Technical Cooperation Document

I. Basic Project Data

▪ Country/Region:	Regional
▪ TC Name:	Delivering Sustainable Finance: Connecting Financial Markets with Sustainable Assets
▪ TC Number:	RG-T2956
▪ Team Leader/Members:	Giovanni Leo Frisari (CSD/CCS) team leader; Hilen Meirovich (INO/NFP) co-team leader; Barbara Brakarz (CSD/CCS), Graham Watkins (CSD/CCS), Gmelina Ramirez (CSD/CCS), Jennifer Doherty-Bigara (CSD/CCS); Sven-Uwe Mueller (CSD/CSD); Tomás Serebrisky (INE/INE), Maria Cecilia Ramirez (INE/INE), Hendrik Meller (INE/INE); Maria Netto (IFD/CMF), Isabelle Braly-Cartiller (IFD/CMF), Omar Villacorta (IFD/CMF); Maria Tapia Bonilla (BDA/ACP), Jan Weiss (INO/FNP), Chiara Trabacchi (INO/NFP); Pilar Jimenez (LEG/SGO), Carlos Güiza (CSD/CCS), Maria Fernanda Alva (CSD/CCS), Juan Carlos Gomez (CSD/CCS).
▪ Taxonomy:	Research and Dissemination
▪ Beneficiary:	Latin-American and the Caribbean countries
▪ Executing Agency:	Inter-American Development Bank
▪ Donor:	Sustainable Energy and Climate Change Multi-Donor Fund (MSC)
▪ IDB Funding Requested:	US$1,000,000
▪ Local counterpart funding:	US$250,000
▪ Disbursement period:	36 months
▪ Types of consultants:	Individuals and firms
▪ Prepared by Unit:	CCS
▪ Unit of Disbursement Responsibility:	CSD
▪ TC Included in Country Strategy:	No
▪ TC Included in CPD:	No
▪ Alignment with the Update to the Institutional Strategy:	Productivity and Innovation; Climate Change and Environmental Sustainability, and institutional capacity and rule of law.

II. Objective and Justification

2.1 The main objective of this technical cooperation (TC) is to support the mobilization of investment capital, particularly from domestic financial institutions in Latin America, towards sustainable infrastructure investments, which within the Inter-American Development Bank (IDB) and Inter-American Investment Corporation (IIC) (IDB Group, IDBG) context, are defined as financially, economically, environmentally and socially sustainable assets. This objective will be achieved by carrying out actions aimed at improving the investment processes and procedures of such financial institutions and other relevant actors. More specifically: (i) promote the adoption and implementation of commonly agreed sustainability definitions, criteria and approaches; (ii) support the development of innovative financial instruments mainly in domestic financial markets; and (iii) assist relevant public and private sector actors in understanding and managing the challenges associated to assets' sustainability, as well as mobilizing resources to finance sustainable infrastructure investments.

2.2 A transformational shift of financial resources towards sustainable investments in infrastructure both in traditional ones such as energy and transport, as well as natural infrastructures such as forest landscapes, is crucial to meet the objectives of the Paris Agreement. The Agreement aims to (i) keep global temperatures from rising well below 2°C by the end of the century; (ii) increase the ability to adapt to climate change impacts (and manage climate risks); and (iii) ensure finance flows are consistent with a pathway towards low greenhouse gas emissions and climate resilient development.

2.3 There is compelling evidence about the sizable global infrastructure gap – both in terms of quantity and quality[1] - that countries around the world are struggling to finance, and which could worsen if such countries were not meet the goals established in their Nationally Determined Contributions (NDCs). Global cumulative infrastructure investment needs until 2030 have been estimated at about US$89 trillion, with an incremental cost of US$4 trillion if sustainability is factored in. Based on current investment flows, countries are expected to have an investment shortfall that ranges from US$39 trillion to US$51 trillion for the next 15 years. For the Latin America and the Caribbean (LAC) region, this implies an estimated incremental investment of about US$120-150 billion annually over the next several years, in addition to US$30 billion to incorporate mitigation and adaptation measures into those investments. Given fiscal constraints in the region, governments will not be able to attain their goals with just their public budgets. Private capital will need to be mobilized towards these needed investments, particularly from institutional investors, who manage assets of approximately US$72 trillion in both equity and debt instruments.

