



# **Tourism Policy Review of Mexico – Assessment and Recommendations**

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OECD Studies on Tourism

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## ASSESSMENT AND RECOMMENDATIONS

Tourism is an important economic sector in Mexico, and the country plays a prominent role in tourism globally. The sector directly contributed 8.5% of GDP to Mexico's economy in 2014, double the OECD average (4.1%), and one of the highest direct shares of GDP among OECD countries. Tourism's impact on employment is significant, directly supporting 2.3 million full-time equivalent jobs, or 5.8% of full-time paid employment, not counting those employed in the significant informal tourism economy. Tourism's share of trade in services is also substantial, as international travel receipts accounted for 77.2% of service exports in 2015, significantly ahead of the OECD average (21.3% in 2014).

Tourism has risen in importance relative to some other sectors of the economy in recent years, notably oil. The sector quickly adjusted and recovered to pre-crisis GDP growth levels, following the impact of the international financial crisis and H1N1 influenza outbreak in 2009. International tourist arrivals have also performed strongly. However, tourism growth has lagged overall growth in the wider economy, and Mexico's travel and tourism sector has faced several difficulties, including challenging economic conditions in key source markets, natural disasters, health scares and security concerns. Recent public sector spending cuts are also impacting the resources available to develop and implement tourism policies in the short and longer term.

Tourism's potential to promote local and regional development remains largely unrealised, and the sector faces competitiveness and sustainability challenges. Attention to date has mainly focused on the development of highly concentrated coastal resorts, which in turn is reflected in tourism demand, marketing and promotion. Mexico will need to evolve this model to compete in the changing global tourism marketplace, and to spread the economic and social development benefits more widely. National tourism policy aims to encourage investment and economic growth, promote balanced regional development and stimulate more productive, inclusive and sustainable growth.

Against this background, this review provides an assessment of tourism-related policies, programmes and plans to support sustainable tourism development in Mexico. Policy recommendations focus on priority areas to help strengthen Mexico's tourism sector and take advantage of opportunities with strong potential for economic growth, investment and development, with a particular focus on the following areas: policy making environment and governance arrangements; transport, mobility and connectivity to bring visitors to and around the country; inclusive tourism growth, regional and destination development, and product diversification; and investment and SME financing.

### Profile and performance of tourism in Mexico's economy

Mexico has recorded moderate economic activity in recent years, with GDP growth projected to be 2.6% in 2016 (OECD, 2016a). This follows three decades marked by slow

growth, low productivity, pervasive labour market informality and high income inequalities in Mexico (OECD, 2015a). Despite lower oil prices and softer external demand, the OECD (2016a) expects GDP growth to strengthen to 3% in 2017, as transitory downward pressures on US demand fade away and the current government's broad and deep reform agenda begins to boost investment.

Mexico is experiencing a boom in international tourism at the moment - 2015 was a record year with 32.1 million international tourists contributing MXN 246.1 billion (USD 15.5 billion) to the economy. Since 2014, growth in people and monetary flows to Mexico has outstripped growth in many advanced and emerging tourism economies. The sharp depreciation of the Mexican peso has improved the price competitiveness of tourism exports in Mexico's main source markets, particularly in the important US market. This follows a prolonged period of modest growth in inbound tourism, relative to other countries.

Travel-related exports have made a positive contribution to Mexico's balance of payments position over the last two decades, and generate higher than average value for the economy (91% of tourism exports consist of domestically generated added value, higher than the OECD average of 80%). Tourists who travel beyond the border zone ("non-border tourists") are a higher value and more promotable market as they spend more, stay longer, and make a relatively more important, and expanding, contribution to the Mexican economy, compared to the large number of short-stay cross-border visitors. In 2015, non-border tourists accounted for 21% of international visitors, but contributed 84.4% of visitor receipts.

By virtue of its geographic location, Mexico benefits from the proximity of the United States, which is the second largest outbound market in the world, and Mexico's most important source market by a long way. While the number of tourist arrivals from the United States continues to rise and Mexico has grown its share of US outbound travel, the US share of arrivals to Mexico has fallen over the last decade (down from 87.3% in 2005 to 79.6% in 2014). Arrivals from other source markets have risen over the same period, notably Colombia which has grown by 41% each year since 2012. This points to some source market diversification and a reduced dependence on the US market. This has been helped by measures to ease visa restrictions and facilitate travel, along with improved connectivity and promotional efforts.

