



## State of Mexico's Sustainability Bond Framework

September 27, 2022

The United Nations Development Programme (UNDP) considers that the Framework for the State of Mexico's 2022 Sustainability Bond is consistent with the sustainable development priorities of this State and that it contributes to the attainment of the 2030 Agenda. This is reflected in the eligibility criteria for the use of resources, the resource management mechanisms, and in the prevision of the allocation and impact reports.

### Context

In 2015, the 2030 Agenda was approved by 193 member states of the United Nations as the sustainable development action plan. This plan seeks to eradicate extreme poverty, reduce inequality, and protect the planet through 17 Sustainable Development Goals (SDGs) and 169 targets. To implement the 2030 Agenda, the mobilization of resources from public and private sources is essential. In that regard, the Addis Ababa Action Agenda (AAAA) represents a global framework for the establishment of an environment that enables development, which recognizes the importance of financial flows and policies as indispensable sustainable development implementation means. This instrument identifies more than one hundred specific measures to finance the 2030 Agenda, considering domestic public spending at the national and subnational levels, through progressive fiscal policies and the development of the bond market. It also acknowledges the importance of effective, inclusive, and accountable institutions to promote the efficient and appropriate use of resources aimed to sustainable development.

With this in mind, in 2020 the issuance of the SDGs Sovereign Bond by the Mexican Government meant a bold and innovative approach to potentiate the capital market's role in the financing of budgetary programs contributing to the SDGs. The success of this instrument in the financial markets reflects the existing interest among the investment community to participate in solutions to the main development challenges of the social and environmental field.<sup>1</sup>

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<sup>1</sup>In 2020, Mexico became the first country to issue a sovereign sustainable Bond linked to SDGs, which had a demand of €4,8000 million of 6.4 times the offered amount. See *Secretaría de Hacienda y Crédito Público SHCP* Ministry of Finance (September 14, 2020), Notice No. 071, "*Hacienda realiza emisión inaugural del primer bono soberano sustentable en el mundo vinculado a los ODS de la ONU*" (The Ministry Finance conducts an IPO of the first sovereign sustainable Bond linked to the UN's SDGs", URL: <https://www.gob.mx/shcp/prensa/comunicado-no-071>.

The issuance of the State of Mexico's Sustainability Bond reviewed in this report is registered within the global and national efforts to diversify the income sources to accelerate the achievement of the SDGs.

## Introduction

In a global scenario, where current levels of investment are insufficient to achieve the SDGs, the issuance of thematic bonds linked to sustainable development increases the resources allocated to the fulfillment of the 2030 Agenda and does so through solid mechanisms for monitoring and accountability of its results. In view of the foregoing, its impact on sustainable development at the national and local level is strategic and allows the reduction of the gap between available and necessary financing.

The State of Mexico's Government, through the Ministry of Finance (MF), when identifying opportunities to implement concrete actions in terms of financing the 2030 Agenda in its jurisdiction, decided to issue a Sustainability Bond to finance outstanding public policies. This initiative allows to replicate and adapt to the local context the federal government's determined issuance of a thematic bond which directly contributes to sustainable development.

Regarding the issuance of the State of Mexico's Sustainability Bond, UNDP provided technical support focused on reviewing the *State of Mexico's Sustainability Bond Framework* (hereinafter, the *Framework*)<sup>2</sup>, as a mechanism for the mobilization of resources from various sources to advance and accelerate the achievement of the SDGs in the entity. In this regard, UNDP reviewed three main elements of this document: use of resources, management of the latter, and forecasting of allocation and impact reports.

Therefore, UNDP's analysis focuses on the *Framework*, including eligibility criteria and the provision of internal controls for adequate resource management. However, it does not delve into the quality of the projects to be financed and is not a pronouncement on the expected impacts, since these aspects will be the subject of the entity responsible for preparing the allocation and impact reports at the time.