2.4 Financial stakeholders are increasingly becoming aware that the environmental, social and economic sustainability aspects of their investments could have significant impacts on their risk-adjusted expected returns. “Sustainable finance” is evolving from a risk management practice, towards an investment strategy that balances the need to deliver long-term value in the context of increased uncertainty. Some examples of such practice are: (i) institutional investors are increasingly adopting responsible investment practices: the United Nations’ Principles for Responsible Investment initiative have over 1,500 members, who manage assets for more than US$50 trillion; (ii) banks and insurance companies are increasingly taking into account environmental, social and governance risks in their financial decisions, with over 70% of project finance in developing countries following the Equator Principles; (iii) stock exchanges are increasingly requiring listed companies to report on sustainability considerations and demanding the issuance of securities to be aligned with voluntary sustainability standards. The issuance of green bonds on the Luxembourg Green Exchange is the most recent example; (iv) companies are gradually incorporating sustainability in their business planning and reporting to stakeholders, who now request additional transparency regarding the exposure to climate-related financial risks. Accordingly, the Financial Stability Board launched the Task Force on Climate-related Disclosure in 2015 to promote more effective climate-related financial disclosures in support of climate-informed investments, enable investors to better manage their portfolios’ exposure to climate-related risks and ensure the stability of financial systems.

2.5 However, an excessive fragmentation of sustainability standards, principles and initiatives, and the lack of commonly shared approaches is increasing investors’ transaction costs and hindering their ability to assess investment in sustainable assets.

[1] See, for example, McKinsey (2016) Bridging global infrastructure gaps.

Thanks to an already established intensive internal and external collaboration with relevant players[2] in this field the IDBG is strategically positioned to lead the convening of key global and regional stakeholders (e.g. existing initiatives, financial regulators, central banks and leading financial institutions), in order to develop and support the implementation of a commonly agreed definition, governing principles and criteria for sustainable investments. Within this framework, it is also well position to create the knowledge and the tools needed to enable an implementation strategy by investors and governments in the region.

2.6 This TC aims at advancing the innovative work started with the TC operation "Framework to Foster Sustainable Elements in Infrastructure Projects" (ATN/OC-14981-RG) to create awareness about the importance to incorporate sustainability considerations in investments. The findings of this TC operation[3] and their dissemination have demonstrated that momentum around sustainable investments has been rising over the last few years. However, they also highlighted that there is a pressing need to continue the process of awareness creation and, more importantly, of agreeing on a consistent and applicable set of relevant definitions and principles, and strategies to translate momentum into tangible investments. This operation will contribute to, and benefit from the work of the IDBG Sustainable Infrastructure Working Group, currently developing a comprehensive definition for Sustainable Infrastructure, that will be defined in consensus with both its public and private sector relevant divisions.

2.7 The work proposed in this TC will complement the actions from the TC "Mapping Infrastructure Private Investors in Latin America and the Caribbean: Challenges of Mainstreaming Infrastructure as an Asset Class" (ATN/OC-15496-RG) executed by the Infrastructure and Energy Department of the IDB (INE), which led a specific analysis on investment flows towards infrastructure in LAC, the nature of the key investors and their investment drivers. It also relates to the Economic and Sectoral Work (ESW) jointly led by INE and the Climate Change and Sustainable Development Department of the IDB (CSD) (RG-K1384/RG-K1400), which seeks opportunities to generate sustainability-related knowledge from IDBG's operations, as well as advance the dialogue about sustainable infrastructure both within the bank and amongst decision-makers in the region. The results of this TC are expected to add value to the operation "Financing Implementation of Intended Nationally Determined Contributions" (ATN/MC-15367-RG), as it will intensify the ongoing conversations with LAC's ministries of finance on the needs and opportunities to align their infrastructure investments with their NDC targets.

2.8 The operation is also consistent with the Update to the Institutional Strategy (UIS) 2010-2020 (AB-3008) and aligned with the development challenge of productivity and innovation, as it will assist stakeholders to develop and implement innovative instruments aimed at scaling up sustainable infrastructure investments that take into account the sustainability of social and environmental aspects of the financing. The TC is also aligned with the crosscutting themes of (i) climate change and

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[2] The Brookings Institution, Mercer, the PPIAF[2] Facility, the World Economic Forum, the UN Principles for Responsible Investment.

