



MEXICO: LOS CABOS WATER

The city of Los Cabos in Mexico faced a water resource deficit and was unable to meet the water needs of households and businesses. With IFC's support, the government implemented an innovative dual approach to meet water demand by designing two public-private partnerships (PPP) that would increase water resources by developing a new desalination plant, and reduce water losses implementing a non-revenue water (NRW) reduction program. The two contracts were awarded in May 2021 and reached financial close in 2022 and 2023.

A consortium of Mexico's La Peninsular and Spain's Acciona Agua won the tender to build, operate and transfer (BOT) a 21.6 megaliters per day (MLD) desalination plant, which is expected to mobilize private and public investments totaling 1.7 billion Mexican Pesos (\$96 million). The NRW reduction project was awarded to the Spanish consortium formed by FCC Aqualia and Aqualia Mexico and is expected to mobilize private and public investments totaling 685 million Mexican Pesos (\$38 million). This is the first time in Mexico that a bulk new water project is paired with a resource efficiency improvement project.

This series provides an overview of public-private partnership stories in various infrastructure sectors, where IFC was the lead advisor.

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IFC's advisory work was supported by FONADIN, Mexico's Infrastructure Fund and the projects benefited from a subsidy from BANOBRAS, Mexico's national bank for public works.

BACKGROUND

The combined effects of demographic growth and tourism was driving increasing demand for water services in the Municipality of Los Cabos in the State of Baja California Sur in Mexico. The existing desalination plant in of Los Cabos (63 MLD) was insufficient to ensure 24/7 water service. High water distribution network losses (NRW levels of approx. 57%) further aggravated the problem, resulting in some areas of northern Cabo San Lucas only receiving water about once a week with customers forced to find alternative sources, such as buying water from tanker trucks.

As a result of these issues, the city's main water sources, the aquifers of Cabo San Lucas and San Jose del Cabo, were being overexploited. This led to declining groundwater levels, increased pumping costs, unreliable service, and the water needs of residential, commercial, and industrial users being unmet.

IFC'S ROLE

The Water Utility of Los Cabos appointed IFC as its lead advisor to assist it in structuring and tendering two PPPs – one for reducing non-revenue water losses and a second for building and operating a new desalination plant that would increase the availability of water for the city by more than 20 megaliters per day.

IFC managed a team of specialized technical, environmental, and legal experts who undertook technical, environmental and legal due diligence to recommend the most commercially and technically viable transaction structure that would attract reliable and reputable private sector investors that could help the municipality achieve its objective of ensuring a sufficient water supply for its citizens.

TRANSACTION STRUCTURE

The selection process included an initial prequalification of prospective bidders based on financial and technical criteria, such as minimum net equity and experience with BOT projects, especially in similar NRW and desalination plants. The government received 15 and 9 applications for the new desalination plant and for the NRW, respectively.

Under the 25-year PPP concession agreement for the development of the new desalination plant, the private partner will design, finance, build, equip, operate and maintain the facilities, in exchange for a fixed sum for the investment and a variable amount based on the volume of desalinated water it delivers for the utility. As per the NRW reduction PPP contract, the private participant will modernize, equip, operate and manage the Municipal Drinking Water System Agency for 10 years to decrease technical and commercial losses and provide a 24/7 drinking water service with adequate pressure, quantity

and quality. In return, the government will pay a fixed sum for the investment, operation and maintenance, and a variable incentive payment based on the achievement of efficiency targets.

This dual approach sets a precedent for public water utilities in Mexico, in which the improvement of water supply services is addressed not just by increasing the volume of water resources, but by also reducing the volume of water losses, thereby improving the sustainability of municipal water resources. It also creates a new business model in the water sector in the country, built on performance-based contracts in which the payment to the contractor is subject to the fulfillment of multiple service quality indicators.

BIDDING

Four firms bid for the new Desalination Plant: three consortia formed by international and national companies, and the operator of the existing desalination plant in Los Cabos. A further four consortia bid for the NRW project. The bidding criterion for the desalination plant was the lowest total tariff per m³, while the NRW was the lowest tariff per user.

Mexico's National Infrastructure Fund (FONADIN) made available a MXN 796 million and MXN 317 million capital subsidy to the desalination and NRW projects, respectively.

The Water Utility of Los Cabos considered the bidding process a major success as the economic proposals were 20% (desalination) and 59% (NRW) lower than anticipated. For the desalination plant, the winning bidder offered US\$/m³ 0.89, one of the lowest tariffs recorded for similar projects outside the Persian Gulf region.

EXPECTED POST-TENDER RESULTS

- The first water project in Mexico to merge water loss reduction with water supply to enhance water sustainability and improve the operational and financial performance of water utilities.
- Mobilization of nearly \$80 million in private investment towards improving water resource sustainability and water supply
- The additional drinking water and loss reduction will improve supply for nearly 280,000 people in Los Cabos.
- Savings in the client's operating costs, freeing up resources for service improvement and increased coverage.