## Use of resources

The State of Mexico's Government has shown a strong commitment to sustainable development and the achievement of the 2030 Agenda by integrating this action framework into different planning processes. Especially, the State of Mexico promoted the mainstreaming of the 2030 Agenda approach in its State Development Plan 2017-2023 (*Plan Estatal de Desarrollo PDEM 2017-2023*) and the programs that derive from it. This involved incorporating human rights, gender and integral development approaches in the diagnosis, as well as establishing the development results approach with a long-term perspective and in

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<sup>2</sup> State of Mexico Government (2022), *Marco de Referencia de Bonos Sustentables (Sustainable Bond Framework)*, URL: <https://transparenciafiscal.edomex.gob.mx/sites/transparenciafiscal.edomex.gob.mx/files/files/informacion-oportuna/Edomex-Marco-Referencia-Bonos-Sustentables.pdf>

line with the SDGs and the 2030 Agenda goals in its objectives, strategies, lines of action, and strategic projects<sup>3</sup>.

The *Framework* is built in alignment with the *PDEM* and is structured around three of its pillars: social, economic, and territorial. In the *PDEM* each of these pillars establishes goals and indicators aimed at results. It is also linked to the 2030 Agenda goals and indicators' levels, which, in terms of planning, is one of the best practices to advance sustainable development.

**Social pillar:** The State of Mexico focused this pillar on public policies which address the social and income deprivations that are decisive for an individual to be in poverty. It also emphasized attention to vulnerable groups such as individuals in extreme poverty situations, women, and indigenous population. This government also implemented a quick response to the changes caused by the COVID-19 pandemic, through the “Strong Families” (*Familias Fuertes*) strategy which focused its efforts on income and access to education, housing, and food. Likewise, the State of Mexico has strongly promoted policies with a gender perspective, such as the “Pink Salary” (*Salario Rosa*), strategy aimed at reducing inequality and assisting women, a priority group of the 2030 Agenda.

**Economic pillar:** The State of Mexico government concentrated this pillar on three main objectives: to increase the productivity of all economic sectors in the state; to generate necessary conditions to improve their competitiveness, attract and retain employment-generating investments; and expand and promote mechanisms that allow for sustained, balanced and inclusive economic development. For this purpose, among several strategies, the State of Mexico has proposed to develop infrastructure with a vision of integral connectivity. This implies actions such as increasing, maintaining, and improving the primary roads, roads and interregional roads which facilitate the entity's connectivity in favor of the industrial and commercial development of each region. In turn, this will contribute to facilitate the transit of supplies and products to the interior or exterior of the entity, thus consolidating its logistical potential. Likewise, the improvement in road and road conditions has been identified as crucial to provide better conditions for industrial, commercial, tourist, and service development.

**Territorial pillar:** The State of Mexico's priority for this pillar is to promote an environment of resilient and sustainable cities and communities in urban and rural areas. For this purpose, the transition towards a clean and non-polluting energies generation system is promoted; actions aimed at mitigating and adapting to climate change are encouraged; the preservation of biodiversity and sustainability care; attention to human settlements and the spatial concentration of productive activity. In particular, the State of Mexico's government promotes the Metropolitan and Sustainable Urban Development program to design safe and resilient spaces with a gender perspective. It also promotes the Air Quality Management Program (ProAire 2018-2030) to reduce pollutant emissions in the long term in a transversal coordination scheme among all government areas. This program is part of the State of Mexico's broader strategy to contribute to the air quality improvement which includes actions such as reducing dependence on motorized transportation means through projects such as Bus Rapid Transit (BRTs) systems. On the other hand, the Sustainable Forest Development Program (2005-2025), implemented by Probosque, stands out, which has

established short, medium, and long-term objectives for the benefit of the environment, including air quality.

All the above evidence planning consistent with the 2030 Agenda and sustainable development, where the Bond and its strategy are framed, which allows guiding the use of resources towards development objectives that catalyze the State of Mexico's population well-being from an integral perspective.

The *Framework* establishes a selection process for *Eligible Projects* that aims, firstly, to seek the contribution of such projects to the 2030 Agenda and, secondly, to identify and minimize social or environmental risks in the policies to be financed through the Bond. To this end, it is planned to install a Sustainability Committee, composed of staff from the Ministry of Finance's General Treasury Directorate and the Planning and Programming Undersecretariat. This Committee is responsible for "the review, selection and authorization of Eligible Projects".

