

TC Document

I. Basic Information for TC

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| ▪ Country/Region: | HONDURAS |
| ▪ TC Name: | Increased investment mobilization for green and resilient recovery with Micro, Small and Medium Enterprises (MSMEs) in Honduras |
| ▪ TC Number: | HO-T1395 |
| ▪ Team Leader/Members: | Schneider Talavera, Christian (IFD/CMF) Team Leader; Villacorta Alvarez, Omar (IFD/CMF) Alternate Team Leader; Alatorre Frenk, Claudio (CSD/CCS); Amaro Andrade, Flor Evelyn (IFD/CMF); Bejar Granda, Diana Mirella (IFD/CMF); Bernedo, Cecilia (IFD/CMF); Frisari, Giovanni Leo (CSD/CCS); Garcia Recinos, Lynda Melissa (IFD/CMF); Landazuri-Levey, Maria C. (LEG/SGO); Marquez, Claudia (IFD/CMF); Messere, Vanina Soledad (IFD/CMF); Netto De A. C. Schneider, Maria E. (IFD/CMF); Vasa, Alexander (IFD/CMF) |
| ▪ Taxonomy: | Client Support |
| ▪ Operation Supported by the TC: | . |
| ▪ Date of TC Abstract authorization: | . |
| ▪ Beneficiary: | Honduras Finance Secretariat (<i>Secretaría de Finanzas de Honduras, SEFIN</i>); Economic Development Secretariat (<i>Secretaría de Desarrollo Económico</i>); Central Bank of Honduras (<i>Banco Central de Honduras, BCH</i>); Honduran Bank for Production and Housing (<i>Banco Hondureño de la Producción y la Vivienda BANHPROVI</i>). |
| ▪ Executing Agency and contact name: | Inter-American Development Bank |
| ▪ Donors providing funding: | Strategic Climate Fund(SCX) |
| ▪ IDB Funding Requested: | US\$750,000.00 |
| ▪ Local counterpart funding, if any: | US\$0 |
| ▪ Disbursement period (which includes Execution period): | 24 months |
| ▪ Required start date: | September 2021 |
| ▪ Types of consultants: | Individuals and firms |
| ▪ Prepared by Unit: | IFD/CMF-Connectivity Markets and Finance Division |
| ▪ Unit of Disbursement Responsibility: | IFD/IFD-Institutions for Development Sector |
| ▪ TC included in Country Strategy (y/n): | n |
| ▪ TC included in CPD (y/n): | n |
| ▪ Alignment to the Update to the Institutional Strategy 2010-2020: | Productivity and innovation; Climate change; Environmental sustainability |

II. Objectives and Justification of the TC

- 2.1 Micro, Small and Medium Enterprises (MSMEs) in Honduras are essential to the country's productive structure and labor market. There were 14,317 MSMEs registered in 2017, employing an estimated 70% of the country's workers. Of this total number of MSMEs, 96% are classified as microenterprises (1-10 employees), 3% as small

businesses (11-50 employees) and 1% as medium-sized businesses.¹ However, Honduran MSMEs have a history of restricted access to financing even prior to the COVID-19 pandemic, with a finance gap estimated at 37% according to a 2018 study by the SME Finance Forum.² This limited access to financing is confirmed by data from the National Banking and Insurance Commission (CNBS) showing that only 19% of the financial system loans to the business sector went to MSMEs in 2019.³