[3] As published in the report "Crossing the Bridge to Sustainable Infrastructure Investing", despite significant activity around sustainable infrastructure with several initiatives formed in the recent years and currently active, and many investors improving their ESG capacities, there's however little evidence of sustainability strategies entering in the core investment process of leading financial institutions. Several reasons have been reported: Lack of familiarity with the business case for sustainable infrastructure; limited standardization of tools and approaches; lack of coordinated policy signals.

environmental sustainability; and (ii) institutional capacity and rule of law, as a common definition of sustainable infrastructure involves environmentally and socially investments that will contribute to the development of climate finance policies in LAC. Additionally, the program will contribute to the Corporate Results Framework 2016-2019 (GN-2727-4) (CRF) by strengthening the capacity of decision-makers and financing institutions –both public and private, to improve the sustainability of their portfolio in terms of the life of the financed asset, its impacts on the environment and the returns it yields, within a context of internationally standardized criteria. The operation is also consistent with the goals of the "Integrated Strategy for Climate Change Adaptation and Mitigation, and Sustainable and Renewable Energy" (GN-2609-1), the Climate Change Sector Framework Document (GN-2835-3) and the Sustainable Infrastructure for Competitiveness and Inclusive Growth (GN-2710-5), which highlight the importance of ensuring the sustainability of future investments in the LAC region. In addition, the operation seeks to develop studies and targeted activities aimed at reducing the barriers to investments in sustainable infrastructure, including renewable energy and energy efficiency. In this sense, it aligns with the objectives of the Sustainable Energy and Climate Change Multidonor Fund (GN-2435-6), which seeks to increase these investments in LAC and reduce vulnerability to climate change.

III. Description of Activities/Components and Budget[4]

3.1 This TC aims at supporting the following activities: (i) identify and profile institutional investors active in LAC, as well as assess sustainable infrastructure investment strategies, with attention to domestic financial markets; (ii) generate evidence of the long-term benefits of sustainable investment practices; (iii) support policymakers and private sector actors to implement sustainable investment strategies and comply with new and emerging regulations; and (iv) convene relevant global and local actors to facilitate knowledge exchange and peer-to-peer education, in order to develop strategies, financial instruments and investment tools for sustainable infrastructure investments.

3.2 The intention of the work program is to facilitate the development of analytical work in partnership with public and private sector actors, and will entail the organization of regional roundtables in key financial markets in the region in venues such as the Leadership Program for Sustainable Finance in LAC currently under design by the IIC. The gatherings in the roundtable will bring to LAC the dialogue initiated in a series of workshops "Convene the Conveners –Shifting the Paradigm towards Sustainable Infrastructure" organized by IDB in collaboration with global partners (e.g. an event in Berlin with GIZ and Mercer). In this first phase, the analytical work and the in-country dialogues will focus on selected countries of the region (approximately 4 or 5), characterized by significant infrastructure investments and domestic financial markets with active local and international institutional investors. The team will try to keep a balance across IDB regional departments, to ensure that results and lessons are disseminated across the region to promote and support sustainable infrastructure investments and the development of local capital markets.

3.3. **Component 1. Promote sustainable infrastructure investment strategies and support their adoption in LAC (US$400,000).** This component draws from the publication "Crossing the Bridge to Sustainable Infrastructure Investing" (IDB and Mercer,

[4] The IDB personnel will support and supervise the execution of this TC and will provide technical and strategic support to high level and dissemination meetings.

2017) and one of its final recommendations for "Clarifying, Committing, Convening and Collaborate" with other institutions engaged in promoting the sustainable infrastructure agenda. It includes a review of investment strategies and financial models for sustainable investments currently available in LAC, which focus on local financial markets, as well as a dialogue about the instruments, policies and regulations that could ensure the promotion of sustainable investments at scale and the mobilization of domestic and cross-border financing in LAC. The review will analyze countries' infrastructure investment pipelines and compare them with investment strategies implemented by investors active in LAC financial markets, highlighting their risk appetite for sustainable infrastructure and the challenges in assessing sustainability and seizing related opportunities. The analysis will constitute the basis for a collaboration effort between policymakers, regulators, and the financial sector, to promote best practices and support the implementation of sustainable investment strategies that are consistent with sustainable infrastructure plans and pipelines originated by governments in the region. The collaboration will take the form of a regional dialogue with domestic and international investors, regulators and policymakers which will engage with the region's dynamics and specific barriers to support investments sustainable infrastructure in LAC, mobilizing domestic and cross-border capital.