The participation of personnel from different departments of the public administration is a relevant element which encourages the achievement of agreements around the Projects to be financed through the Bond. In addition, the participation of the MF, the body in charge of state planning and resource allocation in the State of Mexico, is crucial considering its legal powers and the specific efforts it has undertaken to promote sustainable development. Moreover, their participation in the process contributes to an integral development vision in the allocating process of resources from the Bond.

The *Framework* lists exclusion criteria for projects or expenditures that, due to the risks of affecting sustainable development, should not be financed through the income acquired through the Bond. Additionally, three broad eligibility criteria compatible with the SDGs and the principles of sustainability, gender equality and inclusion are established. The use of indicators for the establishment of priorities and the territorial targeting of resources could be added to these criteria. Likewise, the selection process could benefit from the adoption of greater controls to resolve disputes, and the participation of sectors responsible for the *Eligible Projects*, to favor governance in the selection process.

It should be noted that the link between the *Framework* and the *PDEM* – developed under the principles of the 2030 Agenda – is an element which contributes to the selection process and the preparation of the corresponding reports being consistent with the results framework of the 2030 Agenda itself. Furthermore, the transversal axis “Capable and Responsible Government” (*Gobierno Capaz y Responsable*) foresees various strategies to align control and evaluation procedures with those authorized by the National Audit System. The latter in order to make the resources exerted from public spending transparent, coordinating control actions by external entities, attending to observations, increasing the participation of social observers and making accountability mechanisms for citizens more efficient.

The State of Mexico's Government shared a list of *Eligible Projects* to increase transparency and investors' trust. In this regard, the following was reviewed:

- Linking of the selected projects with existing problems and results that the issuing entity aims to achieve, as well as their relationship with the priorities of sustainable development and the 2030 Agenda.

- The relationship they have with problems where the issuing entity can have a significant impact.
- Consideration of the most significant risks and opportunities in terms of sustainability of the participating units, contemplating that the strongest, most resilient, and sustainable will have more capacity to positively contribute to sustainable development and the SDGs<sup>4</sup>.
- The relevance of the projects chosen to help the entity achieve its development objectives and optimize its contribution to the SDGs<sup>5</sup>.

*Eligible Projects* within the *Framework* are classified into the categories of green projects and social projects. Regarding green projects, the clean transport subcategory was defined, eligibility criteria and examples were listed, as well as alignment with three SDGs (9, 11, 13). This subcategory responds to the problems identified and directly affects the State of Mexico's objectives to adopt measures to combat climate change and mitigate its effects; and promote the prosperity of cities and their surroundings through inclusive, competitive, and sustainable urban and metropolitan development through the consolidation of a Comprehensive Sustainable Urban Mobility System in the state.

For social projects, the subcategories of 1) support for vulnerable groups and people in vulnerable situations, and 2) access to essential services, were defined, eligibility criteria, examples, and alignment with six SDGs were listed (1, 2, 3, 5, 10, 11). These subcategories are consistent with the existing problems identified in the entity, as well as with the priorities of its development strategy. They are particularly linked to the objectives of the State of Mexico to reduce poverty and promote human development, as well as reducing inequalities through attention to vulnerable groups and promoting healthy lives and the well-being of groups in greater vulnerability situations. Likewise, the categories which have been chosen, add to the objective of promoting prosperity of cities and their environment through inclusive, competitive, and sustainable urban and metropolitan development.

