

Environmental and Social Management Report
ES-L1094 Banco Davivienda MSME Financing Partnership

I. Project Description and Background

- 1.1 The proposed project will support Banco Davivienda Salvadoreño, S.A. ("DAV") to increase its MSME lending activities in El Salvador. The financing is part of the weB initiative and has a particular focus on supporting women-led MSMEs. To reach this objective, IDB will partner with DAV through its already established Diversified Payment Rights Program ("DPR Program") to provide DAV with a loan of up to US\$60 million with a tenor of up to 7-years and a grace period of up to 2-years.

II. Project Status and Compliance

- 2.1 Based on Directive B.13 of the Environment and Safeguards Compliance Policy (OP-703), this Project is classified as a financial intermediary and as such is not categorized according to its potential environment and social (E&S) impacts and risks.
- 2.2 DAV has confirmed that it is in compliance with Directive B.2 (country laws and regulations) of IDB Environmental and Safeguards Compliance Policy, complying with all applicable legal and regulatory environmental, social, health and safety, and labor (ESHS&L) laws and regulations.
- 2.3 DAV has an environmental and social management system (ESMS) in place, which applies to transactions above US\$1,000,000. DAV's financing limit will be up to US\$500,000. Its dominant portfolio concentration is in commerce, services, and manufacturing and the average sub-loans is US\$10,000 for micro, US\$43,000 for small, and US\$200,000 for medium. Lending to certain sectors in its portfolio such as manufacturing, construction, and agriculture may present moderate and higher risk. Based on management capacity and portfolio composition, this operation is classified as medium risk (FI-2).

III. Environmental and Social Risks and Impacts

A. Potential risks and impacts associated with DAV's portfolio

- 3.1 Within its MSME portfolio, DAV has the following sector concentrations as of March 2015: Commerce (47%), Manufacturing (27%), Services (15%), Financial Services (5%), Transport (4%), Construction (1%), Agriculture (0.2%), and others (0.8%).
- 3.2 The ESHS impacts and risks associated with loans to MSMEs in DAV's portfolio are likely to be low to moderate. Any likely significant environmental and social impacts would relate to lending in manufacturing, construction and agriculture. The ESHS risks and impacts could include, for example: i) habitat conversion and degradation (agriculture, livestock); ii) poor land use/contaminated land (manufacturing, agriculture, construction), iii) stress/contamination of water resources (agriculture, construction), iv) inadequate waste management and disposal (agriculture, manufacturing), v) use of migratory or informal labor (agriculture), vi) transport, traffic noise and dust management and natural disaster risks (construction).

IV. Environmental and Social Management

A. DAV's Environmental and Social Management System (ESMS)

- 4.1 DAV has an Environmental and Social Management System (ESMS) in place, which applies to transactions above US\$1,000,000 therefore, will not be applicable for the subprojects of this line. The ESMS was designed to comply with domestic environmental and labor regulations; the Equator Principles, which have been followed voluntarily since 2008; and the IFC's Performance Standards, which DAV began applying in 2014. In addition, DAV has an environmental officer in charge of conducting environmental reviews of the institution's lending operations and managing the system.
- 4.2 The bank's ESMS includes a list of excluded activities for funding, an environmental categorization of lending operations that takes into account sensitive sectors, the drafting of environmental management / performance reports, and monitoring of environmental compliance of the operations in the institution's portfolio. Since it began operating as a Davivienda subsidiary in El Salvador, the institution has been adjusting some of its procedures to bring them in line with those of Davivienda Colombia.
- 4.3 The requirements below include E&S risk management measures that will be developed and implemented as a condition of this loan through an action plan designed to work with DAV to introduce E&S analysis for IDB's loans below the US\$500,000 limit.

V. Environmental and Social Requirements

- 5.1 For this operation which involves MSME lending up to US\$500,000, the Bank will require DAV as part of the Loan Agreement to:
- (i) Comply with all applicable Salvadorian legal and regulatory requirements, and in relation to the financing of each MSME loan require and obtain satisfactory assurance that all customers/use of proceeds comply with: (a) at a minimum host country environmental, social, health and safety, and labor regulations and standards; (b) DAV's own policies on environmental, social, health and safety and labor matters for sub-loans (b) the IDB List of Excluded Activities for Non-Sovereign-Guaranteed (NSG) operations; and (c) the Fundamental Principles of the Rights at Work;
 - (ii) Apply a Safeguards Filter for lending operations between US\$250,000 – US\$500,000 to be filled by DAV and applicable to Manufacturing, Construction, and Agriculture operations, and any other potentially higher risk on-lending sectors with IDB's proceeds to identify potential environmental and social risks, identify required environmental and social permits, and propose management responses. The development and application of the Safeguard Filter will be required according to an action plan to be agreed between IDB and DAV prior to the first disbursement, to implement it within 6 months of first disbursement.
 - (iii) Implement measures to operationalize points (i) and (ii) above, including: (i) updating its loan documentation or other tools to obtain a representation and commitment, or other satisfactory assurance, that clients, especially those in the higher risk sectors, will comply with local laws and regulations; At a minimum, DAV will provide a representation to the IDB regarding the clients' compliance with local laws and regulations after conducting its own assessment regarding

compliance; (ii) engage with IDB in the ongoing process of reviewing its environmental and social policies to agree on any needed improvements within a time frame to be agreed at around one year from signing; and (iii) assign staff responsibility to screen for environmental and social issues prior to the first disbursement, and ensure that the designated staff member 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.

- (iv) Present an Annual Environmental and Social Compliance Report (ESCR) with information on the MSME portfolio, and any particular risk issues identified during screening, mitigation measures agreed with clients, and compliance status.

VI. Supervision

- 5.2 The IDB will supervise the environmental and social aspects related to the use of the proceeds of the IDB loan either by an in-house specialist or with external consultants, and if necessary, will require measures to address the management of impacts and risks. To this end DAV will provide and facilitate access by IDB to all relevant documentation, personnel and project facilities.