- 2.2 Despite limited data availability, it is estimated that 35% of MSMEs in Honduras are owned by women, most of which are microenterprises (83%). Moreover, estimates show that at least 23% of women's enterprises in the formal sector face some kind of constraint on access to financing.⁴
- 2.3 As a result of the COVID 19 pandemic, MSMEs were confronted with multiple challenges regarding access to financing and this was exacerbated by the global economic contraction which has led to a reduction and a higher uncertainty of global demand. A strong decrease in external demand coming from Honduras's main trade partners, namely the United States and the European Union impacted the supply chains of primary products exported by Honduras as well as the country's industrial sector.⁵ As MSMEs' revenue decreased and temporary closures increased, the perceptions of the MSME's credit risk worsened, leading to a further decrease in credit supply and to the intensification of the financial system's preference for maintaining liquidity rather than lending to MSME clients confronting economic difficulties.⁶
- 2.4 The Government of Honduras focused its efforts on protecting the country's productive fabric, including the following measures: (i) the freezing of credit history from February 28th 2020 to October 2020, (ii) the establishment of a US\$ 100 million guarantee fund managed by BANHPROVI (trustee) for loans to MSMEs with resources from a Central American Bank for Economic Integration (CABEI) loan approved on April 25th 2020 (the fund guarantees 65% to 90% of loans to MSMEs), and (iii) the allocation of US\$225 million for a credit line by BANHPROVI to provide loans to MSMEs, with support from a CABEI credit line approved on May 8th 2020. During the first term of 2021, BANHPROVI issued a total of 3,314 guarantees, mobilizing over US\$40 million, covering almost US\$30 million (average guarantee coverage of 73%) and financed USD100 million in credits to support the country's economic recovery through loans to productive sectors, including housing and agriculture.
- 2.5 Looking forward, the SEFIN and the Economic Development Secretariat, as decision-making bodies responsible for the financing and support of the productive sector,

¹ M. Dini y G. Stumpo (coords.), "Mipymes en América Latina: un frágil desempeño y nuevos desafíos para las políticas de fomento. Síntesis", Documentos de Proyectos (LC/TS.2019/20), Santiago, Comisión Económica para América Latina y el Caribe (CEPAL), 2019.

² IFC (International Finance Corporation). (2018). MSME FINANCE GAP: Assessment of the Shortfalls and Opportunities in Financing Micro, Small and Medium Enterprises in Emerging Markets. IFC, Washington, DC.

³ Comisión Nacional de Bancos y Seguros. (2020). Presentación de Datos de Cartera MIPYME del Sistema Financiero. Tegucigalpa, marzo 30, 2020.

⁴ IDB (2020). "Global Credit Program for Safeguarding the Productive Fabric and Employment (HO-L1216) – Loan Proposal"

⁵ IADB (2021). "Program to Finance the Industrial Development of Honduras (HO-L1217) – Project Profile"

⁶ Klein. 2014. "Small and Medium Size Enterprises, Credit Supply Shocks, and Economic Recovery in Europe", WP/14/98, Fondo Monetario Internacional (FMI), 2014.

together with the institutions supporting the channeling of financing to MSMEs such as the Central Bank of Honduras, BANHPROVI and other fiduciary structures⁷ are expected to play an important role in the economic recovery of Honduras. This provides the opportunity to make these efforts climate smart by mobilizing and redirecting financial resources towards low carbon and climate resilient activities. Supporting the productive development of the country through greening MSMEs has the potential to make the country more competitive as global value chains adapt to a new context. Furthermore, previous experience in Honduras managing trust funds allows for a flexible structure to further channel sub-loans and guarantees to intermediary financial institutions as well as to channel technical assistance to beneficiary businesses to implement and prioritize green investment pathways.

