (ii) implementation of an industrial health and hygiene and occupational safety system; (iii) the timetable for obtaining a definitive environmental license for operating the existing port facilities; (iv) resolution of existing environmental liabilities such as the treatment of wastewater, compliance with international agreements and treaties (MARPOL, among others), and other matters raised in the due diligence reports.

C. Fiduciary risk

- 2.6 The Bank has no experience with the ENP as an executing agency in previous programs. Accordingly, the required provisions have been adopted to avoid institutional or fiduciary problems, including support of the management consulting firm for execution of the program and the hiring of specialized firms for works supervision. Moreover, works and procurement under the program will involve

⁹ As a complement to environmental and social considerations, during preparation of the operation contract was established between the ENP and the GEF project for the Gulf of Honduras, in order to coordinate future work.

sizable lots, which will facilitate supervision and execution. Consequently, it is recommended, as a contractual condition of execution, that the initiation of any civil works be dependent on the selection and contracting of the corresponding works supervision services.

D. Other issues and risks

- 2.7 **Cofinancing.** From the outset CABEI cofinancing of US\$90 million—40% of the total project cost—has been envisaged. All technical, financial, and environmental due-diligence processes, as well as procurement processes, have been conducted in close coordination with CABEI. **As a condition precedent to the first disbursement, the financing agreement with CABEI will have to be signed and in force.**
- 2.8 **Technical feasibility.** A technical due diligence study was performed to determine the technical feasibility of the planned investments. That study found that the proposed project is an appropriate response to the port's problems: (i) the container terminal is, generally speaking, well designed, well defined, and well presented; and (ii) the organic bulk terminal is well conceived, although only its location and main dimensions have been determined and not the installations and equipment (this will be done with the support of the management consulting firm). The cost estimates were also reviewed, and were found to be correct with a 10% degree of uncertainty, which is typical for projects of this kind (the estimates include 10% for contingencies).
- 2.9 **Economic feasibility.** A feasibility study was conducted to determine the economic viability of the investment project associated with the dredging works, land reclamation, and construction of the specialized container terminal at Puerto Cortés. The results show an economic net present value (ENPV) of 12%, or approximately US\$108.2 million, while the economic internal rate of return (EIRR) is 20%, comfortably above the normal cutoff rate of 12%. The ENPV/investment ratio is 0.58, which is considered good. Overall, the program is clearly profitable. A conventional sensitivity analysis was also performed, calculating indicators of profitability in the event of an increase in the investment amount and of a decrease in container demand at the port. In both cases, the program remains acceptably profitable, with only moderate sensitivity to an increase in the initial investment amount, and slightly more sensitivity to a decline in the volume of container demand.
- 2.10 **Financial feasibility.** The ENP's operating revenues grew at a rate of 7% annually from 2003 to 2008. In 2008, those revenues reached US\$66 million.¹⁰ In 2009, as a result of the crisis in the international markets, cargo volumes handled by the ENP shrank by 15%. In 2010, the ENP expects cargo volumes to return to 2008 levels. According to the ENP's financial projections, it will have the financial capacity to repay the loans from the Bank and CABEI. Under pessimistic demand scenarios,

¹⁰ ENP Statistics Department.

with a substantial slowdown in the country's economic growth or in international trade, or if the ENP fails to maintain an adequate port fees policy, it is possible that the ENP's financial situation and hence its debt service capacity could be adversely affected. This confirms that, as noted earlier in this document, the ENP is not strong enough on its own to shoulder financing of the magnitude proposed here, and that a sovereign guarantee is therefore needed; this will to some extent lighten the financial burden on the ENP. As to the capacity to make the local counterpart contribution during program execution, the financial analysis indicates that the ENP has adequate resources, and no difficulties are anticipated on this front.

- 2.11 **Execution risks.** In technical terms, the works to be executed pose no great difficulty. There is, moreover, a broad market of qualified supervisors and construction firms (except for dredging works) for the types of works to be financed. In environmental terms, the works are not expected to generate any significant indirect impacts, and the direct impacts of the works will be adequately controlled and mitigated during execution. Both the management consulting firm and the supervisory firm will have social, environmental, and health and safety specialists.
- 2.12 **Sustainability risks.** The risks related to technical and operational sustainability range from moderate to high. There is a high risk of gaps in the effectiveness of terminal equipment maintenance. To mitigate this risk, the ENP will present a preventive maintenance plan for that equipment, before awarding the contract for procurement of the container terminal equipment, and will demonstrate that it has budgeted the funds needed to implement the plan. There is a moderate risk of failure to manage the container terminal efficiently. To mitigate this risk, the program includes a strengthening component that will create a well-integrated administration unit with highly trained staff. As to social and environmental sustainability, the planned strengthening and the implementation of the management systems (paragraph 2.4) should result in a substantial improvement in the port's operations.