3.4. **Component 2. Demonstrate the business case for sustainable investments (US$100,000).** This work will generate quantitative, sector-specific evidence on how sustainability considerations are not only desirable to help achieve global development and climate goals, but are also supportive of long-term financial viability. Selected LAC-based projects will be used to study the costs of incorporating sustainability aspects in the infrastructure design and the way those costs balance out with the sustainability benefits along the project cycle (or with downside risks and costs of unsustainable investments). This component will finance simulations on case studies, focusing on at least one project from each economic infrastructure sector (water, energy and transport). Clearly identifying how the inclusion of sustainability modifies the assumptions and conclusions of traditional cost-benefit analyses will turn into valuable information to disseminate among IDB clients and partners, and supporting the IDB's efforts to mainstream a sustainable approach towards infrastructure by public and private sectors in LAC –including mainly the financial sector.

3.5. **Component 3. Support the implementation of sustainable investments in the regulation and management of financial markets in LAC (US$200,000).** Developed in combination with the ESW RG-E1532 "Deepening the economic assessment on climate change", this work stream will support the incorporation of sustainability practices in domestic capital markets in selected LAC countries through the assessment of the current regulatory frameworks and the analysis of the available financial instruments and their effectiveness in mobilizing resources in each market. While benefiting from the existing IDB's network among regulators and policymakers in the region, this component will aim to create partnerships with central banks, supervisory agencies and market regulators (including stock exchanges) to design strategies, products and regulatory tools to support investors in mobilizing resources towards sustainable assets and in complying with sustainability requirements in their investment process.

3.6. **Component 4. Support the implementation of sustainable investments by financial institutions (US$200,000).** This component will build on the work of Components 1, 2 and 3. It aims at providing support to the practical implementation of sustainable finance practices by financial institutions operating in LAC (e.g. commercial banks, asset managers, national securities entities, central banks, institutional investors, banking

networks, and capital markets). Based on availability and demand, the activities envisaged under this Component will seek to support one or more IDBG's clients or prospects to e.g.: (i) integrate environmental, social and governance factors in core business models, policy and governance practices and/or investment analysis and capital allocation decision-making processes; (ii) familiarize and use ESG data, information, index and/or ESG reporting; (iii) familiarize with and internalize emerging climate-related financial risk disclosure strategies; (iv) understand the business opportunity offered by sustainable finance markets/assets; and (v) develop and/or invest in sustainable investments vehicles or assets such as green bonds or asset-back securities. Interested clients will be identified on the basis of their interest and commitment to sustainability and to implement change; the additionality of these resources to influence change in their process; their relevance and impact on the financial stability of their context; and the replication potential of any given intervention.

3.7. **Component 5. Outreach and dissemination (US$100,000).** This component will develop activities with the public and/or private sector in LAC to: (i) create awareness; (ii) disseminate and validate the findings; and (iii) promote a dialogue between public and private stakeholders. This component includes publications and events such as workshops and conferences to be developed during the execution of the operation, in accordance with global and regional meetings focused on financing and developing sustainable infrastructure, such as the Infrastructure Investor Global Summit, the World Economic Forum, and the Global Infrastructure Forum.

Indicative Budget (US$)[5]

Component	IDB Funding	Counterpart	Total
Component 1. Promote sustainable infrastructure investment strategies and support their adoption in LAC	400,000	0	500,000
Component 2. Demonstrate the business case for sustainable investments	100,000	0	100,000
Component 3. Support the implementation of sustainable investments in the regulation and management of financial markets in LAC	170,000	125,000	245,000
Component 4. Support the implementation of sustainable investments by financial institutions	180,000	125,000	255,000
Component 5. Outreach and dissemination	100,000	0	100,000
Contingencies	50,000	0	50,000
Total	**1,000,000**	**250,000**	**1,250,000**

3.8. The total cost of the operation is US$1,250,000 out of which US$1,000,000 will be financed with resources from the Sustainable Energy and Climate Change Multi-Donor Fund (MSC). The remaining amount is the estimated in-kind client contribution consisting of the sum of men-hours by participating professionals from different private sector and governmental teams for the provision of information and expert opinions in