Domestic tourism is the mainstay of Mexico's tourism sector, contributing 88 of every 100 Mexican pesos consumed by tourists in the country. Domestic tourists are more evenly spread across the territory and make an economic contribution in regions which do not attract international visitors. International demand is heavily concentrated in sun-sea-sand destinations, including Cancún, the Riviera Maya and Los Cabos. Quintana Roo in the south-southeast region alone accounts for almost half of all international arrivals (47.5%) and almost two thirds of international overnights (62%). By comparison, 4% of domestic arrivals and 5.7% of domestic overnights are recorded in this state.

### **Towards a more integrated approach and stronger governance for tourism policy**

Tourism is high on the policy agenda in Mexico. The National Development Plan 2013-18 identifies tourism as one of six priority sectors and sets out a strategic agenda to modernise and reposition Mexico's tourism industry globally and better harness the economic potential of the sector. The Sectoral Programme for Tourism 2013-18 details the strategies and actions to achieve this. Tourism is also a core pillar of the National

Infrastructure Plan 2014-18, which recognises the need to take tourism into account in infrastructure planning and includes a dedicated tourism investment portfolio for the first time, while the Regional Development Programmes 2014-18 contain plans to harness the sector's capacity to stimulate regional economies and support local communities.

The tourism dimensions of these strategies and plans are ambitious and wide-ranging, and provide the general policy framework for tourism development in Mexico. Ensuring these plans and actions are effectively co-ordinated and implemented will be vital to realising Mexico's tourism development potential and delivering on these ambitions. This requires a stronger and more efficient governance framework and an integrated and well-co-ordinated approach across many government departments, at different levels of government, and with closer involvement of the private sector.

Mexico would particularly benefit from a more strategic approach to tourism development, and a stronger focus on implementation. The country has a remarkable range of well-articulated tourism plans, programmes and initiatives, but the strategic framework to identify policy priorities and implement actions to address these is weak. Limited information is available assessing the extent to which initiatives are prioritised and implemented, the outcomes measured and evaluated, and lessons drawn to improve future policy. More effective implementation is essential to make the most of tourism policies and programmes and deliver on Mexico's tourism policy objectives.

The current resource constraints facing policy makers in Mexico makes this situation more challenging, but also more necessary. Budgetary realities are impacting on Mexico's ability to deliver on the national tourism plans, strategies and programmes, linked with the public-sector spending and resource cuts introduced following the sharp reduction in oil-related government revenues. Staff turnover and loss of expertise is impacting the development of effective joined-up tourism policy. The political cycle also makes it difficult to develop and implement a longer-term vision for the tourism sector beyond the term of each administration.

Safety and security are important concerns for tourists around the world. Mexico has developed a suite of measures to help provide a safe and secure environment for tourists. Continued attention to these challenges is needed to respond to the evolving situation in the country, and to realise the economic and regional development potential of tourism.

As part of the wider reform agenda, Mexico has taken steps to strengthen the legal and institutional framework for tourism, and improve the regulatory environment in which the sector operates. This has included an internal restructuring of the Ministry of Tourism (SECTUR) to better respond to the changing demands of the tourism sector, and the introduction of new rules of procedure, both of which were accomplished in 2014. A further restructuring process is currently underway and is expected to be completed by the end of 2016. These reforms should focus on modernising and streamlining the institutional arrangements for tourism and more closely aligning the demand- and supply-side perspectives to ensure tourism policy is close to the market.

Mexico's multi-level government structure has implications for the governance of tourism, and the implementation of tourism policy. Strengthening co-ordination with each level of government, and the private sector, and adopting a more participative and collaborative approach would provide for more effective policy making. Such horizontal and vertical co-ordination is legally underpinned by the General Tourism Law 2009, but is challenging to achieve in practice.