III. IMPLEMENTATION AND ADMINISTRATION PLAN

- 3.1 **Borrower, executing agency, and guarantor.** The borrower and executing agency for the program will be the ENP, and the guarantor will be the Republic of Honduras. The ENP meets the requirements established in Bank policy to be a borrower.
- 3.2 **Execution plan.** Program execution will be in the hands of the ENP, an administratively autonomous entity created in 1965 by Legislative Decree 40, with its own legal status under public law and with its own assets and administrative, operational, financial, and legal autonomy, attached to the Ministry of Public Works, Transport, and Housing (SOPTRAVI). The highest authority of the ENP is the Board of Directors, comprising five secretaries of state, two representatives of the private sector, and a workers' delegate. Operating management is in the hands

- of the General Manager, assisted by five divisions (Human Resources, Technical, General Accounting, Planning, and General Services) and a Superintendency.
- 3.3 The program will be implemented through a Project Coordination Unit (PCU), which will report to the ENP's General Manager and will have to be created and staffed with qualified personnel, primarily from the ENP. As a special condition precedent to the first disbursement, the PCU must be created and in operation. The PCU's functions will include: (i) expediting fulfillment of the conditions established in the loan contract; (ii) representing the ENP vis-à-vis the Bank; and (iii) maintaining the program's technical, financial, and administrative information systems. To this end, the PCU will centralize the presentation of accounts to the Bank and to other State institutions. Its specific functions include: (i) planning loan execution and the annual work plans (AWP); (ii) preparing and updating the procurement plans; (iii) reviewing bidding documents and conditions for consulting services, works, and goods, and seeing that they comply with the Bank's procurement and contracting policies; (iv) guiding and monitoring progress with the contracts for consulting services, works, and procurement of goods; (v) preparing project profiles; (vi) processing the corresponding payments; (vii) preparing financial statements and disbursement requests; and (viii) monitoring and evaluating program execution, including the social and environmental aspects. The PCU will be supported by the management consulting firm to be contracted with program funds. **The selection and contracting of that firm will be a special condition precedent to the first disbursement.**
- 3.4 At a minimum, the PCU will be comprised of: a project coordinator, an engineer specializing in ports, an administrative/financial specialist, an environmental specialist, and a procurement specialist. Contracting will be done on the basis of competitive processes, pursuant to terms of reference and profiles agreed upon with the Bank, and results-based contracts will be used.
- 3.5 The ENP will be responsible to the Bank for: (i) opening separate and specific bank accounts to manage the loan funds and the counterpart contribution; (ii) having an adequate system for (a) maintaining internal control and accounting and financial records on the source and use of program funds, pursuant to general clause 7.01 of the loan contract, and (b) keeping records to substantiate eligible expenditures for verification by the Bank and the external auditors; (iii) preparing and presenting (a) semiannual progress reports, and (b) disbursement requests and the supporting documentation for expenditures; and (iv) preparing such other reports as the Bank may request.
- 3.6 **Procurement.** The procurement of goods and works and the selection and contracting of consultants will be done in accordance with Bank policies (documents GN-2349-7 and GN-2350-7) and with the program procurement plan (Annex II). International competitive bidding will apply for goods where the cost is US\$150,000 or more, and for works where the cost is US\$1.5 million or more. National competitive bidding will apply for goods where the cost is US\$25,000 or more, and for works costing US\$150,000 or more. Price comparison ("shopping")

will apply for goods where the cost is below US\$25,000, and for works costing below US\$150,000. In the case of consulting services, a short list may be composed entirely of national consultants when the cost is the equivalent of US\$200,000 or less.