5 This amount includes the costs associated with the participation of IDB sector specialists in the program for purposes of monitoring and supervising the products, and collaborating with the consultants and stakeholders from academia and cities involved during the elaboration of the products and their dissemination. This is required to be able to monitor the products of the TC and to disseminate them to all the beneficiaries. The specialists will provide technical knowledge and will: (i) participate in the dissemination events to monitor and supervise outcomes; (ii) participate in meetings with study counterparties in the region; and (iii) participate in technical workshops and knowledge exchange with key stakeholders. The participation of sector specialists in the TC activities is essential to achieve its objectives. Specific tasks necessary for the implementation of this operation do not constitute functions or tasks that may be considered as routine by the divisions or part of the general tasks covered by administrative budget resources.

the workshops, and review of the technical reports generated through this TC.[6] In addition, the in-kind client contribution will include on-going relevant national studies such as the NDC Action Plans, capital markets sectoral strategies and/or sectoral methodologies for the regulation of financial markets that contribute to the operation's objective.

IV. Executing Agency and Execution Structure

4.1 This operation will be executed by the Climate Change Division of the IDB (CCS), in close collaboration with the IIC Advisory and Blended Finance Team – co-leading the operation, the IIC Financial Products and Services Division, and the IDB Infrastructure and the Capital Markets and Financial Institutions Divisions.

4.2 The execution structure will be based on the coverage of the regional activities to be performed, which encompass possible synergies and complementarities with the IDB's operations and research (e.g. two ESWs on climate risk and sustainable infrastructure, the 2016 Regional Policy Dialogue and operations such as "Financing Implementation of Intended Nationally Determined Contributions" (ATN/MC-15367-RG) and "Support to Climate Change Units within Ministries of Finance" (ATN/OC-13069-RG)), in addition to the ongoing dialogue with relevant ministries in the region. CCS will coordinate with other relevant divisions of the IDBG including the public and private sectors, and will aim to create partnerships with key stakeholders including the academia and national governments.

4.3 Given that this research and dissemination TC is being processed by the Bank's initiative, there is no client request letter at this point. However, non-objection letters will be requested. However, non-objection letters will be requested prior to the start of the project's activities in subject countries particularly those related to Components 3 and 4.

4.4 The IDB will hire individual consultants, consulting firms and non-consulting services in accordance with current Bank procurement policies and procedures.

V. Project Risks and Issues

5.1 The main risks for the successful and timely execution of the TC are the availability and quality of the information to be gathered and the level of qualification of the consultants required to perform the analyses and work proposed. To address and minimize these risks, progress has been made in the identification of trustworthy information sources, as well as a pool of candidates with the skills and experience needed to perform the required tasks.

VI. Environmental and Social Classification

6.1 According to the Environment and Safeguards Compliance Policy of the IDB (OP-703), operation has been classified as "C" (see the corresponding Safeguard Screening Form and the Safeguard Policy Filter).

VII. Required Annexes

Annex I: Results Matrix

Annex II: Terms of Reference

Annex III: Procurement Plan

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[6] Given that the in-kind contribution will depend upon clients' demand, the actual in-kind contribution will be determined as clients confirm their participation.

DELIVERING SUSTAINABLE FINANCE: CONNECTING FINANCIAL MARKETS WITH SUSTAINABLE ASSETS

RG-T2956

CERTIFICATION

I hereby certify that this operation was approved for financing under **Sustainable Energy and Climate Change Multi-Donor Fund (MSC)** through a communication dated March 30, 2017 and signed by Felipe Caicedo (ORP/GCM). Also, I certify that resources from said fund are available for up to **US$1,000,000** in order to finance the activities described and budgeted in this document. This certification reserves resource for the referenced project for a period of four (4) calendar months counted from the date of eligibility from the funding source. If the project is not approved by the IDB within that period, the reserve of resources will be cancelled, except in the case a new certification is granted. The commitment and disbursement of these resources shall be made only by the Bank in US dollars. The same currency shall be used to stipulate the remuneration and payments to consultants, except in the case of local consultants working in their own borrowing member country who shall have their remuneration defined and paid in the currency of such country. No resources of the Fund shall be made available to cover amounts greater than the amount certified herein above for the implementation of this operation. Amounts greater than the certified amount may arise from commitments on contracts denominated in a currency other than the Fund currency, resulting in currency exchange rate differences, represent a risk that will not be absorbed by the Fund.

Original Signed 07/27/2017

Sonia M. Rivera Date

Chief

Grants and Co-Financing Management Unit

ORP/GCM

Approved: **Original Signed** 07/31/2017

Juan Pablo Bonilla Date

Manager

Climate Change and Sustainable Development Sector

CSD/CSD