Established in 2013, the Federal Tourism Cabinet is intended to be a strategic policy instrument focused on tourism policy priorities and provides a framework to support a more integrated approach to tourism policy making across government at federal level. The large number of working groups and limited progress made on some activities suggests that the Cabinet would benefit from refocusing its energies and resources on a smaller number of core priority areas. Stronger application of the criteria established to prioritise the policy issues addressed by the Cabinet, closer monitoring of progress and advance planning for transitioning projects out of the Cabinet would also help improve its effectiveness. Awareness of the impacts arising from the activities of the Cabinet is also key to ensuring continuity through political cycles.

Under Mexico's federal government structure, certain tourism policy, planning and development activities are under the responsibility of the state and municipal authorities, which play a central role in implementing national tourism policy. The Sectoral Programme for Tourism 2013-18 provides the policy framework for state and municipal level tourism plans and programmes. Co-ordination between different levels of government mainly occurs within the context of specific programmes and initiatives, notably the Programme for Sustainable Regional Tourism Development and Magic Towns (PRODERMAGICO). However, this co-ordination is not institutionalised and appears to take place largely at the technical rather than the strategic level, indicating there is significant room for improvement. Strengthening vertical co-ordination will be essential to better align policy priorities across the three levels of government, and support more effective policy implementation.

Private sector participation has been instrumental in the development and implementation of certain initiatives. However, while individual instances of successful co-ordination can be identified, engagement with industry and civil organisations does not currently take place on a regular or systematic basis, and such engagement with industry in the development and delivery of policy objectives is limited. This is largely consistent with the wider framework conditions and the strong role played by the Federal Government in planning, developing and financing tourism in Mexico over the last four decades. One of the challenges in seeking industry level policy input in Mexico is the range of industry bodies that represent different types of businesses and branches in the sector, making it difficult for tourism to speak with one voice.

### *Recommendations*

- **Develop a more strategic approach to tourism in Mexico.** Adopt a more coherent framework for identifying policy priorities and implementing actions in the short, medium and long term. Put in place mechanisms to better align strategic policy priorities across the various plans and programmes, and the three levels of government. Enhance the focus on implementation and ensure sufficient resources are allocated to priority actions. Clearly articulate a long-term vision for tourism policy to 2030 and beyond, to provide an over-arching framework for tourism plans, programmes and initiatives.
- **Improve the effectiveness of the Tourism Cabinet as a strategic tool for integrated policy development.** Strengthen the focus on core policy priorities and reduce the number of work groups and activities within the Cabinet to align with these priorities. Enhance engagement with sub-national levels of government and the private sector. Consider creating a Working Group on Implementation to

guide, evaluate and monitor progress on key aspects of policy implementation. Build on existing engagement with competent authorities to further strengthen co-ordination and address safety and security issues impacting tourism.

- **Strengthen the linkages between policy, product and promotion, and promote a more participative, market-led approach to tourism policy.** Take advantage of the current re-organisation of the Ministry of Tourism to simplify and modernise the institutional framework for tourism. Clearly set out the roles, responsibilities and linkages between the different functions within the Ministry, and strengthen the relationship with, and between, the National Fund for Tourism Development (FONATUR) and the Mexico Tourism Board (CPTM). Adopt private sector engagement strategies to encourage more active and institutionalised involvement in policy making and improve the impact of policy. Consider establishing a National Tourism Industry Council to act as the main industry interlocutor on policy matters.
- **Strengthen the evidence base to support policy development.** Enhance the integration, availability and use of robust tourism statistics to inform policy development, guide implementation and support monitoring and evaluation. Strengthen the relationship between statistical providers and users, including the National Institute for Statistics and Geography (INEGI), Bank of Mexico and the Ministry of Tourism.

### Boosting connectivity to support market diversification and move visitors around the country

Mexico is ranked ninth in the world in terms of international tourist arrivals, which could not have been achieved without a strong, dynamic transport sector. Close proximity to two important source markets, the United States and Canada, provide a natural comparative advantage for Mexico which has been leveraged to build the dynamic industry that exists today. However, while the transport system appears to work well for visitors to coastal resorts, it gets more complex outside of these tourism zones. A closer look at the tourism transportation situation in Mexico reveals areas of concern requiring attention and policy co-ordination.