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<sup>4</sup> PNUD (2022), *Standard Guidance for the SDG Impact Standards for the Bond Issuers*, URL: <https://sdgimpact.undp.org/assets/Standards-Guidance-for-the-SDG-Impact-Standards-for-Bond-Issuers.pdf>

<sup>5</sup> PNUD (2021), *SDG impact standards for bonds version 1.0*, URL: [https://sdgimpact.undp.org/assets/SDG-Impact-Standards-for-Bonds-Version-1\\_0-FINAL\\_EN.pdf](https://sdgimpact.undp.org/assets/SDG-Impact-Standards-for-Bonds-Version-1_0-FINAL_EN.pdf)

## Contribution of eligible project categories to the 2030 Agenda:

Category	SDGs with direct contribution	Direct contribution	Indirect Contribution
Clean transportation	  	     	 
Support to vulnerable groups	 	 	  
Access to essential services	    	          	

As observed, the eligible projects have an impact on several SDGs, targets, and indicators of the 2030 Agenda, thus being able to have a significant impact to advance sustainable development. Although the detail of this contribution at the level of goals and indicators does not appear in the *Framework*, the State of Mexico has the information since all *Eligible Projects* are registered in the *PDEM* and have strategic indicators of these planning instruments, as well as the 2030 Agenda. Likewise, since they are large-scale projects, the agencies involved have institutionalized processes for public policy implementation.

The alignment of the *Framework* with the *PDEM* contributes to the selection process of the *Eligible Projects* and their contribution to the 2030 Agenda. The participation of the MF is a key element to seek an integral vision of development in the selection of *Eligible Projects*. The provision of eligibility and exclusion criteria provides certainty about the use of the resources. The use of indicators linked to the problems to be solved is desirable for an adequate territorial targeting of resources. The participation of other sectors is crucial, to favor the Bond's governance mechanisms. The Bond's eligible-project categories are consistent with the strategy that the State of Mexico's Government has proposed in the

*PDEM* and in its commitment to contribute to the 2030 Agenda. Likewise, the eligible project categories affect several SDGs, which allow to aspire to holistic and integral effects for sustainable development. The effort to link the *Eligible Projects* with indicators of the 2030 Agenda and the *PDEM* is to be underlined, since it places the SDGs at the center and allows measuring the effects of the Projects on social and environmental development.

## Management of resources

Regarding the management of resources, the *Framework* establishes that it will designate a separate account to make the deposit and it arranged processes for the Sustainability Committee to monitor the total allocation of the invested resources. This is in order to ensure that the Sustainability Bond net funds are transferred to the eligible categories. It has also established that the resources that have not yet been allocated will be used under the provisions of the Federal Law on Financial Discipline of the States and Municipalities, as well as the Financial Code of the State of Mexico and its Municipalities. It further established that any payment of principal and interest on the Bond will be made from a separate account and will not be linked to the implementation of any eligible project. The Bond may be used to refinance eligible projects completed in the last 36 months or in the next 36 months, in line with market practices.

On the other hand, although the Sustainability Bond does not have a labeled and final portfolio, from the information provided, it was analyzed that of the 3,000 million pesos budget for the Bond's issuance of 2022, 40% will be allocated to green projects under the subcategory of clean transport which will be implemented in conjunction with the federal government, specifically in the *Trolebús* (trolley) *Chalco Santa Martha*, as well as the extension of the *Mexibus I* and extension *Mexibus IV*<sup>6</sup>. The rest will go to the social projects category, with 52% going to the access to essential services subcategory, where twelve projects will be dedicated to infrastructure to improve mobility involving eleven municipalities<sup>7</sup>; two to Science Parks (*Parques de la Ciencia*)<sup>8</sup> and one to social projects around the Cableway Line 2 (*Teleférico Línea 2*)<sup>9</sup>. The remaining 8% will be dedicated to the subcategory of support for vulnerable groups and people in vulnerable situations through the Women City (*Ciudad Mujeres*) project that seeks to provide gender perspective comprehensive services to girls, adolescents, and women<sup>10</sup>.

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6 The involved municipalities are Trolebús (trolley) Chalco Santa Martha: Ixtapaluca and Valle de Chalco; extension of the Mexibus I: Ecatepec and Tecámac; and extension Mexibus IV: Tecámac.