- 3.7 Purchases will be financed *pari passu* by the IDB and CABEL. Consequently, it is recommended that member countries of CABEL that are not members of the Bank be allowed to participate in the procurement of goods, works, and consulting services, in recognition of the need to harmonize IDB and CABEL procurement policies in order to keep the financing *pari passu*. The bid evaluation committees will have five members: two internal ENP staff, two external port experts, and one representative of the Ministry of Finance. The process for selecting the external experts will take into account their knowledge and experience in similar port projects and will require the Bank's no objection. Limited international bidding will be used for dredging and land reclamation works contracting, which is justified by the fact that there are relatively few firms with the necessary expertise in this market.
- 3.8 Procurement of goods, works and services using program funds will be subject to ex ante supervision, until such time as the Bank authorizes transitioning to the ex post procedure, in accordance with Bank procurement policies.
- 3.9 **Evaluation and monitoring.** The PCU will provide the Bank with semiannual progress reports, with a copy to the guarantor, indicating progress under each of the components as well as the program's overall performance, based on the indicators agreed upon in the Results Matrix. In addition, the reports will include: (i) description of the activities performed; (ii) updated timetables for physical execution and disbursements; (iii) degree of compliance with agreed execution indicators, including implementation of the environmental and social action plan; (iv) a work program for the following six months; (v) a summary statement of program financial execution and a cash flow forecast for the coming six months; (vi) a section identifying potential developments or events that could jeopardize program execution; (vii) a section on the project's social and environmental management; and (viii) in the year-end report, the annual work plan (AWP), including the updated procurement plan.
- 3.10 Moreover, within 90 days after the last disbursement, there will be a final evaluation of the program, which must include, as a minimum: (i) the results of financial execution, by component; (ii) achievement of the established goals, in accordance with the agreed results indicators; and (iii) compliance with contractual commitments. The project cycle management tools will also be applied during execution (procurement plan, implementation plan, results matrix, etc.) to facilitate monitoring and follow-up of activities, outputs, and results of the project.
- 3.11 In order to monitor the financial status of the ENP and its capacity to repay the debt it is contracting, the ENP undertakes to maintain a debt service coverage ratio (DSCR) of no less than 1.0 during the entire program execution period; to submit

- reports annually on compliance with this condition and, should deviations in relation to this indicator present themselves, reflecting a deterioration of the company's financial situation, to submit an action plan to the Bank clearly identifying the reasons for such deviations and the management or financial measures to be adopted, its responsibilities, and the execution timetable for allowing financial sustainability to be recovered; and to present its financial statements, duly audited by an independent auditing firm acceptable to the Bank, and to make them public.
- 3.12 **Advance.** The Bank will make a disbursement of resources under the “advance of funds” modality, based on the program's liquidity requirements, for commitments undertaken to cover expenses related to execution. The maximum amount of each advance of funds will be set by the Bank and will consist of a quantity determined on the basis of the project's liquidity needs arising from commitments undertaken to cover periodic expenses related to project execution that may be financed out of the loan proceeds. At no time will the maximum amount of an advance exceed the sum needed to finance such expenses during a period of up to six months, in accordance with the AWP, the procurement plan, the financing schedule, and the flow of funds required for such purposes, and with the executing agency's demonstrated ability to efficiently manage the financing proceeds.
- 3.13 **External audit.** Throughout program execution the borrower, through the PCU, will present annual consolidated financial statements for the program to the Bank and the guarantor within 120 days after the close of the fiscal year. To this end, it will contract for external audits to be performed by an independent auditing firm acceptable to the Bank and in accordance with its requirements, based on guidelines established in the terms of reference for the external audit of projects financed by the IDB. In selecting and contracting the auditing firm, the procedures established in the document on tendering for external audits will be used. The costs of the audits will be part of the program cost. In addition, there will be semiannual operating and financial audits, which will need to produce the reports required in the terms of reference for the external auditors. Those reports must be presented within 60 days after the end of the respective six-month period.
- 3.14 **Environmental and social audit.** As a condition precedent to awarding the contract for dredging and land reclamation works, the ENP will select and contract a firm to conduct an environmental audit that verifies compliance with the commitments acquired and to confirm progress in setting up the management systems.
- 3.15 **Establishment of information mechanisms.** The program will create mechanisms for dissemination through the ENP's website, to supply, in a timely manner, relevant information on the progress of the program, including the program's procurement processes.