Connectivity for Mexico has to be examined through an end-to-end lens bringing tourists from their point of origin to a Mexican gateway, and beyond this to the multiple places and attractions they wish to experience. This implies greater global transport connectivity to tourism source markets, domestic transport options that cater to domestic, international and mobility-reduced tourists alike, and a seamless integration and co-ordination between the outward- and inward-facing transport networks and services to allow tourists to customise their trips and discover Mexico's attractions that lie beyond its popular beaches. Domestically, it implies the need for greater point-to-point services, bypassing the country's leading hubs and making better use of low cost carriers.

Mexico enjoys excellent air connectivity between its main markets of origin, the United States and Canada, and its main tourism destinations, with Cancún, Puerto Vallarta and Los Cabos all well served. Where direct flights do not exist, connections via Mexico City or other North American hubs provide one-connection routings for most passengers. Air connectivity from Europe, Latin American and in particular Asia is weaker, and the limited direct connectivity reduces the attractiveness of destinations other than Cancún and Mexico City.

While more liberalised air service agreements with the United States and Canada will help improve connectivity with these markets, restrictions still favour the interest of Mexican carriers over that of the tourism industry and the overall economy. Saturation of Mexico City's Benito Juárez International Airport is also preventing new route development and limiting the full potential of Mexico as a hub connecting Latin America to Asia and the rest of the world, an issue that will remain until the new airport opens in late 2020. Domestic air connectivity appears to be good, with a mix of low cost carriers and a network carrier. However, it is articulated around a few key hubs which makes travel between two secondary markets longer and may require connections. Finally, airports should be connected not only to other airports but also to their city. While Mexican airports have good road connection to their city, albeit sometimes with heavy congestion like in Mexico City, there are few public transport options that would be viable for tourists carrying luggage.

Cruise ship traffic has started to recover after steep declines in the beginning of the decade but passenger numbers in 2015 remained 11% below the 6.7 million peak recorded in 2010. Cozumel is the second busiest cruise port in the world and is continuing to grow. However, cruising activity is increasingly concentrated in a smaller number of ports, with Cozumel, Ensenada and Majahual accounting for around three quarters of cruise passenger traffic. With the limited exception of Ensenada, Mexican ports are mainly ports-of-call. This limits the economic windfall that this activity provides.

Aside from air, road transport is the main option available to move visitors around the country. Also, with 57 official border crossings spread over 3 145km, road travellers have multiple options available for driving between the United States and Mexico. The road network constitutes the backbone of Mexico's transport system, but is better developed in the north and centre of the country than in the south-southeast region, reflecting the economic centre of gravity and main population centres. Mexico enjoys a well-developed and high quality inter-city bus network which offers wide coverage of destinations. However, road quality is more variable, while road safety and security are also issues.

Ground transportation can be challenging and even at times daunting for independent tourists. Accessing information and understanding the bus network is not always easy, while available public transport is not very user friendly, especially for international visitors. Tourists are often strongly encouraged to avoid public transport and rely on more expensive hotel taxis and transportation network companies for their urban mobility. Accessible transportation is also not well organised and not tourist friendly. Improving the accessibility of transport will cater to the growing number of people with impaired mobility linked with aging populations in Mexico's main source markets, as well as benefiting local people.

Against this backdrop stands a national tourism policy that seeks to bring tourists to inland destinations, diversify source markets beyond North America and offer tourists a more varied experience. With many other nearby destinations offering sun and beach vacations, Mexico's comparative advantage is the rich mix of other experiences it is able to offer visitors. In order to fully take advantage of this, Mexico requires the transport infrastructure and services to connect noteworthy communities with key global tourism markets, as well as major Mexican cities which can be significant domestic tourism generators in their own right. Lack of adequate transport infrastructure can lead to these lesser known destinations being entirely bypassed. Even when infrastructure exists, it

must be clearly indicated for tourists to find it, hence the importance of wayfinding initiatives like the National Tourism Signage Programme.

The Mexican transport system must cater to the very different needs of these domestic and international tourists. This means a transport system that is both global and local in reach, and is safe, secure and simple to navigate, easy to understand with information available in multilingual formats, makes use of modern technologies, and accessible. Transforming this aspirational goal into a realistic plan requires the transport system to be more responsive to the user's needs and make an effective use of modern communication technology to remove obstacles to seamlessness within the system.

