

Environmental and Social Strategy (ESS)¹

Balam Fund I, L.P.

- 1.1 **Overview.** Balam Fund I, L.P. (the “Fund”) will invest in small- to medium-sized environmental infrastructure projects in the renewable energy and energy efficiency sectors in Mexico. These investments are intended to cover the financing gap that the renewable energy and energy efficiency project sponsors face, as highlighted by the Technical Committee of the Mexican National Infrastructure Fund (“Fonadin”). Fonadin expects that significant investments will be required to meet the large demand expected for renewable energy (including solar, wind, geothermal, biomass, hydro, etc.) and energy efficiency (including industries, energy, water, urban transport, buildings and communities, etc.) projects in Mexico.
- 1.2 **General Partner.** Fonadin, managed a selection process for the identification of an entity to sponsor and manage the Fund, resulting in the selection of TRG Management LP (including its affiliates, “TRG”) and BK Renewables Ltd (including its affiliates, “BK”). TRG is an asset management firm focused on investing in emerging markets. BK is an investment advisory and private equity group currently focused on the sectors of land development, building materials, renewable energy and finance. Balam Fund I GP, L.P., was formed by TRG and BK to serve as general partner of the Fund (“General Partner”). TRG will serve as the manager of the Fund, and will have a sub-advisory agreement with BK.
- 1.3 The objective of the Fund is to make investments in small- to medium-sized projects in the renewable energy and energy efficiency investment market in Mexico through the acquisition of equity as well as senior or subordinated debt. The Fund will seek to invest both in new projects (greenfield) and in operating projects (brownfield) in those sectors. The Fund expects to invest in technologies with a proven track record. The Inter-American Development Bank’s (“IDB”) participation in the Fund will increase the Fund’s investment capacity.
- 1.4 The investment strategy of the Fund is to seek to achieve capital appreciation through the acquisition of private equity, equity-like securities such as mezzanine debt and other debt (such as preferred or subordinated) in small- to medium-sized private projects and companies which tend to be less sought after by large

¹ This ESS will be made available to the public in accordance with the IDB’s policy on information disclosure. The ESS does not represent either the IDB’s approval of the Fund or verification of the ESS completeness or accuracy. The IDB, as part of its due-diligence on the feasibility of the Fund, will assess the environmental and social aspects. This assessment will be presented in the Project Environmental and Social Management Report that will be prepared by IDB Bank, and will be made available to public prior to consideration of the Fund by the IDB’s Board of Executive Directors.

traditional developers and/or utilities. The projects will be located in Mexico, and will comply (in all material respects) with all applicable laws and regulations, consistent with IDB policies. The Fund is expected to seek a maximum of US\$ 200 million in capital commitments (including the loan from the IDB) and expects that its renewable energy investments will contribute to the reduction of carbon dioxide (CO₂) emissions. The Fund expects to invest in 15 to 20 projects and, in terms of diversification, by the end of the investment period, the Fund will not invest more than 20% in a single investment and 40% in a single technology platform or solution.

- 1.5 The Fund is expected to be supported by a public infrastructure fund, development banks and private investors, with total capital commitments expected to be sought of approximately US\$200 million. Included in such amount is the proposed US\$50 million senior loan from the IDB, as well as capital commitments by TRG and BK in an aggregate amount of US\$ 10 million.
- 1.6 **IDB Environmental Impact Category.** Based on Directive B.13 of the Environment and Safeguards Compliance Policy (OP-703), the Fund is classified as a Flexible Lending Instrument (financial intermediary) and as such this operation is not categorized according to its potential environmental and social impacts and risks. However, given that the Fund's target investments will likely include some renewable energy infrastructure developments (including small- to medium-sized hydro and wind power generation projects), it is expected that some of the individual transactions (i.e. Fund-financed projects) could fall into categories A and B under the IDB's environmental and social impact classification system.
- 1.7 **Environmental, Social, Health and Safety and Labor Impacts and Risks.** The Fund will finance renewable energy infrastructure and energy efficiency sectors, projects that have not yet been identified and thus, its potential environmental and social impacts cannot be assessed ex-ante. Fund investments, particularly green-field projects, may have moderate to potentially significant environmental, social, health and safety and labor impacts and risks (direct, indirect and cumulative) that will have to be identified, analyzed and managed on a project-by-project basis. The specific environmental and social impacts and risks will be those related to or caused by each specific project investment. These impacts will be diverse and their significance will depend on the project characteristics, such as size, sector, and location. Potential impacts and risks may include aspects of pollution and contamination from the construction and operation of infrastructure as well as risks related to the insertion of the projects in certain specific contexts, including resettlement, impacts on indigenous peoples, impacts on natural habitats and other social and environmental impacts that could trigger other Bank safeguard policies

such as the Involuntary Resettlement Policy (OP-710); the Indigenous Peoples Policy (OP-765) and the Information Disclosure Policy (OP-102). In addition, there could be other issues commonly associated with the construction of renewable energy infrastructure projects such as labor management aspects, workers' health and safety. Some projects to be supported by the Fund are likely to require public disclosure and consultation activities in accordance with both OP-703.

- 1.8 **Management of Environmental and Social Aspects.** As with other funds financed by the IDB, staff within the General Partner have the ultimate responsibility for screening, assessing and managing the environmental and social aspects in a manner that is consistent with the IDB's environmental and social policies, specifically by implementing an appropriate Environmental and Social Management System ("ESMS"). The ESMS should have key elements such as: screening of subprojects against exclusion criteria, impact categorization of proposed subprojects, undertaking of due diligence and monitoring procedures commensurate with the levels of impacts, the structuring of subprojects so that they meet environmental requirements, and where necessary require corrective actions. As with other IDB funds, the IDB will monitor the implementation of the ESMS closely.
- 1.9 **Strategy for Environmental and Social Due Diligence.** The environmental and social due diligence ("ESDD") will focus on agreeing the key elements of the ESMS with the General Partner as well as the fundamental operational aspects of the ESMS in relation to high risk operations, such as early communication to IDB on a possibility of financing a potential high risk projects to enable the IDB to identify the need of complementary analysis, the need for the IDB to provide non-objection to high risk operations, ensuring the implementation and legal availability of measures and mechanisms to address any non-compliance with IDB policies or unmitigated environmental and social impacts or risks during the execution of relevant Fund investments.
- 1.10 As part of the ESDD, the IDB will conduct the following activities (a) a preliminary identification of any particularly sensitive impacts or risks that may be posed by projects expected to be financed by the Fund, including reputation risks; (b) a review of policies and standards to be established by the Fund; (c) the resources the Fund will need to implement the ESMS; (d) contractual and monitoring arrangements between the Fund and the IDB to ensure proper functioning of the ESMS and sustainability of the projects the Fund finances; (e) measures and mechanisms to address any non-compliances with Bank policies or unmitigated environmental and social impacts or risks during the execution of Fund-approved projects; and (f) compliance with the Fundamental Principles and

Rights at Work and with any other relevant international labor organization conventions and treaties which have been ratified by in the countries in which they work.

- 1.11 The IDB and the General Partner will agree on an ESMS for the Fund and any ESG requirement necessary to be applied by the Fund, based on the findings of the ESDD.
- 1.12 The results of the due diligence will be presented in an Environmental and Social Management Report (“ESMR”). This will include a description of the key aspects of the ESMS and related contractual requirements, and the identification of the activities and its timeframe that will need to be conducted as part of the initial phase of implementation of the Fund’s management mechanisms including the ESMS.