- 2.6 **Objective.** The objective of this TC is to support the Ministry of Finance in Honduras (SEFIN) and the Economic Development Secretariat on the institutional and technical strengthening of the public entities that channel financing to MSMEs, namely the Central Bank of Honduras, BANHPROVI and other fiduciary structures, as well as the provision of analytics and tools to identify green finance opportunities for MSMEs that can directly contribute to a climate-smart recovery of Honduras. This will allow an increase in their ability to identify, exploit and monitor the opportunities for climate finance with MSMEs and, hence, support the efforts of the IDB in increasing the level of climate finance with financial intermediaries dedicated to the productive sector and MSMEs in Honduras.
- 2.7 The country's economy focuses on exporting simple textiles, which represented 42.2% of total exports in 2018, as well as exporting primary goods namely coffee, bananas and other fruits, which represented 18.5% of total exports in 2018.⁸ The textile industry generates an estimated of 15,000 direct jobs and almost 100,000 indirect jobs. As of the agro-industrial sector, it generates 27,000 direct jobs and 320,000 indirect jobs.⁹ Moreover, there are other sectors that have been identified by their high potential to generate revenue and employments such as tourism, business services, car parts manufacturing and electrical equipment manufacturing.¹⁰
- 2.8 The greening of Micro, Small and Medium Enterprises' will provide additional benefits such as diversified livelihoods, increased employment, and improved health (e.g., air quality). Furthermore, the bank continues its commitment to closing gender gaps, incorporating a gender lens in the monitoring of the project's outputs and facilitating the compilation of gender-related data and its analysis. The project will result in at-scale direct investments and market transformation to reduce GHG and positively impact people's lives via increased resilience to climate change. The pandemic's massive economic and social costs have demonstrated the importance of protecting natural ecosystems and strengthening crisis preparedness in order to minimize catastrophic outcomes from shocks. Building on lessons emerging from the COVID-19 response, IDB can boost climate resilience, for instance through community and nature-based solutions which can rapidly create large numbers of jobs, especially through MSMEs.

⁷ The IADB is engaging in discussions with the Government of Honduras regarding the creation of a Public Trust Fund to support post-COVID economic recovery.

⁸ For further information, see the [Honduras Complexity Index](#)

⁹ FAO database (2019)

¹⁰ IADB (2021). "Program to Finance the Industrial Development of Honduras (HO-L1217) – Project Profile"

- 2.9 **Justification.** The project seeks to address two identified barriers, given the scope of the Strategic Climate Fund (SCX). First, there is limited identification and knowledge of green and resilient opportunities for MSMEs. This barrier limits a more targeted program by institutions supporting the provision of funding to the productive sectors or other fiduciary structures that account for green and resilient recovery investments by MSMEs. These entities will benefit from support to provide improved and more targeted banking products and services for improved recovery by MSMEs. This barrier will be addressed by the activities outlined under Component 1. The second barrier that will be addressed is the limited technical and institutional capacity to identify and follow up on green and resilient opportunities for MSMEs, as well to manage climate related risks in their MSMEs financing. This barrier also influences the identification, design and implementation of green and resilient investment opportunities for MSMEs. This second barrier will be addressed by Component 2 on capacity building and knowledge sharing, combining the use of available tools and instruments, with dialogues between financial institutions, regulators, and the productive sector. Hence, the TC proposal is completely aligned with the SCX selection criteria under its Climate Investment Fund (CIF) Technical Assistance Facility (TAF).
- 2.10 Also, the proposal aligns with the priorities of the Honduran Government in the context of COVID-19 recovery. In a moment of restricted access to credit by MSMEs, the SEFIN, the Economic Development Secretariat, together with the support of the Central Bank of Honduras, BAHNPROVI and other entities such as Public Trust Funds, are key partners supporting the Government's efforts to protect the productive sector, particularly MSMEs, by channeling resources to support COVID-19 recovery efforts.
- 2.11 The provision of analytics and tools will help operations with a focus on MSMEs under implementation and/or implementation to identify green finance opportunities for MSMEs. The project will help the beneficiary entities to prepare a pipeline of climate-resilient projects aligned with commonly accepted taxonomies and standards,¹¹ which can contribute to the prioritization of investments projects that match the country's climate priorities. This presents a systematic approach to identify MSMEs that produce technologies, products, and services that support adaptation and mitigation to climate change but that also enables investors and governments to target investment and support. The project will inform the Central Bank, BANHPROVI and other fiduciary structures on how their solutions may support green and resilience investment but also potentially crowd in private capital for MSMEs and associated projects. The project will seek to replicate the IADB's Financial Innovation LABs approach (public-private dialogue among local financial market players) to foster a participatory process to developed well targeted investment solutions for MSMEs.
- 2.12 IDB will take advantage of synergies and complementarities to existing projects in Honduras and will ensure additionality by expanding the scope towards green and resilient recovery investments and the number of sectors targeted by current or in preparation operations. Furthermore, the findings of the project will lay out strategic work streams for the design of future operations by providing analytical inputs on how

¹¹ Including the Joint Report on MDBs Climate Finance.

to make these operations consider low-carbon and climate resilient technological and financial solutions.