Mexico's challenges in transport policy are to go beyond the basics and become a global leader. This will help Mexico to diversify its tourism offer and source markets, as well as strengthen tourism in regional areas and spread the benefits. Tourism stands to benefit from the significant allocations for transport under the National Infrastructure Programme 2013-18, while addressing the infrastructure gaps can also provide socio-economic opportunities for local communities in under-served regions.

### *Recommendations*

- **Better align transport and tourism policy from point of origin to destination, and make the transport system integrated and seamless for visitors and residents alike.** Develop integrated transport offerings to connect tourists with regions and attractions, including bundling the purchase of transport and tourism services, developing tourism routes and designing travel itineraries. Align local transport to the needs of tourists and properly plan public transport access to the country's main gateways, especially the new Mexico City Airport. Leverage transport to better distribute the economic benefits of tourism across the country.
- **Continue efforts to liberalise air service agreements to better support tourism and increase connectivity for all Mexican airports.** Build on the recent air service agreements with the United States and Canada. Focus on enhancing connectivity with key and emerging source markets offering the greatest potential. Make better use of low cost carriers to encourage more point-to-point domestic services. Encourage air carriers to co-ordinate schedules and improve transfer times to open up connectivity with Asia and other source markets, where current demand is insufficient to support a direct air service.
- **Improve road transport by making it safer, more secure and more efficient for tourists.** Enhance road connectivity between secondary destinations across the country and the main tourism centres and gateways, especially in the south-southeast region. Provide better information on ground transport (inter-city buses, taxi, public transport) to tourists who are planning to travel to Mexico, and real-time information during their trip. Significantly improve accessibility for people with disabilities and mobility impairments.

### **Promoting inclusive tourism growth, product diversification and destination development**

Mexico has a well-established model of tourism development based on a strong sun-sea-sand offer, largely built around the creation of centrally planned integrated coastal resorts. This model has benefited from significant public investment over the last four decades and is designed to leverage the country's natural climate and coastline

endowment. It has been very successful in attracting international demand to destinations like Cancún and Los Cabos; however, attempts to replicate this success in other destinations have met with more mixed results. Concerns have also been raised about the highly concentrated impacts of this type of development, and limited return on public investment in terms of economic and social development.

This model is now maturing, its economic impacts are very localised and its capacity to contribute to regional development and spread the benefits of tourism more widely is limited. The scale of these developments also has significant consequences for the natural and cultural environment. The existing product is strongly tailored to the traditional North American market and a lack of supply-side innovation is limiting Mexico's potential to compete in other markets. In the long term, this model is vulnerable to challenge, including from changing consumer demand patterns, environmental considerations and competitiveness issues.

A focus of tourism policy and planning in Mexico is to secure the future development of the tourism industry on a basis that is more competitive, inclusive and sustainable. It is unlikely that the existing dominant model of the resort-based sun-sea-sand product can support these three outcomes. This will require a deliberate and market-led policy focus on destination development and product diversification, supported by private sector investment. Mexico would benefit from a move to a more geographically distributed model of tourism development and the implementation of regional dispersal measures focused on developing new tourism products, routes and clusters across the country. This type of tourism development relies heavily on co-operation between different levels of government and different actors, as well as the provision of supporting infrastructure and facilities.

Such a diversification strategy should be complementary to the existing sun-sea-sand product, and should not be considered to replace it. This product will continue to be core to Mexico's tourism offer. Mexico has an opportunity to build on this to develop a more diversified, higher value tourism offer. In the future, tourism development will require two things – a refresh of the existing product, and a focus on Mexico's considerable asset base to facilitate product diversification, greater regional spread of tourism and greater inclusivity in terms of tourism employment. Maintaining competitiveness in both mature and emerging tourism products will therefore be a key challenge and priority over the medium term.

Mexico has strong alternatives for tourism development. It enjoys a considerable asset base in terms of its natural, built and cultural heritage which goes beyond its coastal environment. The potential to package new and innovative tourism experiences based on this rich and unique resource base is significant. Looking beyond conventional tourism hubs, this asset base represents an opportunity to consider tourism destination development in new locations which will better support the regional spread of the economic gains associated with tourism. This in turn will better support local jobs and incomes and open up new employment and entrepreneurship opportunities, including for women and indigenous populations, as well as providing micro-enterprises with better prospects of accessing local supply chains. A further positive feature associated with this model of tourism product diversification is that around the world, tourists are moving in this direction too.

