

Environmental and Social Management Report
Banco Improsa
CR-L1058

I. Project Description and Background

- 1.1 The proposed project entails a financing facility (the “Facility”) that will enable Banco Improsa S.A. (“Improsa”) to broaden and deepen the scope of its lending to small and medium-sized enterprises (“SME”) in Costa Rica. The Facility, with a tenor of up to three years, would provide a senior secured A loan (the “A Loan”) of up to US\$8 million to be financed by IDB and, a targeted B Loan (the “B Loan”) of approximately US\$5 million, or such other amount to be determined based on market conditions and the needs of the client, to be financed by commercial investors.
- 1.2 The A-Loan would be used to support Improsa’s expansion in SME financing (which currently represents between 85% and 95% of the bank’s portfolio), which would entail a further downscaling and a move to certain segments different from their traditional focus. Through IDB financing, Improsa aims to both increase its portfolio allocation to housing finance, and also increase its market share in the segment. In addition, Improsa will also look to extend credit to new segments within SMEs, such as agricultural cooperatives.
- 1.3 Improsa began operations as Financiera Improsa S.A. in 1986, later becoming Banco Improsa S.A. in 1995. As of December 2011, Improsa ranked as the eleventh bank in the Costa Rican system in terms of assets, with a market share of 1.7 percent. Its market share among private banks is 4.7 percent, and ranks seventh in that segment.
- 1.4 Improsa follows a business model centered on serving small and medium-size enterprises (SMEs), with emphasis given to intensifying this effort in its updated strategic plan for 2012-2015. The bank has received significant credit and capital support from several development institutions such as the IFC, FMO, DEG, BCIE and more recently, BIO. Improsa is now looking to expand its SME coverage to include agricultural cooperatives and other related activity. This Facility would also support this plan.
- 1.5 In the context of the Costa Rican banking sector, Improsa would qualify as a small bank, although would be considered a medium-sized bank in the context of its private sector peers. It has a network of five branches, including two SME centers, Centros de Apoyo y Asesoría Pyme, all focused on the greater metropolitan area of San Jose, serving a total of about 1,500 business clients as of December 2011 and 225 employees.
- 1.6 The Facility would be the first IDB transaction under the Regional SME Financing Facility (RG-X1092), approved in 2011, with a financial institution in Costa Rica and will help IDB advance towards its goal of promoting economic, social, and environmental sustainability in the region by contributing to support Improsa’s strategic loan allocation objectives with regards to SME lending. This is a market segment that often does not necessarily benefit optimally

from the available social programs and at the same time do not have ready access to other kinds of commercial credit.

II. Project Status and Compliance

- 2.1 Given that this operation is being undertaken as part of the Regional SME Facility, authorization is delegated to IDB Management. The Regional SME Facility was approved by the IDB in 2011 and included an Environmental and Social Management Procedure, for the use of proceeds of the Facility, which is being applied to this Facility. The Procedure ensures that potential environmental and social risks and impacts are identified and assessed, commensurate requirements for environmental and social management of these risks and impacts are set out in the relevant documents, and that the environmental and social aspects of these operations are adequately monitored and reported upon. Effectively, each participating FI will undergo an individual and tailored environmental and social due diligence (ESDD) and will require an individual and tailored Environmental and Social Management Report (ESMR – this document), which will be annexed to each individual Loan Proposal. The requirements determined as a result of the ESDD and set out in the ESMR will be translated into the covenants, representations and guarantees, or other applicable clauses of the Loan Contract.
- 2.2 Based on Directive B.13 of the Environment and Safeguards Compliance Policy (OP-703), and given this is a financial intermediary project, this operation is not categorized, according to its potential environmental and social impacts and risks.
- 2.3 Banco Improsa has confirmed that it is in compliance with Directive B.2 (country laws and regulations) of IDB Environment and Safeguards Compliance Policy, complying with all applicable legal and regulatory environmental, social, health and safety, and labor laws and regulations including permits and authorizations.

III. Environmental and Social Risks and Impacts

a. Potential risks and impacts associated with Improsa's portfolio

- 3.1 Improsa's total investments as of 2011 amounted to US\$90.5 million (up from about US\$74 million in 2010), which is largely composed of SMEs, about 85% to 90% of total loans. While the focus is to strategically remain with the SME segment, Improsa is looking to reverse the recent declining trend and begin growing, while also diversifying the portfolio by including additional sub-sectors, most notably small-scale agri-business (agricultural cooperatives) and the larger segment of the SME sector.
- 3.2 Banco Improsa defines an SME as a company with US\$2M to US\$4.5M in sales with between 50 and 100 employees.
- 3.3 Improsa's portfolio is varied and overall may be considered as having minimal to moderate risks and impacts associated with it. As of December 31st, 2011, the most significant sectors in

which Banco Improsa is working were: construction (18%); services (15%), commercial (15%), real estate (13%); finance and brokerage activities (12%) and industry and manufacturing (10%). Improsa also has significantly smaller exposure in sectors such as transport, agriculture, hotels and mining.