**Development Effectiveness Matrix
Summary**

Indicator	Score	Maximum Score
<i>I. Strategic Relevance</i>	Low-High	
1. IDB Strategic Development Objectives	4.5	10
Country Diversification	2.0	2
Corporate Initiatives	2.5	2.5
Harmonization and Alignment	0.0	3.5
Beneficiary Target Population	0.0	2
2. Country Strategy Development Objectives	7.2	10
Country Strategy Sector Diagnosis	6.0	6
Country Strategy sector objective & indicator	1.2	4
<i>II. Development Outcomes - Evaluability</i>	Satisfactory	
3. Evidence-based Assessment & Solution	6.7	10
4. Evaluation & Monitoring Plan	4.6	10
5. Cost-Benefit or Cost-Effectiveness	10.0	10
6. Risks & Mitigation Monitoring Matrix	5.0	10
<i>III. IDB's Role - Additionality</i>		
7. Additionality	3.0	10
Technical Assistance provided prior the project	3.0	3
Improvements in management of financial, procurement, monitoring or statistics internal controls	0.0	4
Improvements in environmental, health and labor performance	0.0	3

I. Strategic Relevance: This is an investment project that will take place in Honduras, classified as a D country. The project falls under the corporate initiative related to infrastructure. The project is aligned with the Country Strategy approved in 2008.

II. Evaluability: The problems being addressed through the program are clearly defined and its diagnosis is empirically based. The main factors that contribute to these problems are clearly specified, as are the interrelationship among factors and the magnitudes of their deficiencies.

The program's outcomes and outputs are clearly stated and show vertical logic. Not all outputs have indicators. There is no indicator related to the completion of the container terminal. All indicators presented in the matrix have baselines, targets and sources of information. Some indicators are not SMART in that they do not measure the economic rate of return ex post. The program has a monitoring and evaluation plan, but the documentation does not present an allotted budget for each activity. The program will be evaluated using a reflexive methodology and analyzed using a cost-benefit analysis which generated a rate of return above 12%. The risks of the operation are identified and classified but not all present mitigation measures. Likewise, no indicators, baselines or targets are included to monitor these measures.

III. Additionality: A technical assistance was provided to increase the likelihood of success of the project.

**PUERTO CORTÉS EXPANSION AND MODERNIZATION PROGRAM (HO-L1037)
RESULTS MATRIX**

Program objective	The general objective of the program is to improve the capacity and efficiency of operations at Puerto Cortés, by promoting better international physical integration and thereby contributing to the sustainable economic and social development of Honduras. In particular, it seeks to: (i) reduce operating costs and delays in vessel and cargo handling, and enable the development of logistics operations typical of specialized terminals (container and organic bulk terminals); (ii) avoid the risks of pollution from bulk cargo operations and prevent interference with urban transit, through the use of specialized equipment and in-port storage yards. These objectives will be achieved through financing for two basic components: (i) construction and equipping of a specialized container terminal; and (ii) preparation of designs for constructing a specialized organic bulk terminal. This will be supplemented with specific institutional strengthening activities to ensure efficient use of the new infrastructure.			
Results indicator	Unit of measurement	Baseline (2008)	Target (2012)	Observations
Enhanced productivity at the dock				
Increase in productivity in the transfer of containers at specialized piers.	Movements per ship and hour at berth (mov/ship.hour)	30	50	Target one year after completion of the terminal
Reduction in average time at berth for Lo-Lo container ships.	Hours at berth per ship (Tb)	9.0	5.7	Target one year after completion of the terminal
Reduction in ship waiting time				
Reduction in waiting times for Lo-Lo container ships.	Waiting time as a proportion of time at berth (Tw/Tb)	0.35	0.01	Target one year after completion of the terminal
Reduction in waiting times for bulk and general cargo ships.	Waiting rate (Tw/Tb)	0.52	0.07	Target one year after completion of the terminal

Results indicator	Baseline (2008)	2010	2011	2012	Observations
Technical support and management capacity strengthening for the ENP					
Organic bulk terminal defined and designed	0%		100%		
Management and technical staff hired and trained	0%	20%	40%	100%	
Preventive maintenance system designed and implemented	0%			100%	Target one year after completion of the terminal
Safety programs and plans designed and implemented in the port.	0%		50%	100%	

PUERTO CORTÉS EXPANSION AND MODERNIZATION PROGRAM (HO-L1037)
PROCUREMENT PLAN¹
(US\$000)