Diversifying the tourism product and securing greater regional spread of the economic gain associated with tourism will require different policies and supports. It will mean greater involvement by government agencies with a more diverse and fragmented

group of small and micro tourism enterprises. This will require government agencies to develop a new and more nimble skill-set focused on the business development needs of small businesses. Most importantly it will require new management and leadership skills that will help overcome the inherent fragmentation in the tourism sector, and also skills that will support small businesses to integrate and cluster, so as to build some local economic scale. The fragmentation of the tourism industry tends to limit the efficacy of centrally planned policy interventions –locally based tourism entities can remain beyond the influence of central government planning.

Infrastructure development will be key to achieving a tourism industry profile based on a more diversified portfolio of tourism products, with investment in tourism-supporting infrastructure equally as important as tourism-centric investment. Ensuring tourism is taken into account in wider infrastructure planning, notably transport and internet connectivity, is required to address the infrastructure deficits currently limiting tourism's development potential, particularly in regional areas. Realising the tourism infrastructure projects in the National Infrastructure Plan 2014-18 and other programmes will also be important. Mechanisms are also needed to develop visitor services, product development and marketing, and enhance information provision.

Opportunities exist to build on existing initiatives to diversify the tourism product based on a wider and more varied asset base and promote higher value tourism markets, including developing tourism clusters associated with cultural, natural and built assets (e.g. Magic Towns, gastronomic and medical and ecotourism initiatives), as well as expand existing sub-sectors with growth potential such as gastronomy and meetings, incentives, conference and events (MICE). It is important these developments are informed by demand-side trend intelligence and by a market-led understanding of product needs, gaps and opportunities. This requires a consumer-centric, market driven approach to tourism planning, development and marketing.

Pursuing a destination development model on the basis of product diversification will thus require investment in marketing and market research. Whereas the sun-sea-sand product typically targets a homogeneous mass-market base, the market for consumers seeking a different experience of Mexico is more niche and fragmented. This will require more extensive market analysis and detailed intelligence on consumer behaviour and decision-making, including the motivating factors that prompt consumers to research and book a trip to Mexico. More information is also required on the background and characteristics of these visitors, their travel and consumption patterns, and their expectations and satisfaction with different aspects of their experience. Consumer insight and increased market segmentation and analysis should be the starting point for all tourism development programmes.

Investment in skills and capacity building is also required. A more diversified industry will be characterised by the participation of a greater number of small businesses which may lack the resources, experience and know-how of larger firms. A specific programme of supports will be necessary to promote entrepreneurship, and to assist the owners of small and micro-enterprises. It will also be necessary to develop capacity building initiatives to support policy makers at federal and state level. An emerging tourism development paradigm based on a growing level of product diversification will require new skills in the areas of strategic planning, policy implementation, horizontal and vertical co-ordination, and integration of action plans. At local government level, it

will also require a strengthened model of collaboration between local government, business groups and civil society.