- 2.13 There is a loan operation approved in 2020 ([HO-L1216](#)) structured to provide liquidity support to MSMEs in the face of COVID-19 short-term financial capacity through BANHPROVI for food value chains and the tourism sector. Furthermore, a technical cooperation ([HO-T1359](#)) is currently supporting the Ministry of Finance (SEFIN) to improve its technical capacity in response to the health and economic crisis of COVID-19 pandemic.
- 2.14 **IDB strategic alignment.** This TC is consistent with the Second Update to the Institutional Strategy (AB-3190-2) and is aligned with the development challenge of Productivity and Innovation, as it is aimed at supporting the adoption of sustainable accountability mechanisms and the alignment of green financial instruments. The TC is also aligned with the cross-cutting theme of: (i) Institutional Capacity and Rule of Law, as it regards enhanced transparency and aims to enhance the capacity of National Development Banks (NDBs) and public sector agencies; and (ii) Climate Change and Environmental Sustainability, as it supports the design of sustainable transparency instruments that facilitate investments in productive and environmentally sustainable activities, and the mobilization of capital to support effective public-private synergies that contribute to the achievement of countries' Nationally Determined Contributions (NDCs). The TC is aligned with IDB Group Country Strategy with Honduras 2019 – 2022 particularly with the priority area of “Expansion of sustainable production opportunities” through the promotion of green lines of financing to SME and also with the crosscutting theme of climate change adaptation given that promotes interventions aimed at supporting production activities, including appropriate designs for resilient infrastructure and lines of credit to improve adaptation among producers, and management of key natural resources for the agriculture, tourism, and energy sectors. Additionally, this TC is also aligned with the cross-cutting topic of Gender and Diversity, as the gender perspective will be considered in the implementation.
- 2.15 **Lessons learned.** This TC will draw from lessons from the development of the joint MDB methodology for climate project tagging and benchmarks from financial institutions. Furthermore, this TC will draw lessons from other regional TCs ([ATN/CF-15571-RG](#), [ATN/FI-17637-RG](#), [ATN/FI-14376-RG](#), [ATN/FI-13401-RG](#), [ATN/OC-13944-RG](#) and [RG-T3885](#)) regarding capacity building support to NDBs. [ATN/CF-15571-RG](#) and [ATN/FI-17637-RG](#) have also provided technical assistance regarding knowledge sharing (<http://greenfinance.org>), which this TC will use to share the knowledge products and information developed. Other lessons that can be used are the creation of dedicated spaces for stakeholders to exchange experiences and identify ways to implement innovative sustainable instruments; regional workshops with relevant stakeholders and the institution of round tables to work with other stakeholders and relevant national and regional partners.

III. Description of activities/components and budget

- 3.1 The project will support the identification of low-carbon and climate resilient potential in MSME lending and mainstream green finance in the portfolio of core banking products and services. The technical assistance will support both lending and non-lending operations, according to institutional needs. The initiative will focus on MSME's institutional and corporate profile, implementing risk management

instruments to identify climate related risks and opportunities consistent (according to specific circumstances) with the TCFD framework, Paris Alignment methodology and the MDB joint methodology to mainstream climate change. This work would allow to increase the volume of green finance of the institution, to inform regulatory and taxonomy discussions as well as the execution of climate-related performance indicators. Specifically, the TC will finance consultancy services focused in the following two components:

3.2 **Component 1. Identification of green and resilient COVID-19 recovery opportunities for MSMEs.**

This component will support the identification of green finance products and operations targeted for MSMEs. Particularly, this component will support the Central Bank of Honduras, BANHPROVI or other fiduciary structures (e.g., a Public Trust Fund) to:

- Review market tendencies and existing financing portfolios to identify green and resilient investment opportunities for MSMEs in selected sectors. This analysis will consider a gender perspective as part of its inputs to understand the gender barriers and needs for MSMEs.
- Analyze green and resilient technologies and their availability for MSMEs financing through the banking channels. This work will develop analytical work using tools and methodologies that better account for green and climate-resilient investments.
- Design new financial products for MSMEs, including risk sharing facilities and specialized products with a focus on BANHPROVI's sustainable housing and agriculture portfolio. These financial products are expected to be tested (pilot) and evaluated in order to be scaled up or improve existing ones.
- Financial structuring of a pilot of financial products for MSMEs for increased investment mobilization for a green and climate-resilient recovery. This will have local and inclusive considerations through a proactive gender sensitive consultation process with key stakeholders, including other local financial institutions, MSMEs organizations, and other relevant stakeholders in each country. To ensure the inclusion of gender considerations, the project will have focus groups to understand and address gender needs and barriers; in promoting some of these initiatives to MSMEs, and the project will implement good practices for gender sensitive communications.
- Update monitoring and evaluation instruments to measure the effectiveness and impact of innovative sustainable financial products, including the proposed pilot, by developing new approaches to understand climate impacts.
- Support the development of a green and resilient project pipeline.

3.3 **Component 2. Technical and institutional capacity building.**

This output aims at building technical and institutional capacities of the Central Bank, BANHPROVI or other fiduciary structures, including undertaking modelling work of their MSMEs client portfolio. These capacity building and knowledge sharing activities will provide equitable access for men and women. This includes:

- Support in the use of analytical tools to review and identify investment opportunities for green and resilient recovery in MSMEs, to assess their alignment

with low carbon and climate resilient development pathways, and to properly manage climate related financial risks. The project will account for gender considerations using already approved gender sensitive training for public banks developed by the IDB Group.

- Design of a corporate strategy strengthening plan for BANHPROVI to incorporate best practices related to sustainable finance and develop an updated business plan that aligns with the revised strategy.
- Strengthen the capacity of financial intermediaries accessing second-tier financial products, including the strengthening of their environmental and social management systems.
- Assessment of BANHPROVI's MSME Recovery Guarantee Fund (Fondo de Garantías para la Reactivación de las MIPYMES), including proposals to strengthen its risk management system, pricing model and guarantee business model in order to play a greater role in mobilizing financing for MSMEs.
- Knowledge sharing, including country and regional-level exchanges to share lessons learnt from designing and/or implementing green and resilient recovery initiatives with NDBs and MSMEs. This will include: (i) national events (virtual or in-presence); y (ii) regional virtual events.
- Targeted capacity building activities to improve institutional capacity on gender equality, including gender-responsive HR policies, supporting women staffs' retention and career development, among others.

Indicative Budget

The proposed technical assistance budget is USD750,000, divided among the two components as shown in the following table. Most resources will go to the identification of green and resilient opportunities for MSMEs (USD455,000), with the rest of the budget going to technical and institutional capacity building activities (USD295,000).

| Activity/ Component | Description | IDB/Fund Funding (SCX) | Total Funding |
|------------------------|--|---------------------------|---------------|
| 1 | Identification of green and resilient COVID-19 recovery opportunities for MSMEs. | 455,000 | 455,000 |
| | Consultancy 1: Diagnostic to review market trends | 205,000 | 205,000 |
| | Consultancy 2: Design of new financial products for SMEs | 100,000 | 100,000 |
| | Consultancy 3: Monitoring and evaluation instruments | 100,000 | 100,000 |
| | Consultancy 4: Support for the development of a green and resilient project pipeline | 50,000 | 50,000 |
| 2 | Technical and institutional capacity building | 295,000 | 295,000 |
| | Consultancy 5: Support the use of analytical tools. | 57,500 | 57,500 |