	Estimated cost (US\$)	Procurement method	Review	Financing source and percentage			Prequalification (Yes/no)	Estimated dates		Status
				IDB %	CABEI %	Local %		Publication of specific procurement notice		
1. Goods										
1.1	Container terminal equipment	67,500	ICB	Ex ante	50	50	--	No	March 2012	
2. Works										
2.1	Dredging and land reclamation	35,000	LIB	Ex ante	57	43	0	No	February 2011	
2.2	Container terminal construction	105,000	ICB	Ex ante	68	32	0	Yes	September 2010 February 2010	Prequal. Bidding
3. Consulting services										
Administration										
1.1	Administration (PCU)	500	SSS	Ex ante	62	38	0	No	November 2010	
1.2	Administration (evaluation committee)	200	SSS	Ex ante	100			No	January 2010	
1.3	Administration (MCF)	3500	QCBS	Ex ante	62	38	0	No	July 2008	Process done and under review
1.4	Financial audit	500	QCBS	Ex ante	50	50	----	No	November 2010	
Supervision										
1.5	Works supervision for the container piers	3,300	QCBS	Ex ante	50	50	----	No	September 2010	
1.6	Works supervision for dredging and land reclamation	700	QCBS	Ex ante	50	50	-----	No	September 2010	
Institutional strengthening										
1.7	Structuring of new maintenance and environmental units	1,000	SSS	Ex ante	50	50	----	No	June 2011	
1.8	Structuring of new port planning and marketing units	500	SSS	Ex ante	50	50	----	No	June 2011	

¹ Must include all project contracts whether or not financed by the Bank, and an indication of who is financing them.

	Estimated cost (US\$)	Procurement method	Review	Financing source and percentage			Prequalification (Yes/no)	Estimated dates	Status
				IDB %	CABEI %	Local %		Publication of specific procurement notice	
1.9 Preparation of safety programs and plans	250	SSS	Ex ante	50	50	----	No	June 2011	
1.10 Implementation of the environmental and social management and health and hygiene plan	400	SSS	Ex ante	50	50	----	No	June 2011	
1.11 Port fees study	250	SSS	Ex ante	50	50	----	No	June 2011	Pending

International competitive bidding; **LIB**: limited international bidding; **NCB**: national competitive bidding; **PC**: price comparison; **DC**: direct contracting; **FA**: force account; **PSA**: Procurement through Specialized Agencies; **PA**: Procurement Agents; **IA**: Inspection Agents; **PLFI**: Procurement in Loans to Financial Intermediaries; **BOO/BOT/BOOT**: Build, Own, Operate/Build, Operate, Transfer/Build, Own, Operate, Transfer; **PBP**: Performance-Based Procurement; **PLGB**: Procurement under Loans Guaranteed by the Bank; **PCP/PSC**: Community participation procurement. **QCBS**: Quality- and Cost-Based Selection **QBS**: Quality-Based Selection **FBS**: Selection under a Fixed Budget; **LCS**: Least-Cost Selection; **CQS**: Selection based on the Consultants' Qualifications; **SSS**: Single-Source Selection.

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-__/10

Honduras. Loan ____/BL-HO to the Empresa Nacional Portuaria
Puerto Cortés Expansion and Modernization Program

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Empresa Nacional Portuaria, as Borrower, and with the Republic of Honduras, as Guarantor, for the purpose of granting it a financing to cooperate in the execution of the Puerto Cortés expansion and modernization program. Such financing, which will be for the amount of up to US\$94,500,000, from the resources of the Single Currency Facility of the Bank's Ordinary Capital, corresponds to a parallel loan within the framework of the multilateral debt relief and concessional finance reform of the Bank, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on _____)

LEG/SGO/CID/IDBDOCS#35385509
HO-L1037

DOCUMENT OF THE INTER-AMERICAN DEVELOPMENT BANK

PROPOSED RESOLUTION DE-__/10

Honduras. Loan ____/BL-HO to the Empresa Nacional Portuaria
Puerto Cortés Expansion and Modernization Program

The Board of Executive Directors

RESOLVES:

That the President of the Bank, or such representative as he shall designate, is authorized, in the name and on behalf of the Bank, to enter into such contract or contracts as may be necessary with the Empresa Nacional Portuaria, as Borrower, and with the Republic of Honduras, as Guarantor, for the purpose of granting it a financing to cooperate in the execution of the Puerto Cortés expansion and modernization program. Such financing, which will be for the amount of up to US\$40,500,000, from the resources of the Bank's Fund for Special Operations, corresponds to a parallel loan within the framework of the multilateral debt relief and concessional finance reform of the Bank, and will be subject to the Financial Terms and Conditions and the Special Contractual Conditions of the Project Summary of the Loan Proposal.

(Adopted on _____)

LEG/SGO/CID/IDBDOCS#35385501
HO-L1037