### ***Recommendations***

- **Evolve the model of tourism development. Identify different destination development models, based on a geographically distributed offer and supported by tourism clusters.** Develop a more diversified, higher value market-led portfolio of tourism products and make the most of Mexico's diverse tourism assets including gastronomy, eco, adventure and MICE tourism. Evolve and rejuvenate the existing model to offer more value to consumers and open up greater opportunities to explore, encounter local experiences and take part in new activities. Promote regional tourism initiatives in existing and new destinations to stimulate local economic and social development. Capitalise on the experience with Magic Towns and other existing initiatives (e.g. medical clusters, ecotourism) as part of this new approach. Review and adjust the role of the Ministry of Tourism, FONATUR and the Mexico Tourism Board to support the new model of tourism development.
- **Target policies and interventions to support businesses in a more fragmented, smaller-scale tourism sector.** Develop the capacity and ability of public authorities at each level of government to support a new model of tourism development, based on greater regional spread, local clusters and more routine development interaction with SMEs. Promote entrepreneurship and support SMEs to grow their business and integrate into tourism value chains. Incentivise SMEs to cluster to support destination development and enhance market profile, and build capacity to deliver (and capture) scale effects, efficiencies and organisational capacity to compete in tourism supply chains. Strengthen collaboration between public and private actors, with the public sector providing a leadership role and acting as an enabler of private sector-led tourism development.
- **Support a consumer-centric, market-driven approach to product and destination development.** Ensure policy, planning, development and marketing is based on strong demand-side analysis and insight. Strengthen the capacity of government agencies to commission, analyse and utilise market-facing consumer research. Develop a mechanism to co-ordinate consumer research, monitor consumer trends in relation to lifestyle, tourism and travel, and convert research into actionable insights. Consider introducing an annual visitor survey to better understand the profile, needs and behaviours of visitors, and assess levels of satisfaction with visitor services.
- **Better align infrastructure and tourism policies.** Ensure tourism-supporting infrastructure planning is informed by a new tourism orientation to a more diverse product, which is regionally dispersed and clustered. Improve broadband access for rural tourism SMEs. Influence and inform infrastructure planning and development undertaken at federal and state level of government.

### Targeting investment and SME financing to support supply-side innovation

Mexico has in place a comprehensive public framework to finance large and small tourism projects, which have different finance needs requiring different approaches. Even where the finance opportunities are not tailored for tourism firms, they are accessible, although informality remains a barrier for many tourism businesses seeking to access external financing, particularly micro-enterprises. However, these public financing supports cater mainly to the current model of tourism development and will need to be adjusted if they are to encourage greater supply-side innovation and support a more diversified model.

Opportunities exist to better target financing to viable tourism projects of all scales and reach small and micro-firms to support product and destination diversification. This requires more rigorous assessment and evaluation to ensure funding is targeted at market-led tourism projects offering the greatest potential. It entails improved co-ordination between the different actors and levels of government, and follow-up supports to enhance the capacity of public and private actors to deliver on this potential and ensure optimal use of public funds. Financing a new model of tourism development also involves the public sector moving from a direct investment role to a more supporting role as a private sector investment facilitator.

Mexico has a well-developed tourism investment model which operates through FONATUR and supports the dominant sun-sea-sand offer. Developed over 40 years ago, this supply-side model finances large-scale, centrally-planned tourism projects, particularly in the resort hotel sector, using these investments to leverage private sector participation. However, the model has struggled in recent years to replicate its early success in attracting investors to new tourism developments. FONATUR finances have deteriorated, linked with the global financial crisis, underlying weaknesses in the business model and other demand-side conditions. Following a financial and organisational restructure in 2012, FONATUR is modifying its business model to promote a broader set of destinations, and finance smaller-scale investment projects, including SMEs. This re-orientation should be supported and strengthened, in order to harness FONATUR experience and know-how to support a new model of tourism development.

The public component of financing tourism development in Mexico is more significant compared to other OECD countries. There are well-known structural reasons that explain such intervention, at least on a temporary basis (e.g. high levels of financial exclusion and underdeveloped credit and capital markets). Tourism development has benefited from significant government investment, and public development banks play a strong role in providing credit, sometimes at subsidised rates which risk crowding out the private sector. The recent reduction and reconfiguration of public budget allocations is constraining the capacity of several ministries and agencies, including the Ministry of Tourism and the National Institute for Entrepreneurship (INADEM), to provide funding to viable private sector-led tourism projects, and also complicates long-term planning. Insufficient funding to meet demand may also reflect a lack of prioritisation or strategic approach to ensure financing is directed to projects with the strongest potential.

Financial reforms are strengthening the role of public banks in counter-cyclically financing SMEs, and creating products capable of increasing participation in the finance market, including women. These reforms are benefiting tourism firms, with an increase in both the level of credit and number of firms financed through the Mexican Foreign Trade Bank (Bancomext). The reforms will also support the diversification of the tourism offer,

including in rural areas and communities. The creation and uptake of new capital market investment finance vehicles, including infrastructure and real estate trust vehicles (FIBRAs) and capital development certificates (CKDs), have strongly contributed to attracting private sector-led investment in the tourism real estate market (e.g. the creation of hotels in agro-industrial corridors). However, these instruments are better suited to the development of hotels which are part of an international chain and cater to the business market, rather than all-inclusive resorts and independent hotels which account for the majority of the sector in Mexico and are more likely to cater to the leisure market.