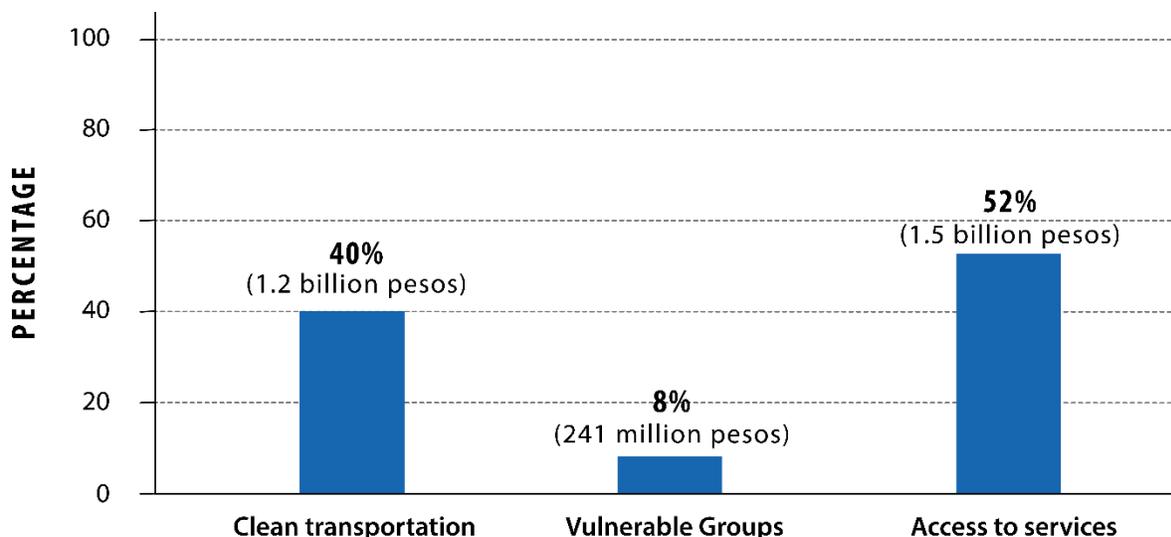
7 Almoloya de Juárez, Atizapán de Zaragoza, Chicoloapan, Chimalhuacán, Cuautitlán Izcalli, La Paz, Naucalpan de Juárez, Toluca, Valle de Bravo, Zinacantepec and the Metropolitan area of the Toluca Valley.

8 To be implemented in La Paz and Valle de Chalco.

9 To be implemented in Ecatepec and Tlalnepantla.

10 To be implemented in La Paz and San Mateo Atenco.

**Figure 1. Percentage distribution of the budget, 2022**



The State of Mexico has established processes to ensure that the resources from the Sustainability Bond are used according to the Provisions of the *Framework* and affect the green and social projects categories. The distribution of funds in the preliminary list of projects shared with UNDP is consistent with the eligible projects categories and the entity's development priorities.

### Allocation and impact reports

In April 2021, UNDP published the *SDG Impact Standards* (hereinafter referred to as the Standards) to be used as a reference to help any bond issuer to contribute to sustainable development and the SDGs. Standards are decision-making tools for operationalizing practice principles and market conventions for the issuance of sustainability bonds. In this report, UNDP in Mexico relies on the standards as a conceptual framework to review the decision-making practices and processes foreseen in the Framework of the Sustainability Bond of the *State of Mexico*<sup>11</sup>.

Regarding the allocation and impact reports, it is identified that the *Framework* provides for the publication of an allocation report on an annual basis (until all the resources raised through the Bond have been allocated). UNDP considers that the expected periodicity for the issuance of allocation reports is adequate, considering the annual budget cycles of the public administration in Mexico. Moreover, it is recognized that the publication of these reports will be carried out under transparency criteria, in accordance with the provisions of the *Framework*, which favors confidence among the investment community.