- 3.4 There are specific ESHS and labor impacts and risks related to investment these sectors, for example related to trade and commerce of products and substances subject to bans and international phase outs (commercial); habitat conversion and degradation (agriculture, construction, transport); occupational health and safety (agriculture, construction, transport); poor land use (construction, agriculture); noise and air pollution (manufacturing, construction, mining), increased greenhouse gas emissions (manufacturing), natural disasters, such as earthquakes, forest fires and landslides.
- 3.5 These risks are considered minimal to moderate (currently Improsa has 2 Category A operations in its portfolio) and may be mitigated and managed through Improsa's existing Environmental and Social Management System (ESMS). See section IV below.

b. Risks associated with Improsas's facilities and human resources

- 3.3 The risks associated with Improsa's facilities and operations, such as environmental liabilities in their offices due to asbestos, lead paint, etc. or Improsa employees having occupational health and safety problems due to working conditions (e.g. inadequate emergency preparedness, lack of fire exits, etc) are considered to be minimal. Improsa's head office is located in San Jose, Costa Rica.
- 3.4 Improsa has stated that they have no material health issues (including legal claims) and do not have any materials employee or labor disputes. Improsa has also stated that its finance application and analysis process is equitable, fair, and unbiased in terms of social factors (e.g. gender, age, ethnicity, or cultural heritage).

IV. Environmental and Social Management

- 4.1 Improsa has received support of several development institutions such as the IFC, FMO, DEG, BCIE and BIO. In 2002, Improsa developed an ESMS which is included in their Environmental Policy (*Politica Ambiental y Procedimiento para el Analisis de Riesgo Ambiental*). This has subsequently been updated, and the most recent version approved in October 2011.
- 4.2 The policy applies to all operations financed by Improsa and consists on an exclusion list, consistent with the NSG List of Excluded Activities, categorization of environmental and social impact, following an A, B, C, FI model (considering the type of operation, size, location, nature and magnitude of impacts), consistent with IDB Environment and Safeguards Compliance Policy. Detailed guidance is provided in the annexes of the ESMS on excluded activities and classification, including an information collection form (Annex 1) and a categorization checklist (Annex 2), as well the government of Costa Rica's classification lists (Annex 2-ii). The ESMS also provides information on when an EIA is required and what this is expected to

include. Finally the ESMS provides guidance and a checklist for environmental evaluation and monitoring based on environmental categorization (Annex III). See below for more details:

ESMS Content Summary

Main Document	Environmental Policy and Procedure for the Analysis of Environmental Risk	Sets out scope and procedure to be followed for all operations financed by Improsa.
Annex 1	Information requirement for environmental evaluation	Provides a basic checklist for an investment officer to collect information on the loan, size and location, relevant co-financiers, relevant governmental authorities and permits.
Annex 2	Environmental categorization	This guides the credit analyst through a series of checks to confirm that the project is compatible with Improsa's list of excluded activities, and then determine the level of environmental and social risk and impact associated with the investment. At the conclusion of this exercise the analyst must confirm the categorization of the investment and determine if this must be consulted with any additional parties (ie source of funds such as MFIs). Part II of this Annex contains additional guidance in the form of a list produced by the Costa Rican Ministerio de Salud, which effectively provides categorization by sector.
Annex 3	Environmental Evaluation and Monitoring	This guides the credit analyst through the environmental evaluation phase, essentially setting out what is required based on the category assigned to the operation. For example Category A operations, must have an EIA the analyst is required to check whether this EIA includes a number of items such as legal framework; detailed project description, environmental and social baseline; impacts; alternatives analysis; a mitigation plan; consultation. A list of permits and documents required by law is set out that must be checked (yes, no, or not required). Similar detailed checklists are provided for Category B and FI operations.

4.3 Overall responsibility for the implementation of the ESMS is with Credit Risk (operational function) and the Risk Unit (control function). One officer has overall day to day responsibility for the implementation of the ESMS, and received training on environmental risk management in 2005. Credit and risk officials have received internal training on the ESMS and its application. Oversight on the application of all policies and procedures, including the ESMS is the responsibility of Management.

4.4 The strength of the system is that it is set out in a way in which it is easy for a non-environmental officer to follow, and to be able to undertake relatively detailed analysis using the series of check lists. The inclusion of checklists for onlending to FIs is also considerably advanced. Oversight. One weakness is the ESMS's instruction and detail on monitoring and follow up, for which it is recommended Improsa review and enhance during the next twelve months.

- 4.5 Improsa reports on the environmental and social aspects annually to fulfill requirements it has for loans with FMO, DEG and IFC. These reports include detailed breakdown of the use of funding for each by environmental category.

V. Environmental and Social Safeguard Requirements

- 5.1 The Bank will require as part of the Loan Agreement that Improsa:
- (i) comply with all applicable Costa Rican environmental, social, health and safety, and labor regulatory requirements, IDB List of Excluded Activities for Non-Sovereign-Guaranteed (NSG) operations, the Fundamental Principles of the Rights at Work.
 - (ii) apply its Environmental and Social Management System (ESMS) to IDB use of proceeds.
 - (iii) include reference to IDB, as a source of financing, in the same way in which other MFIs providing financing are referenced throughout the documents, at such time when Improsa updates its ESMS, ideally during the next twelve months.
 - (iv) Ensure that at least one staff member with responsibility for the ESMS implementation and maintenance take part in the IIC/IDB Environmental Risk Management training course, or a similar workshop by other organizations such as UNEP-FI, to be agreed upon by the IDB, to ensure that Improsa continue to remain up to date with its environmental and social risk management expertise.
- 5.2 The IDB will supervise the environmental and social aspects of the Loan Agreement either by an in-house specialist or with external consultants, and require Improsa to present environmental and social compliance reports in form, content and frequency satisfactory to the IDB.