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|--------------|---|----------------|----------------|
| | Consultancy 6: Design of green and gender oriented corporate strategy | 90,000 | 90,000 |
| | Consultancy 7: Assessment of BANHPROVI's MSME Recovery Guarantee Fund | 50,000 | 50,000 |
| | Consultancy 8: Knowledge sharing/capacity building activities | 7,500 | 97,500 |
| TOTAL | | 750,000 | 750,000 |

IV. Executing agency and execution structure

- 4.1 The IDB will execute the technical assistance given the complexity of the thematic that is still incipient in the country and requires coordination among many counterparts to guarantee the right appropriation and sustainability beyond the CT (Secretaria de Finanzas, Banhprovi, Secretaria de Desarrollo and others). In addition, IDB has extensive experience, lessons learned and the need to align the methodologies to be applied in other countries of the region with the support of other regional TCs. The administrative and technical supervision of the proposed technical assistance program will be under the responsibility of Connectivity Markets and Finance Division (IFD/CMF) with support from Climate Change and Sustainability (CSD/CCS). The activities will be carried out in close coordination with the beneficiaries¹² and the focal points in the corresponding Bank's Country Office (COF) who will have a key role in the national dialogue.
- 4.2 IFD/CMF has ample experience and proving record of successfully executing regional TCs to support NDBs. The Bank is considered to have the adequate systems to guarantee the proper execution of the operation and ensure the sustainability of the implementation of the project in line with the "Operational Guidelines for Technical Cooperation Products" (GN-2629-1). Likewise, the TC team has the necessary experience to ensure compliance with the relevant procurement policies and procedures.
- 4.3 To ensure a proper execution of the proposed program, the project team will organize launching, midterm and final review meetings/conferences with the beneficiaries and their consultants for each of the phases contemplated in the design and implementation of their respective systems. The project team will also fulfill all the annual and periodical monitoring requirements established by the Bank, under current policies and procedures for this type of operations.
- 4.4 A reflexive impact evaluation of the program will be conducted by the project team before the end of the disbursement period to assess whether the impact indicator of the program was achieved.
- 4.5 All acquisitions will be carried out in accordance with the Bank's policies and procedures: (i) AM-650 for individual consultants; (ii) GN-2765-4 and Guidelines OP-

12 Honduras Finance Secretariat (Secretaría de Finanzas de Honduras, SEFIN); Economic Development Secretariat (Secretaría de Desarrollo Económico); Central Bank of Honduras (Banco Central de Honduras, BCH); Honduran Bank for Production and Housing (Banco Hondureño de la Producción y la Vivienda, BANHPROVI).

1155-4 for consulting firms providing services of an intellectual nature; and (iii) GN-2303-28 for logistics and other related services.

V. Major issues

- 5.1 A possible implementation risk of this TC is the lack of appropriate engagement of the counterpart, providing full access and participation of their personnel into the TC activities well as of their commitment toward the sustainable recovery post COVID 19 and the election process taking place at the end of November 2021. This will be mitigated by securing, prior to the TC begins implementation, of proper buy-in of activities at the management level, so there is a clear mandate within participating institutions to conduct the proposed activities.

VI. Exceptions to Bank policy

- 6.1 There are no exemptions to the Bank policies present in this TC.

VII. Environmental and Social Strategy

- 7.1 This Technical Cooperation is not intended to finance pre-feasibility or feasibility studies of specific investment projects or environmental and social studies associated with them; therefore, this TC does not have applicable requirements of the Banks Environmental and Social Policy Framework (ESPF).

Required Annexes:

[Results Matrix - HO-T1395](#)

[Terms of Reference - HO-T1395](#)

[Procurement Plan - HO-T1395](#)