<sup>11</sup> This report does not constitute a review conducted by an accredited independent certifier. The SDGs standards are only mentioned as a conceptual framework. To obtain further details: PNUD (2022), *SDG Impact*, URL: <https://sdgimpact.undp.org/sdg-bonds.html>

As to impact reporting, the extent to which the *Framework* integrates impact management into its approach to operation and administration was analyzed<sup>12</sup>. This review sought to identify the processes and mechanisms of the issuing entity to achieve the impact strategy and goals of the Bond. This review also sought to analyze whether within the scope of its impact strategy, the entity evaluates and compares the possible positive and negative material effects of its services and operations and makes decisions among options to optimize their contribution to sustainable development and the SDGs in line with their impact targets. Finally, it was analyzed how the issuing entity systematically monitors and manages its continuous results and acts to optimize its contribution to sustainable development and the SDGs (including management of unexpected results).

The *Framework* provides for annual publication of the impact report in order to account for the effects of Eligible Projects financed by the Bond on key indicators. Just as for allocation reports, it is considered that the expected temporality is adequate, considering the programmatic and budgetary cycles in force in the State of Mexico.

In the State of Mexico there is an infrastructure for planning and monitoring the *PDEM* that exists *ex ante* to the issuance of the Bond and that starts from a legal framework that includes the constitutional scope at the federal and state level, laws, regulations, codes, and other legal instruments. The Planning Law of the State of Mexico and its Regulations, as well as the Comprehensive Development Monitoring and Evaluation System (*Sistema Integral de Monitoreo y Evaluación del Desarrollo SIMED-EDOMEX*) stand out.<sup>13</sup>

SIMED-EDOMEX, among other two aspects, monitors the strategic indicators of the PDEM aligned with the goals of the SDGs, providing timely information on the progress of the strategy of the State of Mexico's Government. This system makes visible the contributions to the 2030 Agenda of the 125 municipalities of the entity, as well as the different sectoral dependencies.

On the other hand, the projects financed by the Bond will be implemented by instances independent of the issuing entity. These agencies operate under laws, codes, regulations and procedural manuals that hold them accountable for the progress and results of each program and project, including those that will be funded by the Bond.

As for the Key Performance Indicators (KPIs), which have been proposed in the Framework at the category level for the issuance of the Bond, it is observed that they are useful tools to measure the progress of the impact that the Bond aims to achieve.

UNDP considers that the Framework establishes elements which allow to identify and objectively measure material contributions of eligible Projects in development, specifically in social and environmental dimensions. Likewise, the effort to report indicators in a disaggregated manner by relevant categories (gender and age) where possible, in accordance with the principles of the 2030 Agenda, must be recognized. Impact reports can be strengthened by territorial disaggregation of the indicators, in order to identify where the

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<sup>12</sup> Impact management is the process of identifying the positive and negative changes an organization has over individuals and the planet with the purpose of reducing the negative impacts and incrementing the positive impacts, see Impact Frontiers (before Impact Management Project) URL: <https://impactfrontiers.org/norms/five-dimensions-of-impact/>.

<sup>13</sup> This element also stands out in Sustainalytics analysis over the Framework. See Sustainalytics, *Segunda opinión Marco de Referencia del Bono de Sustentabilidad del Estado de México*, (Sustainalytics, Second opinion, Referece Framework of the State of Mexico's Sustainability Bond) May 2, 2022, <https://transparenciafiscal.edomex.gob.mx/sites/transparenciafiscal.edomex.gob.mx/files/files/informacion-oportuna/Edomex-SPO.pdf>.

main advances were made from the application of resources from the Bond. The establishment of linked allocation and impact reports is desirable.

The *Framework* provides for the annual publication of allocation and impact reports, under the transparency principle. Impact reports will reflect sex and age disaggregated effects, where possible, in line with the inclusion and gender equality approaches of the 2030 Agenda.

## **Conclusions**

In a post-pandemic context where development challenges have deepened rather than reduced, the commitment to seek management focused on well-defined results, with transparent criteria and evidence-based accountability schemes is essential. UNDP recognizes the efforts of the State of Mexico's government to promote these types of policies by issuing the Sustainability Bond for the financing of Projects that contribute to sustainable development and that can lead to very favorable institutional practices and dynamics. UNDP also reiterates its commitment to contribute to the strengthening of initiatives which promote the efficient and appropriate use of resources for sustainable development.