Mexico can build on its experience using public-private partnerships (PPPs) to leverage network infrastructure investments (roads, connectivity, water and sewage treatment) to strengthen future tourism-related PPPs, which can provide the necessary funding, expertise and demand-side view for potential projects. However, horizontal and vertical co-ordination remain a challenge, as these activities are decided and financed at the sub-national level, often with support from the federal government, while the capacity to implement these activities at local level is an issue.

Mexico is promoted as a destination for foreign direct investment (FDI) in large-scale commercial tourism-related projects, but has seen declines in FDI inflows in the sector, which are subject to the macroeconomic conditions in the both the host and source country. This limits in part the scope for Mexico to influence FDI inflows for tourism. Attracting FDI also has the potential to indirectly benefit tourism SMEs, but to secure these benefits Mexico has to ensure that FDI investments connect with local firms, promote knowledge transfer and create local linkages that will enable SMEs integrate into global value chains.

For tourism SMEs and entrepreneurs, Mexico has a wide range of dedicated and general finance instruments available. Financing constraints on the supply (small scale of funding relative to transaction costs) and demand side (lack of financial knowledge, culture and collateral, high informality) mean that tourism SMEs are unlikely to be financed through the commercial banking system. Public supports play an important role in this context, to capture the wider economic and social benefits and support the finance needs of firms in certain geographic areas. Mexico offers standard loans and credit guarantee programmes with public support through the private credit market, as well as programmes providing access to venture capital and credit to fund start-ups or expand SMEs and innovative micro-enterprises. However, access to finance is only part of the story as issues remain around the uptake and effective use of these instruments. Non-financial supports are also important for tourism SMEs. To address this, the finance products available make provision for technical assistance and mentoring.

Since 2012, the INADEM promotes entrepreneurship development and provides comprehensive support for SMEs in all sectors. Tourism SMEs are covered by these supports, but INADEM does not have a specific tourism mandate or budget, unlike Bancomext. There is potential to strengthen INADEM role to match viable tourism-related projects with finance opportunities, provide capacity building and mentoring, and help small firms integrate into value chains and enterprise networks, to benefit from economies of scale. Strengthening and expanding the role of the Tourism Enterprise Attention Centres and Rapid Business Start-up System (CAET-SARE) can reduce informality and is a starting point to build on financing tourism SMEs.

### *Recommendations*

- **Direct financing to tourism projects offering the strongest potential and ensure more strategic and efficient use of public monies.** Undertake more robust assessment and evaluation of public investment in tourism. Examine the cost and potential welfare gains of using subsidies to finance tourism-development projects, particularly in the context of overall constrained resources. Establish ex-ante fiscal caps on public sector finance provision. Improve co-ordination between levels of government and implementing agencies. Capitalise on Mexico's experience using public-private partnerships to finance basic infrastructure to support tourism development. Consider the provision of finance for tourism projects within a wider destination context, to support the creation of routes, clusters and strategic destination developments.
- **Support better uptake and use of financing opportunities by small and micro-enterprises.** Strengthen the role of INADEM in providing financial and non-financial supports to small and micro tourism enterprises. Improve the financial capacity of small and micro-enterprises through technical assistance and mentoring. Encourage tourism enterprises to formalise and move out of the informal economy, including through administrative simplification and expanding the role of the Tourism Enterprise Attention Centres and Rapid Business Start-up System. Explore the potential of alternative financing sources (channelling remittances through crowdfunding, micro-finance) that bring a private sector perspective to the selection and funding of projects.
- **Capitalise on the capacity for FONATUR to be a pivotal actor in financing and engineering a new model of tourism development.** Support FONATUR in driving the implementation of a new model of tourism development from design to evaluation, under the leadership of the Ministry of Tourism. Build synergies between FONATUR, INADEM and other financing actors to foment and support product and destination diversification. Strengthen Mexico's leadership on tourism development in Latin America by exporting FONATUR know-how in tourism engineering and providing advisory services to countries in the region.

